

MICROFILM DIVIDER

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SFN 2053 (2/85) 5M



ROLL NUMBER

DESCRIPTION

2268

2007 SENATE INDUSTRY, BUSINESS AND LABOR

SB 2268

2007 SENATE STANDING COMMITTEE MINUTES

Bill/Resolution No. **SB 2268**

Senate Industry, Business and Labor Committee

☐ Check here for Conference Committee

Hearing Date: **January 30, 2007**

Recorder Job Number: **2287**

Committee Clerk Signature

Viatical Settlements: STOLEY

Jim Poolman – Commissioner ND Insurance Dept. - In Favor

TESTIMONY # 1

Went over testimony. Viatical settlements are created to help terminally ill, cancer or aids patients. When we see a policy taken out on another person we see "fraud." There is a secondary role in the marketplace. When it is stranger originated, the investor gets the roll over funds. [6:00m explains]

Bill does prohibit action but gives a narrow window of 5 years to settle the policy. If this is public policy is it a moral hazard? You would need to die sooner to maximize your benefits. Covers Bid Rigging 8:31m] Coventry pays off other companies to not bid on policies. Instead of 3-4-5- bids, who wants to make most money off a policy. Second issue is the net bid on his policy. Broker is presented a gross offer. \$250,000 told, really would be \$500,000 and will cost an extra \$250,000 extra in fees and charges.

There is no property right unless you're an investor. ND is not the first, there are 9-10 states that are introduced. Viatical agreements are adopted by 30 different states.

ND Bankers' Association will have an Amendment.. [ends 13:56m]

S Klein: So this is a "Stranger Originated Policy," what about those relatives who want to plan to provide for their kids upon an death of a parent.

J Poolman: Family interest laws are clear, this is an invisible interest and it will not be affected under this bill.

S Hacker: Does this effect buy-sell insurance in business?

J Poolman: Yes, there is a portion that talks about those specifically exempted. In this bill

S Wanzek: Does this also cover employers who cover employees who are key people like a Manager?

J Poolman: Yes, all are legitimate. CO-LEE is for CO insured and is legitimate.

S Heitkamp: I've read the press release from Spitzer case. Do you have the power to replace the agent and settle?

J Poolman: We have control over Viatical controllers now. This bill makes it clear that we have authority over the viatical settlement company who's committing bid rigging and specifically the broker who makes the transaction.

S Hacker: Bid rigging still is illegal.

J Poolman: this specifically spells it out also to the consumer

Marilyn Foss – ND Bankers Association - In Favor – PROPOSING AMMENDMENT

TESTIMONY # 2 Agree with Jim Poolman, in favor and asking for the bill with amendments.

Went over testimony and amendments. Marilyn visited with Commissioner and agreed on the points in the amendments. [25:20m ends]

Bruce Fergeson – Trade Association – In Favor'

TESTIMONY #3

Talked of Jim Poolman's testimony..

Did look at the amendments prepared by Banker's association and make sense to us.

Add needed clarification. Our goal is to legitimate transactions.

S Klein: This goes from a 2 to a 5 year change.

B Fergeson: Having to wait longer is a deterrent as a type of protection.

S Klein: Why not 8 or 3, why 5?

B Fergeson: The proposal was drawn up for a 5 year waiting period. It would be reviewed on how it would change in the legislature. No magic in it.

S Hacker: The investors are buying multiple policies at a time. Do you have an idea on how the market works, and what sort of return.

B Fergeson: The individual policies are taken out and sold as an investment .

S Hacker: Can those packages be sold in the secondary market or do they have to wait the 2 years or 5 years?

B Fergeson: There are several exceptions to the both the 2 year and 5 year waiting period. Terminal or chronic illness, retirement, divorce, are exceptions to the waiting period.
[explains 32:30m]

S Wanzek: The grace period, is that going from 2 to 5 years? What is the risk for investor? Is there a risk that the insured might die within the 5 years and then the insurance would go to the family.

B Fergeson: 5 years, without insurable interest. It is a risk to investor not getting his hands on the policy. If you're not putting up your own collateral, the 5 year waiting period applies to the sale of the policy for someone without an insurable interest.

S Wanzek: Would it make investors reassess the risk of making the investment and taking a harder look at it. The risk might be higher now.

S Heitkamp: Can't this all be settled by you and how you sell the policy?

B Ferguson: More and more companies are trying to detect these types of transactions that were design to settle. Insurers are asking, "have you been approached by a settlement company, are you getting premium financing from another source?" so that they can detect these type of transactions at the onset.

S Heitkamp: Can't you write rules so you don't get the policy.

B Ferguson: The Insurable Interest law says you must have insurable interest. It can be used as property. It's a different kind of property, it is a contract on someone's life.

S Heitkamp: Like a savings account.

B Ferguson: You can't sell a policy to someone without an insurable interest.
Also, how can we come up with something that legislates intent?

S Hacker: How many transactions took place in the last year, industry wide?

B Ferguson: No, there are no rules to track them.

Terry Weis – ND Association of Insurance and Financial Advisors - In Favor

TESTIMONY # 4 Went over testimony. Not a complicated issue. Support with amendments.

S Wanzek: Sometimes I need to say what I'm thinking. What you're essentially saying that there is potential value and I can see potential value in this type of situations, but there is also potential for abuse. And you're trying to find that balance at that point, we don't want to keep the door wide open.

T Weis: You're correct, we need to pass this to change the bill.

S Behm: "Keep the shysters away from the door."

T Weis: We're not going to say that.

S Hacker: From 2 year to 5 year, it would adjust the price. The legitimate ones, 5 year prior, do you feel the price will drop?

T Weis: I have had corporations have owned policies on some of their share holders and the share holders have sold their stock back to the corporation so therefore they didn't have any interest in that individual anymore, so they've had their life insurance policies. Not a lot of cash value to them, only 4 or 5 years old, they're not old and not going to die quick, so there was no interest in their policies. A 5 year waiting period would be a deterrent to an investment organization looking to wait a long time before they see a return on their investment.

OPPOSITION

Tom Kelsch – Peachtree Settlement Funding - In Opposition

[43:16m] Deals with structured settlements

Jack Kelly – Peachtree Settlement Funding - In Opposition

Is this a solution looking for a problem? Has anyone come up and mentioned this issue to you? People are saying here, "we have an issue we have to deal with." In all honesty, has anyone said, "Senator, you really have to do something about this, I'm really getting ripped off." It's about the rights of ND citizens. It's a right you have to do as you please as an individual, to insure property, and you like to do with it as YOU choose, is your right as an individual. Insurance is used for many different purposes. Now days insurance companies sell insurance for "viance" purposes. Use it as an investment tool. [48:46 examples on life planning]
Explains how there are not issues on this point [49:25m] Do we generally need to have this done? Is this a problem or do we need to find a problem. Unintended thins happen when we rush.

S Hacker: How many did you purchase?

J Kelly: If you're a charity and do Co-Lee , you have to report to treasury. Nobody really knows how many are out there.

S Heitkamp: How many other states are you having to go in and have this debate.

J Kelly: This is the first state.

S Heitkamp: How many other states....

J Kelly: This is the first one that introduced it.

S Klein: Have they adopted any portions of? None? Zero?

J Kelly: That's the key fact that it was only adopted by a committee, because it's contentious and isn't sure it will be adopted by the whole committee, because of fact that Encoil legislators committee said we have an issue, we need to debate this, we need to move this onto our meetings in March and April. Most legislators are saying, let's slow this down, it's not a race and see where it's going.

S Wanzek: I see legitimate value in these tools, may eliminate that tool for our consumers in the state. Trying to find a balance to protect the consumers of abuse and still providing the business. Can you explain the procedure of paying off other bidders. i.e. Bid Rigging

J Kelly [turns red 56:40m]

[gives examples] Bid rigging is not in my interest. If we had bid rigging from another company we would shut it down. We price them right. We like to make better offers than the competition, it is better for the consumer.

S Hacker: If we move from 2 years to 5 years, what effect would that have on consumer?

J Kelly: It will deflate the price as actuary.

Michael Freedman – Life Institute. – In Opposition

TESTIMONY # 5

National Conference of Insurance Legislators did a review of this bill didn't just put it off, it was rejected. According to their rules, it goes too far. It impairs and interferes with life settlements.

Imposes numerous restrictions on life settlements that have NOTHING TO DO WITH INVESTOR-INITIATED LIFE INSURANCE. Goes well beyond the attempt to try to capture the

STOLEY programs. I think it's important they REJECTED it, not just that they weren't going to use it. The problem is the initiation, illegal manufacturing of life insurance. Is lying on the application of a smoker or non-smoker, health conditions or not. The incident at inception of the life insurance policy.

Inducing someone to take out a life insurance policy already illegal.

It already says a stranger cannot initiate that life insurance. The laws in the nation, someone with an insurable interest cannot be used as a dupe for a policy. The law ALREADY says that you can't agree to sell your policy any time within the first 2 years of the policy, so there are at least 3 laws in the general provision of the U.S. law that you can't initiate life insurance through

1. inducement
2. pre-arranged settlement
3. violation of insurable interest laws

The carriers are trying to investigate at inception the same way as if someone were trying to defraud a life insurance company through lying about medical conditions, etc. The problem is the inception.

The average life settlement done in the country today isn't on anyone who has a terminal, chronic illness it is on seniors with a life expectancy of average of almost 10 years which means investors today are estimating they will pay on average more than years of premiums in order to see a realization of their investment. 5 years is an arbitrary number, it doesn't recognize that investors are already paying excess of 5 years of premiums.

It says the consumers can not have the property right established in their life insurance policy, that right to assign which is protected by the Century Code and by Supreme Court of State and U.S. It takes away for 5 years any value other than the value the life insurance establishes for that policy, "cash surrender" value. It punishes consumers and their rights. [continues to

17:30m] Every state that has adopted a law with the exception of Iowa and the NAIC's bill that was passed by the life aid committee, specifically says that if you are a life insurance agent with one year of authority you are able to operate as a settlement broker. This bill carves that out. If you can't get the advice and assistance from your agent on a market to see your policy in an open market and your agent has to go through a separate licensing scheme to become a separate viatical settlement, it deviates from the other states in the country.

S Wanzek: I'm trying to figure a scenario that I could utilized. I farm, when you start you have a lot of debt, take out a lot of debt, have lot of life insurance, when 65, 70, mortgage is paid, the insurance policies are still there, wife and I would like to enjoy retirement years, other than sell land, I could come to you and show my life insurance policies and find out what the value of them to you and negotiate with you or any other viatical settlement company and essentially get a payment and not have to wait until I die. Just for my understanding.

M Freedman: That is a life settlement.

S Hacker: Same question as I did for Jack, on the 2-5 year, what sort of impact would that have on the price you can offer to the consumer?

M Freedman: It eliminates any value, we wouldn't make you an offer.

S Hacker: Based on returns, how will the 2-5 years be affected?

M Freedman: We would be able to make an offer, it would be illegal.

S Hacker: [example 68:26]

[looks at the actuarial process] How will that affect the prices for the people? You need them to pass away at 5.5 or whatever...

M Freedman: We can't have the ownership of the policy, so any performance would be irrelevant until we have an ownership interest.

S Hacker: [uses example] I'm 70 years old and have 3 policies and want to sell one, I talk to you, TODAY you would give me "X" price. Tomorrow this bill is enacted into law, how much of a price reduction would it be that you could offer me?

M Freeman: How old is your policy?

S Hacker: Had it since I was 22.

M Freeman: It wouldn't affect the price at all as it's over 5 years.

CLOSE

2007 SENATE STANDING COMMITTEE MINUTES

Bill/Resolution No. **SB 2268 B**

Senate Industry, Business and Labor Committee

☐ Check here for Conference Committee

Hearing Date: **January 31, 2007**

Recorder Job Number: **2446**

Committee Clerk Signature

Minutes:

S Heitkamp: Pooley sends us an email calling, that you and Encoil (?) in fact didn't do that, which one was it?

S Klein: If they get into a discussion where they don't agree, they just drag it on to the next dinner. There is a small group of ACLI which Bruce Ferguson and does Doug Head who isn't here, who sent Jack and Mike. It got testy, so they put it off until the next meeting. There's probably more in favor of what we're doing in the group than that little life settlement group that wants to repeal those ideas. George is on this one, George is a bigger player than I certainly am, so to me that has brought more credence to the fact that Encoil is biting off on this and we're moving it forward, it's just that meeting 3 times a year in an hour life settlements discussion, they need less time than we do on our viatical bill that we heard yesterday.

S Heitkamp: For them to say Encoil has said, "Absolutely, no possible way,"...

S Klein: That's not true.

S Heitkamp: Ok

S Klein: I was sitting in there that day and I , where did they get that from because that wasn't the message I got.

S Potter: I would really like to know why I'm voting the way I am.

S Klein: I want people to formulate that.

S Behm: I was here and I'm still not sure what they're talking about.

S Hacker: This bill touches a very narrow section of the insurance policy buyers, it doesn't affect them all. They painted with a broad brush that it would affect the whole industry and it would not. It's about the 5 year thing and how they finance that with these people. Most people have had their policies for a few years, and what they're trying to avoid the people who are going out and buying a policy for the sole purpose of selling that policy and so it's not a very large segment; in fact, Peachtree said they only had a couple hundred last year. Michael Freedman is a member of the "Institute." He is an employee of one of the companies, Covenant obviously it was not exciting to tell the committee that. There's a lot of underlying things going on with the bill.

S Potter: I'd like to give the Commissioner one, he's probably right, I just don't know my arguments.

S Wanzek: I thought I had my mind made up, but as I listened to the opposition yesterday, I started to have some doubts and questions about; my concern was I thought they said the minute you transaction that sale to the viatical company, you have to wait 5 years before they can own the policy. That is not the case. [example of farming situation 4:19m]

My concern was that was when I made the transaction I had to wait 5 years and that would lower the value.. now I understand I just need to have owned the policy for 5 years, which I could have sold it and liquidated into cash. Putting a 5 year period on it from a moral issue...

S Klein: It's about the "shysters," Senator Behm hit it on the head.

S Wanzek: It kind of bothers me that somebody you've never done business with before or buy a policy and their only interest is to have you die, I think putting a 5 year period on it may be stop some of the abuse.

S Heitkamp: Move a "Do Pass."

S Klein: We have a **Do Pass** on 2268.

Second by S Hacker

S Klein: I did visit with Mr. Kelsch, asked him, "Do you have anything that would sway anybody with any good information?" He just smiled and said, "It would be over to the House then probably where you'd need the work if there are some issues.."

S Hacker: I have to mention this because it is the core of everything, this is what really tripped me up. In this letter that we got, in the very last paragraph with a situation that was going on in one of the settlements [talks about paragraph in testimony].

S Klein:

We have a DO PASS on SB 2268

Call the Roll: 6-0-1

As you recall we have some punctuational issues that need to be reviewed.

S Heitkamp Send it to the House for that.

2007 SENATE STANDING COMMITTEE MINUTES

Bill/Resolution No. **SB 2268 C**

Senate Industry, Business and Labor Committee

☐ Check here for Conference Committee

Hearing Date: **February 5, 2007**

Recorder Job Number: **2850 Retraction and Revote w/amendments 2851**

Committee Clerk Signature

Minutes:

S Klein: I think we got ahead of ourselves there. On the viatical settlements.

S Wanzek I move that [2850 ends – pick up on 2851] we reconsider as there are amendments that we needed to apply to the bill.

Second by S Hacker all in favor – Aye – Unanimous

Opposed, No [no contest]

S Klein: Even the securities commissioner got a hold of me today and said, "what did you do?"

Those amendments are – We have the ND Bankers Association amendments, we have amendments as proposed by the Insurance Commissioner.

S Heitkamp: So you took out the criteria for the architect and all that? Then I vote yes.

S Klein: Then we have everyone on board. We have suggested to S Erbele to work on it in the House if they can find another way to work it. Two sets of amendments, Bankers Amendments, this was to make sure that the Commissioner's amendments made sure the Securities Commissioner had the regulator authority over the portion that becomes an investment.

S Heitkamp: Do you want a motion on the insurance commissioner's amendment?

S Klein: Yes

S Heitkamp: I'll move.

Second by Hacker

Roll Call for Insurance Commissioner Amendments – 6-0-1 Passed

S Klein: I know the banker's amendments are minimal, with margins and punctuation. Can I have a motion for the banker's amendment?

S Heitkamp: What does the banker's amendment do that the insurance commissioner's don't?

S Klein: I think it's how the bank holds the policy as a security of the loan.

S Heitkamp: I thought it was to clean up the amendment and if we just amended with the insurance commissioner, are the banker's amendments right?

S Klein: I believe they are.

S Wanzek: They're not going to be in conflict in any way are they? They appear they don't conflict. I haven't seen one area where they test it. I just want to make sure we don't have to reconsider our actions again.

Motion by S Wanzek

Second by S Hacker

Vote on Bankers Amendment – 6-0-1 Passed Amendment

S Hacker: Could you send Marilyn a note that she can just say "number accordingly?"

Motion to DO PASS AS AMENDED on SB 2268 - S Wanzek

Second by S Hacker

Vote for DO PASS AS AMENDED – 6-0-1 - Passed

Carrier: S Klein

S Heitkamp: So basically what we did there was just cleaned up language, and the bill just changed Viatical settlements from 2 years to 5 years.

S Klein: Correct

FISCAL NOTE
Requested by Legislative Council
03/26/2007

Amendment to: Engrossed
 SB 2268

1A. State fiscal effect: *Identify the state fiscal effect and the fiscal effect on agency appropriations compared to funding levels and appropriations anticipated under current law.*

	2005-2007 Biennium		2007-2009 Biennium		2009-2011 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues						
Expenditures						
Appropriations						

1B. County, city, and school district fiscal effect: *Identify the fiscal effect on the appropriate political subdivision.*

2005-2007 Biennium			2007-2009 Biennium			2009-2011 Biennium		
Counties	Cities	School Districts	Counties	Cities	School Districts	Counties	Cities	School Districts

2A. Bill and fiscal impact summary: *Provide a brief summary of the measure, including description of the provisions having fiscal impact (limited to 300 characters).*

The amendments to the bill will have an impact of less than \$500.

B. Fiscal impact sections: *Identify and provide a brief description of the sections of the measure which have fiscal impact. Include any assumptions and comments relevant to the analysis.*

See 2A.

3. State fiscal effect detail: *For information shown under state fiscal effect in 1A, please:*

A. Revenues: *Explain the revenue amounts. Provide detail, when appropriate, for each revenue type and fund affected and any amounts included in the executive budget.*

See 2A.

B. Expenditures: *Explain the expenditure amounts. Provide detail, when appropriate, for each agency, line item, and fund affected and the number of FTE positions affected.*

See 2A.

C. Appropriations: *Explain the appropriation amounts. Provide detail, when appropriate, for each agency and fund affected. Explain the relationship between the amounts shown for expenditures and appropriations. Indicate whether the appropriation is also included in the executive budget or relates to a continuing appropriation.*

See 2A.

Name:	Charles E. Johnson	Agency:	Insurance Department
Phone Number:	328-2440	Date Prepared:	03/26/2007

Date: 1-30-07

Roll Call Vote: 1

2007 SENATE STANDING COMMITTEE ROLL CALL VOTES

BILL/RESOLUTION NO. 2268

Senate INDUSTRY BUSINESS & LABOR Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken

DO PASS

Motion Made By

Heitkamp

Seconded By

Hacker

Senators	Yes	No	Senators	Yes	No
Chairman Jerry Klein	✓		Senator Arthur Behm	✓	
Vice Chair Nicholas Hacker	✓		Senator Joel Heitkamp	✓	
Senator John Andrist	NP		Senator Tracy Potter	✓	
Senator Terry Wanzek	✓				

Total Yes 6 No 0

Absent 1

Floor Assignment Klein

If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE (410)
January 31, 2007 3:35 p.m.

Module No: SR-21-1708
Carrier: Klein
Insert LC: . Title: .

REPORT OF STANDING COMMITTEE

SB 2268: Industry, Business and Labor Committee (Sen. Klein, Chairman) recommends
DO PASS (6 YEAS, 0 NAYS, 1 ABSENT AND NOT VOTING). SB 2268 was placed
on the Eleventh order on the calendar.

Date: 2-5-07

Roll Call Vote : 1

2007 SENATE STANDING COMMITTEE ROLL CALL VOTES

BILL/RESOLUTION NO. 2268

Senate INDUSTRY BUSINESS & LABOR Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken Remove - withdrawn.

Motion Made By Wanzek Seconded By Hacker

Senators	Yes	No	Senators	Yes	No
Chairman Klein, Jerry			Senator Behm, Art		
Senator Hacker, Nick, VC			Senator Heitkamp, Joel		
Senator Andrist, John			Senator Potter, Tracy		
Senator Wanzek, Terry					

Total Yes _____ No _____

Absent _____

Floor Assignment _____

If the vote is on an amendment, briefly indicate intent:

Date: 2-5-07

Roll Call Vote: 23

2007 SENATE STANDING COMMITTEE ROLL CALL VOTES

BILL/RESOLUTION NO. 2268

Senate INDUSTRY BUSINESS & LABOR Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken Barriers Amendment

Motion Made By Wanzek Seconded By Hacker

Senators	Yes	No	Senators	Yes	No
Chairman Klein, Jerry	✓		Senator Behm, Art	✓	
Senator Hacker, Nick, VC	✓		Senator Heitkamp, Joel	✓	
Senator Andrist, John	N		Senator Potter, Tracy	✓	
Senator Wanzek, Terry	✓				

Total Yes 6 No 0

Absent 1

Floor Assignment _____

If the vote is on an amendment, briefly indicate intent:

Date: 2-5-07

Roll Call Vote : ~~2~~ 4

2007 SENATE STANDING COMMITTEE ROLL CALL VOTES

BILL/RESOLUTION NO. 2268

Senate INDUSTRY BUSINESS & LABOR Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken DPAA

Motion Made By Wanzek Seconded By Hacker

Senators	Yes	No	Senators	Yes	No
Chairman Klein, Jerry	✓		Senator Behm, Art	✓	
Senator Hacker, Nick, VC	✓		Senator Heitkamp, Joel	✓	
Senator Andrist, John	NP		Senator Potter, Tracy	✓	
Senator Wanzek, Terry	✓				

Total Yes 6 No 0

Absent 1

Floor Assignment Klein (remains)

If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE

SB 2268: Industry, Business and Labor Committee (Sen. Klein, Chairman) recommends AMENDMENTS AS FOLLOWS and when so amended, recommends **DO PASS** (6 YEAS, 0 NAYS, 1 ABSENT AND NOT VOTING). SB 2268 was placed on the Sixth order on the calendar.

Page 1, line 20, remove "purchase or"

Page 2, line 2, remove "or other agreement"

Page 2, line 28, remove the third "viatical"

Page 2, line 29, remove "settlement investment agent,"

Page 3, line 9, remove ", or as a result of a viatical"

Page 3, line 10, remove "settlement purchase agreement"

Page 3, line 12, remove the underscored comma

Page 3, line 13, remove "viatical settlement purchase agreement"

Page 3, line 16, replace the first underscored comma with "or" and remove ", or viatical settlement purchase"

Page 3, line 17, remove "agreement"

Page 3, line 18, remove the underscored comma

Page 3, line 19, remove "viatical settlement purchase agreement"

Page 7, replace lines 1 through 5 with:

"(2) A loan made by a bank or other licensed financial institution in which the lender takes an interest in a life insurance policy solely to secure repayment of the loan or, if there is a default on the loan and the policy is transferred, the further assignment of the policy by the lender, provided that the default itself is not pursuant to an agreement or understanding with any other person for the purpose of evading regulation under this chapter;"

Page 8, line 8, after the underscored period insert "A viatical settlement investment agent is an agent as defined in section 10-04-02."

Page 8, line 19, after the third comma insert "or" and replace ", other" with ";

(2) A"

Page 8, line 20, remove the underscored comma

Page 8, line 24, replace "(2)" with "(3)"

Page 8, line 25, replace "(3)" with "(4)"

Page 8, line 28, replace "(4)" with "(5)"

Page 8, line 31, replace "(5)" with "(6)"

Page 9, line 1, replace "(6)" with "(7)"

Page 9, line 2, replace "(7)" with "(8)"

Page 9, line 3, replace "(8)" with "(9)"

Page 9, line 4, replace "(9)" with "(10)"

Page 9, line 10, after the underscored period insert "A viatical settlement purchase agreement is a viatical settlement contract as defined in section 10-04-02."

Page 10, remove lines 20 through 27

Page 10, line 28, replace "c." with "b."

Page 11, line 3, replace "d." with "c."

Page 11, line 24, replaced the underscored comma with "or"

Page 11, line 25, remove "or viatical settlement investment agents,"

Page 14, line 2, remove "or a viatical settlement purchase"

Page 14, line 3, remove "agreement"

Page 15, line 9, remove "viatical settlement investment agent,"

Page 15, remove lines 17 through 19

Page 15, line 20, replace "c." with "b."

Page 15, line 23, after "desirability" insert an underscored comma and replace "d." with "c."

Page 15, line 25, replace "e." with "d."

Page 15, line 29, replace "f." with "e."

Page 16, line 1, replace "g." with "f."

Page 32, remove lines 22 through 24

Page 32, line 25, replace "5." with "4."

Page 33, line 10, replace "6." with "5."

Page 33, line 18, replace "7." with "6."

Page 34, line 5, after "provider" insert "or it is otherwise conclusively shown by the viatical settlement provider"

Page 34, line 19, after the underscored semicolon insert "or"

Page 34, line 22, remove "or"

Page 34, line 23, replace "(6)" with "c."

Page 34, line 25, after "viator" insert "in default," and after "bankrupt" insert an underscored comma

Page 34, line 28, replace "c." with "d."

Page 36, line 12, remove "viatical settlement investment agent."

Page 36, line 20, remove "viatical settlement investment agent."

Page 37, line 1, after the second underscored comma insert "or" and remove "or"

Page 37, line 2, remove "viatical settlement investment agent"

Page 37, line 6, remove "and viatical settlement purchase"

Page 37, line 7, remove "agreements" and remove "and viatical"

Page 37, line 8, remove "settlement purchasers"

Page 37, line 10, remove "or viatical settlement purchase"

Page 37, line 11, remove "agreement bought or sold"

Page 37, line 17, remove ", viatical"

Page 37, line 18, remove "purchase agreements."

Page 38, line 4, remove "or viatical"

Page 38, line 5, remove "settlement purchase agreement, product, or service"

Page 39, line 8, remove ", purchasers, or"

Page 39, line 9, remove "prospective purchasers"

Page 39, line 11, remove "or viatical settlement purchase agreement"

Page 39, line 14, remove "or viatical settlement purchase agreement"

Page 40, line 3, remove "or viatical settlement purchase agreement"

Page 40, line 5, remove the second "or"

Page 40, line 6, remove "purchasers"

Page 40, line 18, remove "or viatical settlement purchase agreement"

Page 40, line 28, remove "or viatical settlement purchase agreement"

Page 41, line 8, remove "or viatical"

Page 41, line 9, remove "settlement purchase agreements"

Page 41, line 10, remove "or viatical settlement purchase agreement"

Page 41, line 11, remove "or viatical settlement purchase agreement"

Page 41, line 22, remove "or viatical settlement"

Page 41, line 23, remove "purchase agreement"

Page 41, line 28, remove "or purchasers"

Page 42, line 4, replace the third underscored comma with "or" and remove "or"

Page 42, line 5, remove "viatical settlement investment agent"

Page 42, line 8, remove "or viatical settlement"

Page 42, line 9, remove "purchase agreement forms"

Page 42, line 23, after "desirability" insert an underscored comma and replace the second "or" with an underscored semicolon

Page 42, remove line 24

Page 42, line 25, remove "or viatical settlement purchase agreement"

Page 43, line 15, remove "and purchase agreement forms"

Page 43, line 19, remove "or a viatical settlement"

Page 43, line 20, remove "purchase agreement"

Page 47, remove lines 16 through 21

Page 47, line 22, replace "4." with "3."

Page 47, line 26, replace "5." with "4."

Page 48, line 4, replace "6." with "5."

Page 48, line 10, replace "7." with "6."

Page 48, line 15, replace "8." with "7."

Page 48, line 17, replace "9." with "8."

Page 49, line 25, after "fees" insert an underscored comma

Page 49, line 26, replace the underscored comma with "and" and replace "and viatical settlement" with an underscored semicolon

Page 49, remove line 27

Page 50, line 2, replace the underscored comma with "and" and remove "and viatical settlement"

Page 50, line 3, remove "investment agents"

Page 50, line 5, replace the first underscored comma with "or" and remove ", or viatical settlement investment agent"

Page 50, line 7, replace the first underscored comma with "or" and remove ", or investment agent's"

Renumber accordingly

2007 HOUSE INDUSTRY, BUSINESS AND LABOR

SB 2268

2007 HOUSE STANDING COMMITTEE MINUTES

Bill/Resolution No. SB 2268

House Industry, Business and Labor Committee

☐ Check here for Conference Committee

Hearing Date: 03-06-2007

Recorder Job Number: 4435

Committee Clerk Signature

Lisa M Thomas

Minutes:

Chairman Keiser opened the hearing on SB 2268.

Jim Poolman, ND Insurance Commissioner, introduced the bill. See handout A.

Poolman: As you know, SB 2268 is a lengthy bill. For those of you that have read it, it is approximately forty-nine pages. *See written testimony.*

Rep. Thorpe: How many complaints and problems have you had that this is addressing in the last four years?

Poolman: We actually do not have a lot of complaints in the business because people I think don't know. The viatical settlement business in North Dakota is growing. We have about three dozen viatical settlement brokers licensed in the state of North Dakota and all but two of them are out of state licensed viatical settlement brokers. There are only two that are residents of the state of ND. Just yesterday we received oddly enough, a complaint and I can't give you all of the details of the complaint but it is somebody that was out buying a number of policies specifically to viaticate them in the end we believe, so as the business grows, so will the number of complaints and so will the potential for this business to take advantage of ND consumers.

Rep. Zaiser: In terms of competition this committee has often talked about competition as one of the keystones of insurance rates. What will this bill do to create more competition in the business and thus maybe make it more competitive and maybe just a better run program?

Poolman: I am a firm believer in competition in the marketplace. I believe in fair competition and there will be more competitors in this marketplace because there is so much money available in the marketplace. When people are making hundreds of thousands of dollars in one transaction then there will be other people that get into the business and that is why you need fair regulation within the century code to protect consumers because there will be more and more people getting into this marketplace to be able to then encourage folks to sell their policies in the secondary market. Bottom line is the market is competitive. It will continue to get more competitive. I met with a brokerage house in New York City who is creating an auction platform for these particular products because so many people are getting into the business and so they will not only auction them in a computerized marketplace, but then they will be sold off again and again in the marketplace, that is the need for regulation in the business.

Rep. Zaiser: Just put it simply, if you could describe how this bill makes it so much fairer and eliminates the potential of corruption.

Poolman: There are several pieces of disclosure that viatical settlement companies are supposed to give under this bill to the consumer to empower the consumer to make a better decision on what they want to do with their policy. For example, if the viatical settlement company and the brokers are required to disclose how much money is involved in them vs. the consumer and what they are making off of the transaction and it requires all offers be given to the consumer. Not just one, all offers. So the consumer has the best purchasing or selling power and information to be able to make the most informed decision.

Rep. Zaiser: Last session I was the primary push behind economic development and accountability and there was a push from the other side that said it was too much. Now so I guess I am wondering is this over kill? Are we really making substantive changes or are we using a lot of words and filling up a lot of space? That was the accusation made of me in my...

Poolman: I wasn't involved in making the accusations for the bill, but what I can tell you is that under this bill there are economic accountability of public officials and accountability of folks that are dealing with consumer's money, are very different. When buying a contract from a specific consumer where a consumer may not be always the most informed consumer out there, it is very necessary to give them as much information as possible when dealing with a private company.

Rep. Thorpe: How would I know that I am getting all the offers?

Poolman: Because you are required to under the law, if you didn't get all of the offers and it was found out that there were other offers pending, that the broker did not deliver to you, we could revoke the license of that broker and potentially punish them, just like we would punish any other insurance that breached their fiduciary responsibility.

Rep. Thorpe: How would you or I know that we got all of the offers?

Poolman: In some cases, that information surfaces later and there may have to be a complaint filed with the ND Insurance Department as we would get any other complaint on an insurance agent or a broker, we would then investigate to see what other offers were out there and if you look under the examination section of the code, under the bill, they are required to hold all of that information under a records retention of all of the offers that were available so then we could go back and do the investigation of the broker and of the viatical settlement company to make sure that all offers were present.

Rep. Thorpe: What if the million dollar policy is brand new so if this bill as I understand, I couldn't sell to a purchaser of the policy for five years, is that right?

Poolman: No, that's wrong. If you were to purchase the policy after the two year incontestability period you could turn around and sell that policy in the secondary market. If somebody else paid for that policy for you, you would have to wait for five years to be able to sell that policy. That is where the rhetoric about this bill is that this is this broad five year waiting period for people to sell their policies. That is inaccurate. It is a narrow five year waiting period when somebody else is paying for the policy under the bill.

Rep. Kasper: I want to get to an example to be sure that your bill covers this situation. Let's say Rep. Boe and I are insurance brokers and you own a ten million dollar life insurance policy and you are going to sell that policy. Rep. Boe is going to solicit offers from viatical settlement companies and I will do the same. Let's say Rep. Boe comes up with an offer for three million from company A. I come up with my best offer which is two and a half million from a company B and all of the other ones are lesser offers or don't meet the guidelines that we are looking for. Rep. Boe and I are friends and we get to talking about it. Rep. Boe says the Rep. Kasper you have a two and a half million dollar offer and I have got a three million dollar, so why don't we co-broker this deal and let's talk to the viatical settlement companies about withdrawing this three million dollar offer. And if we do that, we have no competition because you think you are getting the best deal and what happens then with that two and a half million dollar offer is the commission is determined by the two of us because it is a gross offer for two and a half million. So we say, how much commission do we want out of this deal? Well, let's take a million and we'll split it fifty-fifty and we'll pay you a million and a half dollars. You trusted us to do our best effort and you really don't know the difference and we make the deal. What does this bill do to address that?

Poolman: Essentially, there would be the disclosure of third parties and that would be covered under this bill and we would go out and bust their butts.

Rep. Kasper: Currently, that practice is occurring in the industry per the Spitzer brief and I have read the whole thing.

Poolman: Yes. Clearly, this has not been taken to trial yet.

Rep. Keiser: Be careful. We are on record here. We need to stick to the facts.

Poolman: You have a pending case out there, but I think it is important to look at the allegations that are being made. The allegations, people are innocent until proven guilty, but if this case is true and it is proven true and these transactions are occurring in the marketplace, I believe that they would be covered under this particular bill.

Rep. Keiser: Just a point of clarification, Commissioner, in all of the other lines of insurance, would that be illegal for two agents to get together and work knowing that each will offer for a different companies and there might be a higher commission. This kind of backroom negotiation.

Poolman: If a complaint was filed with our office on that particular case, we would go after both of those.

Rep. Kasper: And the reason is that the broker represents the client, not the insurance company and therefore it is the brokers responsibility to fully disclose what is on the table and that is under current ND law with the broker definition.

Poolman: I believe that is correct.

Rep. Kasper: Let me get back to this lack of competition and ant consumer on the five year stoli. Your prohibition in the bill is only for five years, if it is an initiated offer from an outside party such as you coming to me and saying Rep. Kasper I want you to buy this ten million dollar policy and I will finance the premiums. Where I see that it is not anti-consumer is let's

look at what happens if the insured dies during that five year period when he or she had to own the policy. Let's say the premium is forty-thousand a year so in four years you paid one hundred and sixty thousand totally financed by the viatical settlement company and it's on my life and I die.

Poolman: Mama Kasper gets the money.

Rep. Kasper: She gets the money and loan gets paid off, is that anti-consumer that is a good deal for my wife. That is not anti-consumer, it is pro-consumer. So at the end of five years then if that sale is going to be made, then the viatical settlement company gets their premiums and I guess the policy gets their loan paid off.

Poolman: That was more of a statement than a question, I would agree with that particular statement.

Rep. Kasper: There has been some criticism that this bill that you are introducing is a rush to market. That you and NAIC want to get this out there quickly, so I am wondering if you can explain the process that has led up to this bill being introduced and whether or not ND is first, is that a problem in the industry or for ND?

Poolman: As I mentioned, the NAIC did a hearing and explored all the instances and stolen transactions and thus then a life settlement market. We researched and did a bill put together some legislation, added amendments to it from the interested parties. Of course the interested parties being viatical settlement companies, didn't like the outcome of the bill because it further regulates them and as I said before if I were a viatical settlement company or a broker, I probably wouldn't like it either. This particular bill passed the life insurance and annuities committee at the NAIC unanimously. So yes, we are first. We have bill deadlines that are probably more aggressive than other states but I could list off at least a half a dozen other states here today that are introducing this bill and in fact I am going to another Midwest state in

April to talk about this bill. There is interest country wide from many commissioner and legislators about introducing this bill. In fact, the Indiana legislature is going to have a bill to unband settlements all together. Some are taking an even more aggressive stance on this issue than we are in ND. Being innovative and first in a marketplace of protecting consumers here, I don't think it's a bad thing.

Rep. Keiser: Has the NAIC adopted this clause?

Poolman: No, we have not taken a vote on this bill yet. From a full membership standpoint but a stamp out of a committee much like the stamp out of the IBL committee, if it comes out unanimous, is a pretty good indication of how things may go at the NAIC. The corporate jets have been flying around the country lobbying the commissioners and legislators all over the country on this piece nationally.

Rep. Ruby: What is so magical about the number of five years? In two years now if someone purchases their own, what is so special about five years?

Poolman: We thought that five years struck a balance between the necessary property rights of consumers and them being able to get at the economics of the transaction that where stoli policies were created. If you want to amend that to eight or ten years, that would be perfectly fine.

Rep. Ruby: What I am wondering is if somebody is knowledgeable enough that they are going to sell the policy that they purchased within two, why they wouldn't be able to sell that? They are going to sell that within two years of purchasing it, but yet they are approached to do the same kind of deal in a two year period when it has been initiated by a third party, why wouldn't they annex in it?

Poolman: They still have the ability to go in and initiate a transaction, they just have to wait under those initiated transactions for five years and the purpose for the five years is to again

get at the economics. The likelihood that these investors are going to want to wait for that window of five years when in Rep. Kasper's case, the likelihood of a death occurring where the investor gets no money back on that transaction, it is far more significant in that five years than it would be under two years and again this is a very narrow five year exemption or five year waiting period for those transactions.

Rep. Ruby: On the other section, thirty seven, with advertising. Do you have this type of legislation for other types of advertising, I am wondering why this language in there?

Poolman: You will see as a notation on a side of this thesis that we do regulate advertisements in long term care insurance and life and health insurance. We do it by regulation and instead of doing it by regulation we did it by statute. If you want to take that section out and just give us blanket rule making authority to put it in code, I would be satisfied with that. The bottom line is legislators don't like to give regulators that broad based authority to be able to do that type of thing, so that is why we put it in code and added the language so you could see it up front rather than adding it in administrative code.

Rep. Zaiser: We were talking about organizations, NAIC. I have heard anecdotal information that there wasn't a whole lot of discussion when this bill was proposed, is that true?

Poolman: I couldn't disagree with that more. We worked on this issue for about seven months at the NAIC so input from all interested parties by in person meetings, telephone calls, we considered amendments from all interested parties and so those whose ox is being gored would like to say that there wasn't enough consideration on the bill because they are being further regulated. Absolutely not, the process was fair and in the end, just like you folks have to press a red or green light, the people at the NAIC pushed a red or green light and made a decision on the bill as it stood.

Rep. Zaiser: The other organization that deals with some of this stuff is NCOIL, and again I heard second hand that NCOIL recommended going slow on this legislation and being very cautious and maybe holding off for a session.

Poolman: The National Conference of Insurance Legislators has their own viatical settlement model. That model is about to expire and at the end of last year and NCOIL chose to move forward with their own model. They have considered no amendments to their own model, they have just taken comments on that model and have chosen to do their own as I mentioned, we have a model out there, it is one that I have been personally involved in writing and I stand behind our model as one that will protect consumers nationwide and in ND.

Rep. Zaiser: To make sure we are answering the question, they would prefer theirs and they are asking you to go slow on yours?

Poolman: The quote that comes out of NCOIL is that their policy makers want to way in on the issue. The NAIC has weighed in on their issue and so they would prefer to use their model that is not even finished yet.

Rep. Zaiser: Rep. Kasper talked about combining a couple of individuals to make a better offer, combining a two million dollar deal or whatever the numbers, wouldn't that already be illegal under the anti-trust laws and so this bill really wouldn't add to that?

Poolman: I believe that it would be illegal under the anti-trust laws but under the viatical settlement piece that you have in front of you, makes it very clear of what activities are legal and illegal under the bill.

Rep. Keiser: Does ND have an inferable interest law?

Poolman: Yes we do. The argument that you will hear is that regulators ought to enforce their current insurable interest laws.

Rep. Keiser: What is insurable interest?

Poolman: It's actually a pretty tight insurable interest law. I can't recite it to you but it is a pretty tight law. For example, insurable interest means that if Rep. Gruchalla's wife wants to buy a policy on the Rep., she would have an insurable interest in him because if he were to pass away obviously she would be harmed. For example, under corporate owned life insurance, under Quality Printing for example, the chairman has an insurable interest in his employees, so with prior consent has the ability to purchase life insurance on his employees because he would have a negative economic impact if he were to lose one of his employees. So that is the genesis of insurable interest laws. One of the arguments that you will hear is that "by God, regulators ought to just enforce the current insurable interest laws that we have related to Stoli transactions." Well if we were going to do that we would have to go in and examine every one of the transactions to make sure that it fit within the insurable interest laws that we have in ND. We can't do that. It's impossible to do that. We could do that under the new examination provisions that we have under this particular bill to help enforce the insurable interest laws that we have and to be able to go after the Stoli transactions.

Rep. Keiser: Who determines the insurable interest?

Poolman: Those that are buying the policy or selling the policy and those that are taking the policy because it really the owner of the policy, the determination, would probably be with the carrier to determine if there was insurable interest.

Rep. Keiser: So it would be the agent, when they meet with me on behalf of the company that are they suppose to determine whether I have insurable interest.

Poolman: I am not sure I can answer that question I think that is a question might be better asked of the agents but insurable interest is somewhat nebulous in how we enforce it and how we track it and so that is why I think the argument is a bit of a red herring because insurable interest really isn't tested until somebody goes to court.

Rep. Keiser: The target for Stoli's really aren't the million dollar plans, they are the big ones typically. I don't know where the cut off is, but they tend to be the bigger ones. Then somebody comes to an insurance company and says I have a person who and I want to insure their life for ten million, what due diligence is there in the underwriting and determining insurable interest. If I am underwriting a policy for ten million, I want to know a lot. I want to know a lot about their health, I want to know who is doing what. What is the role there?

Poolman: Much of the information gathered is on the application and one of the arguments will be well why not just allow the companies to ask the proper questions on the application, interestingly enough, many of the settlement companies are opposing adding language to those specific applications to be able to ask the right questions to get at the transactions so they are very hard to determine if they are being funded from an outside source. That is why we are getting at what we are getting at. The life insurers in many cases can't get the information, they don't know where the money is coming from to pay for those policies and so that is why the bill is written the way it is because they can't get that information.

Rep. Keiser: But that's their job.

Poolman: They will continue to ask about your health and that is a good question for the carriers for examples because they do that underwriting to determine what the premium should be on that policy but they do not ask the questions, you can't ask the question, where are you getting the money from to pay the premium so they can determine the underwriting on what they are going to charge you and whether or not you have insurable value on your life but they can't ask how I am going to get the money to pay for the premium.

Rep. Keiser: Isn't part of the problem underwriting policies of ten or twenty million that you are pretty sure aren't going to last?

Poolman: Yes. These companies don't know if they are going to last because they don't know that these policies are going to settle. You will hear the argument. By the way, these are not ten and twenty million dollar policies. These are one or two million dollars and they are getting smaller as the market expands. The scope of the policy is changing.

Rep. Keiser: Not stoli's

Poolman: I am talking about stoli's. These policies are not just ten and twenty million dollar policies, they are getting smaller and smaller and if you ask the independent experts in the field, they are getting smaller. You asked about pricing. There is and the reason that the policies and the price of policies and the risk that you run of increasing prices on all policies is because there is a lapse built in. Whether we like the issue of lapse being built in, it keeps the price of insurance lower because some people do lapse their policies. The secondary market will have and probably should have a change in how policies are priced. Under the stoli transactions when there is a complete intent to settle from the very beginning it will raise the cost of insurance for all consumers like you and me who are not involved in the stoli transactions.

Rep. Keiser: Isn't that really, you said insurance premiums have gone way up. My term insurance has gone way down. It's really whole life and universal life or other products that get into this market so it's not the whole range.

Poolman: I would disagree. I think there are all products being used, but you are accurate in saying that whole and universal life is the policies that are typically targeted. We have made other regulatory changes that have affected the price of term life and you know that for a fact being involved in the principal face reserving project and allowing for different mortality tables that allows companies to better assess their risk related to term life insurance that has helped drop the price of term life across the country.

Rep. Keiser: But term life has dropped, not gone up.

Poolman: Generally, that is because of the reserving requirements that are forced upon companies and holding redundant reserves or noneconomic reserves for term life insurance policies. We have made some very positive moves in that area to lower the price for term life.

Rep. Keiser: One of my heartburns and the only one that I really have with the bill is the attempt to carve out exception and when you do that you run into trouble. One of the carve outs is if I either bite it or retire from full time employment, do we define that in code?

Poolman: No, we don't. When I drafted this bill we tried to make the exceptions as broad as possible.

Rep. Keiser: I understand that. Let me give you an example and have you respond to it because this is something that the committee may have to deal with. I am retired and seventy-five years old, could a company hire me, pay me for two years and then I retire. I don't even go to work, I make the payments on the premium and I assign it to them and I re-retire and then, so statutorily we have created the option for a stoli.

Poolman: That argument could be made. To draw the definitions as broad as you could.

Rep. Keiser: I understand you want to be broad on the one hand, but what this bill may well do is create a legal opportunity for stoli's.

Poolman: I think if you did that, we could probably prove intent on when the policy was dreamed up and created.

Rep. Keiser: They pay social security tax, they pay federal income tax, they pay state tax, and everything and the investors knew what was going on. I get the retirement contribution on the deal and now I have a legitimate legal stoli operational in the state and we become a haven.

Poolman: If you have heartburn with that specific section, I would be fine with you taking it out.

Rep. Keiser: Let me give you another example. One of the problems with stoli's is the moral hazard. In fact, if you have people who own the policy on your life, they may very well want you dead. That may lead to certain accidents that you would not be very excited about.

Poolman: I call it the Tony Soprano factor.

Rep. Keiser: The second item in your current bill, gives me much greater heartburn from the Tony Soprano perspective. From the insurable interest, I could take out a policy on myself, my spouse wouldn't need to know about it, I could viate it, sell it off and then somebody is going to be very anxious if she dies because I can then sell. Oh yeah, I can.

Poolman: I would respectfully disagree with that, obviously on what grounds is the fact that if you have the ability to turn around and buy a policy now and pay the premiums for however long and then if you kill your wife, there is a fraud prevision in any statute that somebody could go after and contest that policy to be able to then prove that someone got ill-gotten gains from killing off somebody's spouse. I think that is pretty far fetched.

Rep. Keiser: You are introducing a moral hazard potentially.

Poolman: We are potentially, if one were to take your argument at face value which I think is a stretch...

Rep. Keiser: No more Soprano argument, I'm sorry.

Rep. Kasper: I am going to clarify where the chairman was going on this argument. First of all, this is only on the investor initiated life insurance contracts and that is where the viatical company approached someone to buy the policy. This has nothing to do with the legitimate sale of a policy that anyone of us would have purchased and decided we wanted to viaticate, is that correct?

Poolman: That is correct.

Rep. Kasper: Okay, so let's set that issue aside because we can argue about those issues but the problem that I have with the investor owned initiated process is, number one, the insurable interest that you were talking about. Everybody in this room is part of the investment pool that is going to buy these policies and they don't know me from a hill of beans but being I'm a legislator, they heard about me and I've got a high profile and I own all this property and somebody approaches me and says, we have got a deal for you. We are going to pay for a five million dollar life insurance policy on your life and we are going to pay the premiums. And in five years or two years, if this bill doesn't pass it's two years, we will buy that policy from you. Now why do I have to wait two years on the insurable interest vs. the incontestable clause, explain that.

Poolman: I need you to rephrase that because I didn't follow everything that you said.

Rep. Kasper: I am approached on a stoli purchase from an investor to buy the policy. I haven't heard about viatical settlements. All of the sudden I say, you know, I'd like to pick up an extra million dollars, this sounds like a good deal for me. The first part of me having to own that policy for two years, to satisfy the incontestable and insurability clause. Why is that?

Poolman: That is to protect you as a policy holder and the company who is issuing the policy and I think the explanation is pretty self explanatory.

Rep. Kasper: Is it because the insurance company wants to know that there is a legitimate reason for the life insurance, other than somebody making money on a viatical settlement when I die?

Poolman: That is the issue of insurable value on someone's life too. I am a state employee. I don't have a ton of insurable value I am not the target of a stoli transaction because I don't have good to stay, so the company is not going to write a five million dollar policy on me.

Rep. Kasper: So this appeals to the greed factor of this, all built into each one of us that if I can make something for nothing, and this is a good deal. But what it does Commissioner, and correct me if I am wrong, this type of approach, if the market gets large enough, it does throw off the actuarial tables which will result in the increased premiums.

Poolman: That was one of my points, yes.

Rep. Ruby: If I have a million dollar life insurance policy that I bought and paid for, for ten years, and I am approached by a company that would like me to bump it up to five million. I immediately sell that?

Poolman: No, because it would be a brand new policy to add on additional units to your policy.

There were no further questions from the committee.

Norbert Mayer, Fic. LUTCF, spoke in support of the bill. See written testimony.

Rep. Keiser: You mentioned that you asked the person what is the purpose and if it's large dollars, you have to give a lot more information. When do you have to start getting large information? Is there a dollar amount?

Mayer: I believe it is at a million dollars. It's not an extremely large contract that for instance, if it is a farm situation, you have to get financial information, what is the debt and net worth of the farm and what are the assets and so forth.

Rep. Keiser: You mentioned the great purpose with life insurance to continue the lifestyle upon your death. I have heard more numbers about lapses and people dropping their insurance, do you know what our rates are in ND on lapses?

Mayer: I am not sure what the lapse ratio in ND is. As I look at statistics from insurance companies as well as my own company, it is generally well under ten percent. Those lapses occur for numerous reasons. In some cases, some individual took a contract that they simply could not afford to pay for and yet in other cases there may have been a need for the

insurance when the contract was issued, but it no longer exists and they decide to cash it in or lapse the contract.

Rep. Keiser: But that is the lowest rate I have ever heard with lapses, but if it's true with the ten percent, what's wrong with making a payout? The owner of policy, if you are going to make the payout regardless, what difference is there to make to pay off the investors vs. the individual?

Mayer: If I understand the question, you are saying the payout of cash value, or death benefits?

Rep. Keiser: Death benefits.

Mayer: If this is a contract that you purchases with the proper insurable interest, it probably would not be a problem with that situation, where you yourself now, have different needs and whether the payout goes to you or to someone else, probably doesn't matter because legitimately, you have a reason to cash that particular contract in.

Rep. Boe: I was wondering if you could have some numbers for what is the volume of the stoli contracts in ND.

Mayer: I do not have numbers. Commissioner Poolman would probably have the best answers.

Frank Keating, CEO of the American Council of Life Insurers, spoke in support of the bill.

Keating: Our organization represents just shy of four hundred life insurance companies, obviously including all of the companies that do business in ND. Representing nearly ninety-five percent of the premiums, I want to thank the chairman for your leadership in NCOIL and Commissioner Poolman and his leadership at the NAIC to attempt to get their arms around this difficult issue of life settlement viaticals, stoli, ioli transactions. By way of background, I served two terms as Governor of Oklahoma which was obviously a glorious experience, but even

more glorious experience, I had the honor of serving the only Governor in the history of my state to serve in both houses. The reason I mention that, is not in a bragging sense, but to appreciate the challenge that you ladies and gentlemen have attempting to balance on one hand, the right of consumers and on the other hand, the property owners. How do you make sure that you, me, any of us that own personal property have the right to freely dispose of that property, consistent with public policy and the best interest of consumers it's a difficult balance. We do fully support the concept behind this bill. Obviously the individual variations, whether a particular clause or sentence should be removed is up to you members to determine what you wish to do. Now let me give you a couple of examples, shedding some new light on this challenge that might help you in your deliberations. My twin brother is in the life insurance business and I purchased my annuity from him and my life insurance policy from him. That is a seven figure policy. My wife and I have three children and all of them are out of school. I do believe in my grandkids and helping to pay for their education, but if that policy, if I should need the money, or if I should get sick or if for some reason I decide I want to sell it, I have an absolute right to sell that policy. For me as a property owner of that policy, I paid the premiums and the company is offering me a dollar and a life settlement company is offering me two dollars, I will take the two dollars. Let's take another example and let's say that my net worth were ten million dollars and some life settlement company came to me and said listen, Mr. Keating, we understand you have nine million of your insurance capacity, we have this great idea, we will pay the premiums on the policy. It's like taking my life insurance contract to protect my family turning then to an investment vehicle hoping for me to die, but we will take these nine million dollars and we will give you six figures in order for you to sign this contract and we all will live happily ever after. To us in the industry, and it's really interesting, the aging groups, you would think well they would like this stoli practice to continue because they make

premiums or their life insurance companies, you all must like this because you all sell policies.

Not at all because we see this as a direct threat to the reason for life insurance. The widows and orphans protection, life insurance contracts, are not investment vehicles. They are life preservation vehicles. So if the public policy issue here is to prevent a life insurance contract to be signed and issued on my life with the real purpose of encouraging me to die, but the bill proposes is a hiatus there. Five years subject to a series of exemptions where I could sell them if I wish, but to make sure that it's a legitimate transaction, just simply isn't an investment transaction, so public policy wise it's not good to hope that someday they die and it's in our judgment, it's a terrible perversion of the concepts behind life insurance and to get into business of investment as opposed to life preservation. But the second issue I wish to share with you. I am in the ranching business, but in Congress when you talk to members of the House and Senate, and you discuss with them a two hundred and fifty billion deficit, the question particularly with them is pay those. If we are going to continue tax cuts if we are going to take action in category A vs. B, it's got to be paid for. So there has got to be some offset tax increase someplace. Well, early in the seventeenth century, in the United Kingdom, laws were created with the sole purpose specific purpose of making sure we didn't speculate on the life of strangers, that was bad public policy because you had a policy on your life, somebody else took it out, the beneficiary was somebody else, you would watch what you ate and you would watch where you walked, so with insurable interest laws, were passed to protect people. That is still the law in most states. Because of the good public policy reasons for life insurance, the bill value in those is tax free and the payout of those policies to the widows and orphans that we seek to protect, or business partners to keep a business wherever it may be, those proceeds are tax free as well. If this concept, and that is why Jim Poolman said the five year will kill 'em. That is what we want. To stop this investment vehicle which is not a life protection

vehicle, it is strictly an investment vehicle, hoping for the death of people so the investors can get their money. But if this is strictly an investment vehicle, then that lifetime, tax-free build up and the lifetime tax free payout are in jeopardy. I think it would be calamitous for the people of America who don't save enough money to start. Young families or business partners to have a significant person die. The father, the mother, the provider and you have to pay little ordinary tax breaks on that life contract. That has not been the history of what insurance contracts in the US but that is very much what could happen if these kinds of perversions are permitted to continue. Remember the companies who can make money by doing this are against it. We Representatives have said that nearly ninety-five percent of the companies and the agents, they are against it even though they would make commissions on the sales of the policy so we know that you will have a difficult time and we would hope that this bill would be successfully considered as amended and this concludes my formal comments.

Rep. Thorpe: Could you share an idea on what the percentage increase in the stoli procedures has been in let's say the last four or five years?

Keating: There have been, since the viatical business began and it really began to provide an opportunity for AIDS patients to sell the policies. But since then a lot of very creative people on Wall Street figured out that money can be made here and there has been an explosion of interest in these kinds of products and alliterations. We had a hearing in New York called the NAIC had twelve commissioners and I remember one of the commissioners asked to the life settlement people, there is nothing wrong with life settlements, but let's say an individual gets a policy intending to sell it and it is solely an investment vehicle hoping for the death of that life insurance beneficiary, is that good or bad? All of these people said bad. I thought we are the bad guys because it sounds like everybody is in agreement, but quietly this industry has blossomed and our concern is that there is very little lapse here which is going to drive up the

cost of life insurance. But it is a perversion of what a contract is all about. We know there are a lot of policies being sold, we don't know the number exactly.

Rep. Kasper: You alluded to the basic nature of the life insurance contractors is the tax free death benefit. I am in the life insurance business and it's been my whole career out of college. If the perversion of this tax free benefit is challenged and Congress someday says we are going to take it away, what would happen to the viatical companies where their death benefit would no longer be tax free?

Keating: Investors will respond as you know to the bottom line. If I make thirty percent less I'll figure it out whether I can sustain that figure. The problem is if there is a tax due on a life insurance payout then that widow or orphan that business partner is going to have to do less with less. The nation and Congress has found that is not just what the policy does. Life insurance should be paid out tax free, it's not an investment vehicle, and it's to keep mothers and children in their homes and businesses afloat. The investors will figure out whether or not they want to continue because of a lessened percentage. What I am afraid is going to happen and we have not enough people in this country with enough life insurance to start with, you will have a lot people saying it's not worth it, I'll just buy a new plan. And that is not good public policy.

Rep. Keiser: I am not sure that a viatical is tax free.

Keating: That's right.

Rep. Keiser: This bill clearly states, one of the very positive things in this bill is the disclosure to the party.

Keating: What I'm pointing out is, if the Congress in a PACO environment, needs two hundred and fifty billion dollars a year, this is a rich target environment. The people who get hurt are not the investors, it's the mom's and the papas.

Rep. Keiser: Everybody agrees that stoli's are bad. This is attempt to regulate them, again my concern is that if we have two options, as some of the states have done, we take out these sections and then move it to five years and if we do that, it affects everybody. If I divorce my spouse, so I go out and get a stoli and we are seventy-five years old and they say look you know what, you can take out this policy for two years and then we are going to legally divorce, but I promise to remarry you and then we could settle that. Most people are going to find a way around these exceptions and make it legal.

Keating: Mr. Poolman made the point that you will wrestle with these exceptions and like in my case, when I bought my policies from my brother I paid the premiums, I can sell it at any time, but if somebody phones me and it looks like a duck and talks like a duck then I have this five years requirement and I think what the Insurance Commissioner did and others is tried to find exceptions so it doesn't appear so onerous if something happens. Remember the worst that can happen if the investors don't get their money, if you die, you spouse or your business partner gets the money. That is a good deal.

Rep. Keiser: Unless you can't sell it on the market.

Keating: For you all, it is a balancing act, tug of war between right of personal property ownership and also consumer protection in the light of what is good in public policy.

Rep. Kasper: On the stoli policy you have already sold it. You've got the premium financing for a five year period of time, so under stoli you have no money out of your pocket. The viatical settlement company is paying the entire premium and they are going to forgive the loan at the end of the five year period and they are going to pay you a premium for using your life. So under all circumstances, you have got nothing to risk and everything to gain, whether you die before five years or sell it after the five years.

Keating: Basically it's somebody else's investment and you get a little cut in advance or later.

There were no further questions for Governor Keating.

Bruce Ferguson, American Council of Life Insurers, spoke in support of the bill. See handout B and written testimony.

Rep. Keiser: The bill that Commissioner Poolman presented to us does have a lot more in it than just the stoli issue. It has a section on disclosure a section on marketing, oversight and the volume requirement. ACLI's position I assume, is very supportive of those components?

Ferguson: As Commissioner Poolman alluded to, we worked with the NAIC for well over seven months to look at all of the various aspects of the model that needed to be updated. From our perspective, the most critical provisions were those dealing with stranger originated life insurance (stoli's), so we spent a lot of time looking at how to take this concept of intent to settle and put it in a form of a very specific amendment in terms of what is and what is not a viatical settlement contract. So our focus was on those areas. There are other areas of the model that needed to be updated as the NACS, the Elliot Spitzer complaint, clearly point to and those were parts that we did work on along with the agents as well.

Rep. Keiser: You made the comment that the differences between the NCOIL and the NAIC market, those differences really deal relative to the issue of the balance between property rights and stoli's and relative to the exception and the fact that as NCOIL people interpret these exceptions, it just creates a statutory opportunity to legalize stoli's. Which is a concern they have?

Ferguson: There has been a voluminous set of comments as you know submitted by all of the various stake holders in this debate that are just now being considered by NCOIL and my guess is that you will at least have two more meetings to look at how to figure that out. That similar debate had already taken place at the NAIC. The NAIC model upon which the ND law is based is in place in about thirty states or so and the NCOIL model, which is also slightly

different from the NAIC model also needs to be updated to address the same issues that the NAIC already went through, and so, the equilibrium we think was reached in the NAIC model, we are hoping to reach a similar equilibrium through the efforts of updating the NCOIL model.

There were no further questions from the committee.

Marilyn Foss, ND Bankers Association, spoke in support of the bill.

Foss: The interest of our members in this bill comes about because of the focus on financing the purchase of insurance. Banks finance the direct purchase of insurance for people who want to buy a policy for themselves and also obtain interest in life insurance to better secure the ultimate repayment of the traditional bank's loan. When we reviewed the act with Commissioner Poolman, we were concerned that several of the provisions in it had the potential for treating traditional bank activities as something that is regulated as a stoli and by the insurance department. In the Senate we did introduce and propose discreet amendments to make it clear that those traditional bank activities would not be covered by this bill. The commissioner agreed to those amendments, they were adopted by the Senate and we would urge the inclusion of those amendments in this bill.

Rep. Kasper: So the amendments that you are concerned about are on the bill as we have it in front of us right now?

Foss: That is correct and I would simply note that the office of currency has used our amendments to propose amendments at the NAIC level also.

Rep. Zaiser: Then you are in total support of the bill as it stands?

Foss: I am supporting the bill because of how it treats banks. I don't pretend to be an expert on viatical settlements or people who are purchasing these products for investments. I am supporting it for how it handles bank financing of insurance loans.

Elaine Fremling, agent, spoke in support of the bill.

Fremling: I am here representing myself as an agent in Fargo. I am here to provide for opportunity of protection, not except of being for life insurance. I have many policy holders and I think it's important that I bring you some local perspective to what is happening in the industry. About a year ago I was in Minneapolis with a client and they said they had a meeting held at our work the other day and there was a guy in there that was talking to all of us about starting to pool some money together or do something, he didn't know exactly what it was about, but he was talking about stoli's being sold on his corporate board room while they are at work. I bring information for a local peer agent of mine in Fargo who was recently approached. I think it is very important to understand that this stuff is not the big numbers that you hearing about. He described how he had been approached with the opportunity to pay ten thousand dollars as a representative for the opportunity to sell this. Like a privilege tax. If you are licensed in the state of Tennessee, you pay four hundred dollars to have a license there. With those ten thousand dollars, he would then have the right to market these policies and earn ten thousand dollars per each policy that was sold. The insured would receive about a fifty thousand dollar lump sum and I was not involved in the interview process or what actually occurred there but he gave enough information for me to say this doesn't smell right. If we want to return to the days of Billy the Kid it is a wagering contract. I am opposed to wagering contracts in my career and for my clients. My client's lives are protected because people die under natural occurrence, other than things like Katrina or college buses falling off of freeways and even that is taken into account. If we are trying to change the time frame under which money is being paid, somebody else has to get hurt. If someone is going to gain by getting the million dollars or whatever in five years time or two years rather than age eighty-six when they are forty-five. Time is a factor. Time is what is taken away from the insurance companies and their ability to properly write and rate and place the right premiums in place on insurance.

When you shorten time, more has to be charged from someone. My average client out there has to be charged more to be able to pay for the price of the investor wagering opportunity. I am fully opposed to what stoli does and I would like to see it not exist, but I understand there are legitimate reasons for people to sell their insurance policies and I appreciate that. I hope that it is not my client's needs that are driving that. I would simply ask that you might support this bill.

Rep. Kasper: I wanted to let the committee know that Elaine is too a gracious to give you her background and Elaine has served as a national trustee of the National Assoc. of Life Underwriters, and she has held various capacities and very prestigious positions.

Opposition was heard at this time.

Tom Kelsch, representing Peachtree Settlement Funding, spoke in opposition to the bill.
See written testimony.

Rep. Kasper: You make a statement on the top of page two that about forty percent of the policies lapse in the first five years. If a stoli contract were in affect, how many policies would lapse during the first five years?

Kelsch: If the policy was sold to somebody else?

Rep. Kasper: Stranger owned, by the viatical company, how many of those policies would lapse during that five year period?

Kelsch: They probably wouldn't lapse because they would be paying the premium.

Rep. Kasper: So this solves that problem then doesn't it?

Kelsch: The premiums would be paid and the policy wouldn't lapse and the individual would have gotten something for his policy rather than nothing.

There were no further questions from the committee.

John A. Kely, of Peachtree, spoke in opposition to the bill.

Kely: I was here before when this was heard in front of the Senate committee and I posed a question. When we look at legislation and law we look at it because it is a problem. When people have a problem they tell you when you are home. When constituents have a problem they find you at the gas pump, or wherever and that is usually when we start to think about things. The good Commissioner Mr. Poolman alluded to the fact that he hadn't really any anecdotal problems that have been brought to his department on this project. So I say then, why then and what is the issue here. No one seems to see that there is a problem. You have a bunch of big shots here from D.C., Ohio, but very few people here from North Dakota standing here as an opponent or proponent, it's people from outside. This is the genesis of a national debated issue that isn't resolved at NAIC yet. What this is about is a battle between segments within the industry between life insurance companies and the ability for the secondary market to exist. We talk about that this is imminent and it's something that needs to be done. Indiana was referenced. The bill in Indiana was defeated last week. It was withdrawn because it couldn't cross over. New York and California, our two largest states, Florida our third largest state, Texas, our fourth largest state, all with some of the largest insurance volumes in America and not one of those states is this legislation introduced. In Virginia, who concluded their legislative session less than four days ago, they did not consider this legislation. Why? Because it is not right. Why? Because it is being debated. NAIC debated this for seven months. A model act had been brought forth and ten days before it was adopted, the model that had been debated and brought forth and voted on, was dramatically changed. That changed version was the one that was adopted because no one was given any chance other than a several hour discussion at a hearing, as to what would go forward. It was referenced earlier that about NCOIL. NCOIL members are just like you. They are legislators. They create law and then turn around to the agencies and the departments to enforce the regulations for

those laws. NCOIL adopted a resolution that came back unanimous out of its subcommittee and twenty-eight to two out of its full committee and I'll read to you what it says so there is no confusion. It's says NCOIL- Resolution regarding the enforcement of existing state insurable interest laws (stranger owned life insurance and related actions). Adopted by NCOIL it is hereby resolved that NCOIL believes the first step in combating stoli schemes, lies with the enforcement of existing state insurable interest. Life settlements or other consumer protection laws and that state departments of insurance should in a timely manner take such appropriate actions. It is further resolved that NCOIL request that the National Association of Insurance Commissioners NAIC delay final action on it's model act addressing the assignment of life insurance policies and life settlements until December 2007 meeting, while NCOIL completes it's reviews and revisions of the NCOIL life settlements act. I stated all of the other legislatures that haven't done anything yet. I stated the fact that NCOIL has said to NAIC, please delay, let's look at this carefully. Is there a problem and are there laws? Well people have talked about stoli's is fraud. It's fraud. Commissioner Poolman sited a cause of action initiated by the Attorney General, now Governor of New York, Elliott Spitzer, under the laws that he had on his books, he went out and went after someone who was allegedly a bad apple for fraud, and if somebody is crooking' the books and if some brokers are getting together and colluding under anti trust and doing things like that, the laws are on the books. That is why Elliott Spitzer was able to go after them. Stoli is about at the inception of a life insurance policy. The fraud is committed at the inception. The fraud is committed when that broker, not the secondary market, goes and sets up the application for that life insurance policy and if he's telling the truth and if the disclosures that he has to put out there are truthful then this stoli's will be discovered and be precluded because that is truly what it is about. In the two years that the insurable interest is being established, the carriers have the ability to look at that.

Rep. Kasper: Briefly, who is Peachtree?

Kely: Peach holding company is a company that does settlement fundings. We purchase life settlements, we purchase structured settlements we purchase lotteries. We are one of the largest settlement funding companies in America.

Rep. Kasper: So you are saying that Peachtree has never to your knowledge participated in a co-brokerage circumstance like what was described in the New York cases?

Kely: To my knowledge, I can't deal with every transaction. It is not in our interest. It is not in our interest to not go out and put the best price on the table and to get a reputation. Some of these companies and the company that this law suit is against is a life settlement company. We just don't do life settlements. We do structure settlements, lotteries, lots of others. We have a fairly large reputation in the settlement industry. We are known for being the person who is going to give good prices. I would rather do five deals at good pricing than one deal at shenanigans.

Rep. Kasper: You talked about "the Insurance Commissioner should enforce state insurable interest law" and then you made the reference to vs. the property rights, where is the insurable interest in a life insurance contract where as an investor initiated contract? In other words, if Peachtree approaches me....

Kely: Peachtree doesn't approach anyone.

Rep. Kasper: If a viatical settlement company approaches me and they say to me, or a broker, where is the insurable interest if the offer to me is you apply for the life insurance policy, you keep it for two years or five years and we'll pay all of the premiums and then we will transfer it to a company. In your opinion, is there an insurable interest for that purchase?

Kely: In my opinion, the scenario you are talking about is what a broker is doing. I have nothing to do with that. Let me give you this scenario which is the same. I can only speak to

myself. A life insurance broker says to me when doing financial planning, with your values and your assets and money, as we look towards the things we are putting together, you will qualify for ten million dollar policy. One of the things you can do if you take that ten million dollar policy is there is no reason you should have to pay for it because you would be eligible for premium finance. And I would be eligible for premium financing because of my net worth and the premium financing value would all be against the value of the policy. The beneficial value of the policy. If you desire, ten years from now you want to sell it, that is your prerogative. The person who was saying that to me was not an individual with anything to do with the life settlement world. That is a bonofied premium finance transaction that many lawyers and many doctors and people like that go into. Yet under this law I would not make it. I bet you a lot of people of high worth use premium financing. High worth life insurance is not done with cash payment.

Rep. Kasper: The scenario you are talking about is a legitimate scenario because your financial planner is saying a bank would loan you the money. What I am talking about is stoli's and not that transaction, I am talking about where a broker or a viatical company initiates the desire to purchase the policy with the intent from the beginning to sell it to the viatical company.

Kely: That was just the point that I said. At the inception, that broker committed fraud. At the inception that broker sat there and said, you enter into this and don't worry we are going to have somebody else pay for this and pay you back. He at that point, committed fraud.

Rep. Kasper: You mean under this bill?

Kely: Under existing law. He would have to ascertain in his application the true value and reason for the policy. He could prosecute him today. That is why NCOIL said to use existing laws.

Rep. Zaiser: One of the things that I hear throughout is anecdotal information about what might happen to vulnerable adults if you were to come in and take advantage of them and it has come from a variety of sources. What would be your response to that and maybe these people have, these are some of the people that support the legislation?

Kely: I don't think that this legislation should be thrown out the window. I think that the work that NAIC and the work that NCOIL, and no one has disputed that eighty-five percent of this has some great value. I think one of the greatest things that could be accomplished is protecting consumers and I am a great advocate of it, is disclosure and information and I believe in disclosure in this sort of way. I believe that if you have a document you are trying to sell somebody a dual life settlement with a ten year old policy, I think that you should have a red stripe across the bottom and down the side that says buyer beware. This is necessarily not the transaction for you. It's got certain consequences and you need to know about that. I think that when you type it should be in two point mouse type. I think it should be in twelve point print so that the consumer knows that this product has certain ramifications to it. That if they are the life settles the product, that they may not be eligible again for more life insurance. They should know that. If my ninety-six year old mother, if she had done this, she should be able to know that she might not be able to get life insurance. She should know that there are ramifications. I fully disclose them. She should be told that if there are offers from me at Peachtree and offers of life settlement, she gets to see every offer that is put on the table to her. If that broker puts it in his hip pocket, then he should go to jail. It's bottom line fundamental right.

Rep. Keiser: So you support in the current draft, the disclosure sections, the marketing sections, the oversight by the commissioner, and the bonding?

Kely: I support the disclosure, yes. I think the bonding, the commissioner said that you could get a bond for twenty-five hundred dollars and could use it nationwide. If you look at the statute that he puts. I think if you are licensed broker, you shouldn't have to go out and get an additional policy. I think also that the question begs me, is there the ability to get to the two hundred and fifty thousand dollar bonding? Nobody's ever done it. On the marketing, I think the state now has one page of rules in the regulations for marketing rules and advertising for traditional life insurance. All of the sudden here there is seven pages? How is it that much different? I think that maybe you need to conform all insurance advertising to make sure that it's consumer educated and consumer friendly and it tells consumers what they need to know and that you can't misrepresent consumers in advertising. So I agree that those are the values and the disclosures. I will be happy to send you a Peachtree disclosure.

Rep. Dosch: Could you tell me from your company's standpoint, what has been the increase in the number of stoli and life settlement transactions over the last couple of years?

Kely: I think what you are saying is could you tell me for our company? We don't do stoli's.

Rep. Dosch: Life settlements.

Rep. Keiser: Within the industry.

Kely: It has grown substantially within the industry. Nobody really knows. Our company, we know our information. It's not a reportable transaction. That is why on the charitable owned life insurance, Congress turned and said one of the major problems is that we don't know how many of these transactions are out there that are causing a problem.

Rep. Keiser: This bill wouldn't require those transactions to be reported.

Kely: Under this bill, it would require that you notify the insurance department, but when we say a reportable transaction that a contraband. People have great weight in having to require

and make somebody make a reportable transaction to the IRS out of fear of what the IRS will do to them.

Rep. Johnson: You mentioned choli's, have they gotten any reports on how much?

Kely: No actually, the choli's provision was passed this last August and made it that transactions be reportable as of January 1. I believe it was about two weeks ago that the treasury issued the requirement publication having to do with reporting and when the reporting would start. Under the rule that Congress proposed for twenty-four months they would delay collection of the information and then they would report back to Congress what the details are. To respond to the reportable transactions, in the law here, that is proposed here, it is reportable but not to the state, it is reportable to the insurance carrier. So it goes back to the ultimate problem again. There is no central depository. So if a reportable transaction were to be done, it would probably be better if we reported the transaction to an entity other than the carrier. Not that the carrier shouldn't have information.

Rep. Kasper: I want to go back to the financing of life insurance. Does your company finance life insurance premiums?

Kely: Banks that we deal with finance them.

Rep. Kasper: Does your company provide the money to the banks?

Kely: When I give you that puzzled look, it's not out of disrespect, it's like I'm trying to figure out, because I really don't want to answer.

Rep. Kasper: If there is going to be a new purchase of life insurance policies and someone has heard about the viatical settlement opportunity brought to them by a broker and I am going to finance this policy and the decision has been made, does your company at that point of sale ever get involved in providing the dollars to finance that purchase. If there is a finance policy down the road, that a bank financed, would that be a new policy?

Kely: We would see it, it would be at least two years old.

Rep. Kasper: How many of those policies that you are aware about that are financed do you end up purchasing?

Kely: I would know how many policies we have that we purchase.

Rep. Kasper: That were financed?

Kely: I have to be able to see them.

Rep. Kasper: What I am getting at is that there are ways to structure a set of circumstances that end up being like a stoli only we've taken one or two steps toward the stoli provisions to be circumvented. It is still a stoli because it is still a financed policy.

Kely: No, no, no, no. I'm so glad you hit that. Because a life insurance policy is premium financed doesn't mean it's a stoli. In fact, there are brokers here, life insurance is regularly premium financed and high value life insurance is almost always premium financed. So the nexus that you are trying to say that if you premium financed an insurance policy, it's a stoli, that is not true. Is that what you were saying?

Rep. Kasper: I was just trying to get, to be absolutely sure that you are on the record that you are saying that to the best of your knowledge, your company does not initiate point of sale new policy products with the intent to the insured that once the two year incontestability clause is gone, that you will purchase that policy and you will either finance it yourself or arrange for the financing some other place.

Kely: We don't initiate policies.

Rep. Kasper: Let's talk about a broker that initiates it on your behalf.

Kely: No, no, no, no. Fundamentally, you have a broker. He comes to a life settlement company and says I have an insurance policy that I want to settle with you. So my settlement company, say bring me the policy, we'll then reach out to the carrier, we will see the validity of

the policy and find out it's life expectancy and analyze it. We, the life settlement company has nothing to do when that broker goes out and meets that person and says do you want to...people don't buy life insurance. So we are not involved in any point when somebody sells somebody an insurance policy. We have nothing to do with that end of the business. So to say we are involved in premium financing, we are not involved in that.

Rep. Kasper: Now we are getting to where I wanted to get. The broker, finds someone who owns zero life insurance. The broker finds someone and convinces them to buy a life insurance policy and the broker says I can find a company and finance this policy for you and I can also find someone at the end of the financing period who will buy the policy from you and you are going to make x number of dollars. The insurance says that sounds like a good deal to me. The broker then calls your company and two or three other companies and says, I have a client that wants to buy a life insurance policy, will you finance that policy for me and what terms would you do so if you will. Does your company enter into those types of transactions?

Kely: There are people who do that, but we don't.

Rep. Kasper: There are companies who do that, but you don't.

Kely: Again, it goes back to what I said, I think it is very important, even under that transaction, I go back to a fraud is a fraud is a fraud. The point that I was trying to make is that at the inception of that policy when that insurance broker did just what you said, picked up the phone and called the company and said I have somebody who is willing to take out an insurance policy if you will do this and if you will pay him that. On the application to the carrier, he has to state that question is there. He has to lie and commit fraud, so that broker is the one who is committing the fraud and under the law, right now, in the state of North Dakota, you can prosecute that broker and you can have that stoli and put him in jail and do what needs to be

done. That's why NCOIL said to deal with the laws on the books. They are there already.
That is why they were able to sue in New York.

Rep. Kasper: So therefore, under the circumstances you just described almost all stoli life insurance policies have the potential to be fraudulent transactions because if on the application the insured has to answer that I'm going to buy this policy and sell it to a viatical settlement company, that policy would never be underwritten by that insurance company, most likely and therefore in order for a stoli to be a stoli, there has to be fraud in the front end.

Kely: In order for the type of transaction that broker would have to commit fraud and the insured. What I am trying to say is the bill isn't needed, you can already get to there now. That's the point, the transaction that you just talked about is already under ND law, illegal, and can be fully prosecuted right now.

Rep. Kasper: Then there should be no problem with the bill, if it is just clarifying an insurance statute.

Kely: What I am trying to say though is if that is what your intent is then why are you dealing with the issue of the premium finance and affecting all premium finance products for the five year period. That the fundamental. As I said earlier, eighty percent of this bill has great value. Many of us worked for months to get towards it. What we are saying is on the way it was corrected on the five year provision of premium financing. It's not carefully crafted to deal with the realities of what today's premium financing laws are like.

Rep. Kasper: Perhaps it would help for Mr. Kely to look at some possible amendments to end his concerns.

Kely: The OCC submitted to NAIC their amendments to perfect the banking issues that were raised here in North Dakota and what the OCC said is they looked at the ND amendments and thought they were great. But said they are not actually accurate and made a few minor

changes that they filed, and this is the OCC this is the US Government. The US Government sent what they proposed as amendments in specific places and I would urge this committee that in perfecting your bill here that you use the OCC changes because that is what they are going to seek nationally. I think it's a minor tweak or two, but why end up in a constitutional challenge when you could use theirs and then turn around if the federal government and say we changed it the way you like it anyways so why are you coming back at us. So I would urge that you do that.

Rep. Keiser: When can you do premium financing?

Kely: Any time.

Rep. Keiser: So you can negotiate with a broker, we will do premium financing for a customer before the policy is initiated?

Kely: I am not an insurance broker and I don't want to speak for them. When I go out and I broker a policy and I seek an application, part of the process of that application is I am given the opportunity to finance the product. Am I going to use cash, am I going to use an asset like my house or whatever and insurance carriers and banks, credit unions, all do premium financing programs for insurance. Traditionally in the state tax planning as a state tax planner, you would use premium financing to fund the insurance policy for the payment of the estate tax at the end. Ironically under the provisions you have here with the exceptions and the five year rule, one of the exceptions it doesn't cover, you have a very fluid phenomenon going on in Congress right now about the "death tax". It comes to a cliff in the year 2010 meaning that in 2010 it comes back into full force. If in 2008 Congress would eliminate the estate tax and you would have adopted this five year provision, and I say well, I don't have any estate taxes pay anymore, I don't need this big insurance policy I got, so I might as well life settle it. Under this law you have here you would have to wait the five years. So those are little tweaking that you

so rightly point out Rep. Kasper that there is ways to make things better and maybe we can work towards that.

Rep. Kasper: I don't think that is quite true because under the current law, if it is a legitimate purchase at the front end with a premium financing you have the opportunity to sell it after two years. Stoli is the stranger initiated, the other if it is a need for estate planning, that goes away and the person on purchased on the front end, after two year incontestability period, the reason that is not done before the two years I think and correct me if I'm wrong is because the viatical settlement company wants to be sure that you get by the two year incontestability period so that the insurance company has less of an opportunity to contest the policy that you purchased because of the insurable interest level.

Kely: Under this statute, if you premium financed it for five years you could.

Rep. Keiser: Where does it say that?

Kely: Non-recourse premium finance. Non-recourse premium finance is when you are insuring...

Rep. Keiser: Do you know in the bill itself where it refers to that?

Kely: I don't have the section. At the bottom of page thirty four. Policy premiums have been funded exclusively with unencumbered assets including an interest in the life insurance being financed only to the extend of it's net cash surrender value, provided or fully recourse liability incurred or insured. If you didn't do your premium financing that particular way, you are covered under the five year provision. If I take out my premium financed and I am a very rich person and I premium finance and the bank says all we care about is we'll take an interest in the insurance policy because there is enough in the insurance policy and it's beneficial payment to cover your premiums, we'll write your policy. And they will do that when you are a person of means. That's what they do in estate planning.

Rep. Zaiser: How do you go about soliciting or securing or finding customers or potential clients, is it door to door or mass?

Kely: We don't buy life insurance. We don't sell insurance. We buy life settlements. So what will happen is a broker, usually the same broker who sold you the policy, one of the wonderful things about insurance agents, insurance agents are like funeral directors and bankers and car dealers. They have a relationship with their community. You always have the same broker to go to. The person you bought that policy from, they will call them up and they will say George, I have that million dollar insurance policy I took out about ten years ago and I am hearing maybe I should settle and sell it. He looks into it. That broker who sold you that policy knows that there are a half a dozen companies that are out there that buy life settlements so he is going to get on the phone and call them and say I have got John Smith in Fargo and he has a policy and what will you give me for it and he will call five other companies. Then he will come back and say here is what I got as offers. Which one do you want to go with? That goes back to the question that was raised earlier, showing the offers. It's key that when that agent gets those five offers that he is forced to show all of them.

Rep. Zaiser: So basically I hear it as a relational development, but then can I assume that there is not a lot of buying of lists and data where you see that there might be potential from people who might be ready to enter into a viatical?

Kely: In reality, is that insurance brokers have their list of customers that they communicate with on a regular basis and they will send them newsletters and sometimes they will say with Katrina, the following changes, you might want to look at flood insurance you might want to look at other options we have available and deductibles for your other property and casualty claims. There are now more annuities that are available and they might put in there by the

way, life settlements is an option you might want to look at. So yeah, mailing do go from brokers to people.

Rep. Johnson: Do those offers go out to the policy holders and what kind of commission is there for growth?

Kely: We provide in our disclosure what we are offering the individual who purchases the policy and what fees are being paid to the broker. It is plain and simple. Here is how much we are going to pay you and here is how much your broker is going to get.

Rep. Johnson: What was changed in the current law? In the current law, in the proposed engrossed bill it talks about having the commission included with the information that goes to the policy holder. In the law that is in place, do you know if that provision is in there where the policy holder gets to know the commission and interest?

Kely: I am not an expert on viaticals because we don't do viaticals. We do life settlements. We were never in the viatical business and never have been in the viatical business. We do life settlements. There is a significant difference so I would have to speak to somebody that knows viaticals. I don't know what ND's law requires now as far as offers.

There were no further questions from the committee.

Doug Head, Life Insurance Settlement Association, spoke in opposition to the bill.

Head: I have been around this industry for quite a while. I want to start out by siting a little story that Rep. Johnson told me about another bill you heard. *(skip story and went to testimony regarding the bill)* . One of the things that you can't talk about in the current law or in the proposal that you have from Commissioner Poolman, is that I would suggest you all consider real seriously, the option that consumers aught to be disclosed, the option of a settlement when they are about to lapse or surrender a policy. This is a phenomenon that is going to affect a whole lot more North Dakotans than three or four or five and that is the total amount

that has occurred in this state in the last year. Why don't consumers know of this option when they are about to lapse or surrender a policy, shouldn't they know that there is a secondary market that they ought to explore for the value of their policy and why are such disclosures not in this proposal. We suggested them at the NAIC level. Commissioner Poolman felt that this was sort of an advertising for our industry, not a disclosure to consumers but as long as we are talking about disclosures and I support disclosures across the board. We support the disclosures for the potentials for conflicts of interest by the brokers although there is already law on the books that says they have to represent the fiduciary duty of the seller and therefore would be tripped up by that provision. There is one thing that is not in current law and that is just to tell people that this option exists. How do North Dakotans find out about this option?

There is an old line that insurance is not bought, it is sold. They have sold a policy, whether it is a premium financed policy or the stoli's that we have been talking about. Where a stranger comes and says just lie on these applications and I'll fund it and you don't need it and we will somehow get you insured and then we will be able to sell the policy we get free life insurance. All of the provisions relating to that type of activity, we like, but interestingly, they seem to capture activities that are completely innocent, where someone, a business owner decides to for his own financial planning purposes, to take out a life insurance policy that he may or may not sell, depending on what happens with the state tax or any variety of other circumstances that he might face in the future. What happens to a typical North Dakotan when they contemplate a settlement? If they know about it number one. Number one, they usually don't know about it, so every year, in North Dakota hundreds if not thousands of policies are lapsed or surrendered by people who don't know that the value exists in those policies on the secondary market. Why don't they know about it? Because the insurance companies put out bulletins to their agents and they say don't talk about this option, it's a bad thing for

consumers. You shouldn't be helping to resell a policy that you sold. There is a lot of policies in the market today that we find in our market, because of the changing rates that are charged for life insurance where if somebody bought a policy ten years ago that has a lot of provisions that drive the premiums up, where as today he can get a better policy at a lower price if he just switches over to that new policy. Insurers like it when it's an exchange within their family of policies and they keep that client happy and they charge them a lower rate, but if the consumer takes the value of the previous policy, moves it over to another policy and has not used up all of his insurable interest, they don't like it because there is more value in the secondary market than in the lapse and surrender that the insurers offer. It is important for North Dakotans to know the option. So suppose they go to their agent and they say they would like to know about this settlement option. Well, the first thing the agent has to do is say I can't talk to you about it.

I am not properly licensed. Mr. Poolman indicated that there are two agents in the entire state who live in this state who are authorized to talk about it. Why are they not becoming authorized? We suggest that you consider direct authority to all producers to immediately engage in this activity so that they can talk to their consumers they represent about the option of a settlement when that option is appropriate. I am not suggesting that they talk to them actively selling the option of a settlement, but they should certainly be told of the option when they are about to surrender a policy. One of the things you could do is the agent could say to the consumer you can surrender this policy, you can do an exchange for a new policy within my family of companies and if you are representing only one company you might do that. If you have multiple appointments from multiple companies, you might know of another new insurance product that is out there where the consumer sells the policy in the secondary market and can go out and buy a new policy, a better policy for him and it's from another company. Now insurers don't like that activity. They have never liked that activity and have

resisted it all along but I would suggest that it is a good activity for consumers in that you have an opportunity to set a national bench mark by requiring disclosure to the consumer of the option of a settlement when it is appropriate and the consumer is otherwise going to lapse or surrender their policy. What happens when a consumer finds out about the secondary market from his cousin in Florida who has sold a policy? Well, he immediately goes to one of his agents and he can say, well, there is on the internet a bunch of people who are licensed in North Dakota who are professional brokers who help people to sell these policies and those brokers who are members of my association will help them. But they are not living around the corner. They are not able to determine really what is in the best interest and they certainly would be affected by this policy but they are out of the state. We would like to see a lot more people in North Dakota licensed and a lot more companies buying. Suppose that a domestic North Dakota agent helps his client find somebody to buy the policy. Right now in ND there are only nine licensed companies. Under the current law, that are able to buy the policy. The hurdles to enter the market are big and a lot of the companies have entered the market for advertising purposes because they want to say around the country, we are licensed in a lot of states, but they are not really actively perusing the market here because there are some hurdles in this market that damage the interest of consumers in trying to sell the policy. Some of the provisions in this law indicate that consumers who are trying to sell the policies need to go back to the life insurer who originally issued that policy five or ten years ago and just goes to all kinds of confidential medical information that they would now have to disclose to the insurer under any other circumstances. We think that is an invasion of personal privacy, that is not disclosure or consumer interest that is an effort by the insurers what I would describe as clever language in this bill that requires them to disclose additional information that requires the consumer to disclose the information, not to the settlement market which is interested in

buying them, but back to the insurer so they can figure out how to call them up and tell them over a period of a month or two, don't do this, it could be dangerous to you, we have a better deal. It is protectionist in my view and it sucks the consumer into giving the insurance company with whom he has one relationship and that is the insurance policy that was issue a number of years ago, it sucks them into all kinds of disclosures that are unnecessary. What happens if the provider actually goes through the hurdles to get a policy the capacity to buy policies in ND. And he is ready to buy the policy from that consumer, but the consumer is ready to sell the buyer is ready to buy. It's an arms length transaction with all of the disclosures that we do support in this bill that should be out there, available to the consumers and they sign an agreement, well, oddly enough, in this bill, the capacity of the consumer to have second thoughts about the deal, once the deal is cut and all the information is out there and the best price has been determined, the consumer has not thirty days but now has two months to reconsider, meanwhile, the insurance company has all of this new information about the insurer and can go back and say well we have got new information about you and you really shouldn't do this and will otherwise interfere with the transaction and get it rescinded. Buyers of policies in ND with a sixty-day window of rescission will be very reluctant to invest money in ND when they can invest money in New York or some other state with fifteen day rescission period. So expanding the rescission period which looks like a consumer protection, is actually a methodology for interfering with the transaction in my view. What if the consumer says I am sick and tired of dealing with this marketing in ND where I can't get any advise, I am going to Florida on vacation and he goes down there where his brother had sold him a policy and he said I want to sell the policy. There is a provision that say you can't move the policy out of ND. Now the license companies in ND support that provision because the policy isn't crossing the boundaries and the resident of ND is protected even if he tries to move the policy out of the

state. We support that proposal but I got to tell you, there are consequences in that proposal and that is narrowing the market to the very limited number of companies and as far as I know, only one company actually bought policies in ND last year. The reports were given to commissioner Poolman on Friday, the first of the month and should be available to this committee at some point in your deliberations. After the consumer has gone out and sold a policy hopefully successfully amid all of the disclosures that we support then comes the question that a lot of my colleagues have discussed which is the question of was the policy premium financed, typically these are the big policies. Chairman Keiser indicated most of the large policies do involve an element of premium finance, but this law prohibits the sale within five years if they are not exclusively funded with unencumbered assets. In other words, the assets, if there is an element of premium finance, ten percent or fifteen percent of the premium is premium financed then it falls under the five year band and that concerns us a lot. The provisions that go to the issues of the ND consumer are to me central to this bill. I think that there has been a law that inhibits the growth of this industry in this state on the books for some time. It is the law that you all passed five years ago. It was the second revision and during this time, the law has ballooned since thirteen pages to forty-nine pages. I support Commissioner Poolman's suggestion that you take out seven of those pages by removing the advertising prohibitions and letting the commissioner decide on appropriate advertising goals so if North Dakotans can become aware of this option. That is the kind, you have got one paragraph in the insurance law governing insurance advertising. You have seven pages that are in settlement advertising. Throughout this bill, there are provisions like that that we can squeeze out to get at the essence of what you want to protect and what you want to do and I would suggest that what you really want to do is protect consumers in the state, and advise them of their options to give them a maximum number of disclosures that they might need, just going

through the hazards of selling a policy the moral hazard or any of these other issues, but at the end of the day, let the consumer decide what they want to do.

Rep. Thorpe: I have been thinking of this five year thing in here and really having some problems getting around it. Who is going to get protected the most here? I understand the intent of the bill however, it is for pretty much an agricultural state and we have producers out here that are large operators and I'm sure that some of them would be probably for lending purposes, would be required to have some life insurance coverage for protection of their loans. So then if they have to get some financing on that policy then they are subject to the five year penalty? Am I correct on that? So on the second year of that policy, they have a severe drought or have to sell off their livestock, they wouldn't be able to sell on that secondary market to satisfy, so we are protecting some people maybe on one end, but we are hurting some people over here.

Head: I view a lot of these proposals as highly protectionist. One of the things that we suggested in the NCOIL process and the NAIC process are some warranties from buyer's policies where they have to sign a document that says I am not engaged in any transactional plan to sell this policy down the road. We are fine with that kind of warranty. We are fine with documents that allow the life insurers to grill down on the major and the reasons behind the purchase. We believe that life insurers pay a lot of money to very fine actuaries and that they ought to use them and use their underwriting departments to understand what they are selling. I can tell you a true story from back in the viatical era when a lot of policies and most of the fraud involved investments but there were situations where sick people with AIDS were buying policies and were lying on their applications and the life insurers said, we can't afford to underwrite hundred thousand dollar policies we can't afford to drill down and find out what is going on, we are just moving paper around so fast and we are taking in policies and we get

thousands of them everyday and we can't analyze them. Now they are saying they can't afford to or they can't somehow underwrite a ten million dollar policy with premium finance up front.

They got all of the documents and I think that underwriting is where it's at.

Rep. Kasper: You indicated that it is onerous to be licensed in ND. Can you tell me what the requirement is that is concerning you?

Head: Under current law, I believe that it's the basic problems, the idea that you have to obtain second license. Many states have gone with the idea that all, Maine was the first state to go in this direction. All life insurance producers are automatically able to help their client sell a policy by virtue of their life insurance alliances which train them to sell the policy in the first place, they certainly want to be able to help the client understand it's value in the secondary market and I think that is the way you ought to go.

Rep. Kasper: Are you concerned about the insurance company level, about licensing in ND. You said that it is onerous for insurance companies to get licensed in ND, where is it onerous from your perspective?

Head: I think it's a primary deal is really the size of the potential market. If I understand that nine companies have gotten licensed and from my members, every single one of those companies that is currently with a valid license that hasn't been rescinded is a member of the association and they all tell me that there isn't much traffic here. That it is hard to get the communications to the community about the option of a settlement that as a consequence they are licensed for purposes of being licensed in ND so they can say they are licensed in twenty-five states. They are not licensed because they are seeing a lot of market activity here.

Rep. Kasper: I will answer the onerous question for you. To get licensed to sell viaticals in ND you need to pay a two-hundred and fifty dollar license fee and supply the proper

documentation so I don't think that is real onerous. I am wondering in the area of advertising is there anything in the current ND law that prohibits companies to advertise their product in ND?

Head: There are many pages of advertising provisions in the current law.

Rep. Kasper: But you can advertise?

Head: If you follow the details of the law. I would suggest that it may be more appropriate to give the commissioner the authority to set those rules as he has with the life insurance business rather than put it all into one.

Rep. Kasper: When you are talking about onerous for the brokers. I have been licensed for many years in ND. We have continuing education requirements in our state so that we are continued to be updated on what is going on in the marketplace. Would you not think that before a broker would sell viatical settlements that they should be educated so that they can properly inform the clients?

Head: I think that would be absolutely an acceptable provision and I would support it. I suggest however that educating agents should not be, it should be part of the agents responsibilities to talk to his client about the settlement option when he is about to lapse or surrender. He should not require another two hundred and fifty dollar payment and special education and a certificate and a bureaucratic process to be able to do that. It ought to be part of the essential business of any producer to be able to do that.

Rep. Kasper: Does your association provide continuing education to agents around the country so that agents who wish to sell these products can be educated?

Head: We are working with a number of education providers and we are working to develop a course of that.

Rep. Kasper: Would you agree that if a life insurance company chooses not to be in the viatical settlement business that would be their choice of how to do business and not your association's choice?

Head: Here is the issue. If a life insurance company chooses to prohibit their representative, the agent, from talking to the consumer about the options I think that is an interference with the consumer's right to know some stuff about the value of his life insurance. Now if the insurer demand that they not talk about it and there are a lot of documents out there where insurers say to agents that you can't talk about this to your client and therefore perhaps a lot of the agents in ND are discouraged from even seeking a license which is kind of a red flag. They don't get licensed.

Rep. Kasper: That still under the right to be able to engage in business an insurance company has a right to decide how they will do business and a broker has the right to determine whether or not you will mark the cards with one company or multiple companies. I could be marketing products with fifty companies that say I could not do viatical settlements but I could find twenty or so out of the seventeen or eighteen hundred that would have no problem so as a broker, I really better have an opportunity to look.

Head: I think an awful lot of companies allow their agents to talk about viatical settlements or do not interfere. What I would suggest as public policy makers you may want to say to the public that you are going to guarantee your right to know in certain circumstances whether the insurance company allows it's agent to talk about it or not, you can go get advise from another agent. And your agent ought to disclose to you that he is prohibited from talking about the option.

Rep. Kasper: Or your association or companies could advertise in ND to call an 800 number if you so chose to do so.

Head: I think it would be a lot more helpful for most people in ND to talk to their friendly agent down the street.

Rep. Keiser: For the two hundred and fifteen documentations, is that for each agent or for the company?

Head: That is for each agent.

Rep. Kasper: It is a two hundred and fifty dollar company license fee and then the broker is a two hundred and fifty dollar fee.

Rep. Keiser: So there is more than two fifty.

Rep. Amerman: The stranger that goes out and says you should have this life insurance I am going to pay the premium, that is a stoli?

Head: Yes.

Rep. Amerman: Is there, in your opinion, a certain age group that they focus on?

Head: I think that life insurers in general focus less on young people than on older people. Life insurers in general get higher premiums. Some more volume to older people because that is where the money is. The settlement business is following the life insurance business's lead in looking at options. The more options there are for older Americans, we think the happier they are going to be.

Rep. Amerman: It's probably then the older people, and so then there is a lot of things in here about advertising and this is one way to get to these people and come to them. Do you know what other methods they might use to go out and solicit this? If somebody in another state finds out that I am an eighty-two year old man, how is he, does he buy lists?

Head: I think they try to find out who might sell. They try to talk to local agents who are familiar with the circumstances of their clients. They try to get those local agents to talk to their clients and if the local agents don't tell them, they then are reduced to trying to figure out methods of

talking to seniors through senior advertising in New Mexico and Florida in the winter. I have seen a number of seminars on the subject in Florida last year. We target the seniors because seniors have those policies that might be settled. A person who is forty years old and in great health is not a great settlement subject.

Rep. Keiser: I want to do premium financing and maybe sell my policy, if we have a five year limitation, can I buy my policy in another state?

Head: Sure.

Rep. Keiser: Can I buy anything else? So this wouldn't, if passed here, it won't include other states in doing this or?

Head: It won't conclude people from doing premium finance deals when people go on vacation.

Rep. Keiser: I couldn't go out to another state and buy it?

Head: That is my impression

Rep. Kasper: If your broker became licensed in MN or AZ, then signed the application in that state, so long as they were licensed you could buy it there. It called a nonresident insurance license.

Rep. Keiser: Okay, so if a non resident insurance in any other state?

Rep. Kasper: I am licensed in twenty some states for the sale of insurance.

Rep. Keiser: But would the policy have to meet these conditions or the conditions in MN?

Rep. Kasper: I think the insurance department could answer that. I would think that the law of the state in which the policy was purchased.

Lori Wolff, State Insurance Department: It would be where the policy was actually sold.

Wolff: Yes, the policy would go to the state where it was actually sold. So if Mr. Kasper licensed agent dually licensed in multiple states had a client in MN transactions sold over in MN, it is MN law that would follow.

Head: When you seek to sell the policy would ND law prevail?

Wolff: If they are going to seek to sell it and viaticate it, again, where are they going to go and have that transaction happen? Are they going to cross over to Moorehead and Rep. Kasper who is also licensed viatical settlements broker, are they going to do it all over in Moorehead? Then it's MN law. If they do it over here, then it is ND law.

Rep. Keiser: If I do live here and I go to MN and Rep. Kasper is my agent, we will be able to use MN law whatever it is and on a big deal, I might even fly to Hawaii.

Head: Rep. Amerman has a district on the corner of MN and I can see people get into their cars to go across the line to buy or sell insurance, in both South Dakota and in Minnesota, there is no law what so ever governing these transactions for seniors. In Minnesota, they cover only terminally ill people and in South Dakota they cover nobody. So we have protected people in ND in a way that is sort of I think interferes with their options.

Rep. Dosch: Give us a rough ball park estimate, when we talk about selling these policies, say you have a sixty-five year old million dollar policy and he wants to sell it and is in relatively good health, what is something like that ball park?

Head: The Florida department has gathered statistics from around the nations. The only one that I have been able to see the statistics around the nation and generally speaking, they are finding that the typical policy that is sold is about a million to a million and a half dollars in face. The seller gets on average between fifteen and twenty percent of the face and that the surrender value of the same policy is five percent of the face on average. So we believe that our industry in total is bringing ten percent of the face of the policies to the consumers who

know about the options and I wish a whole lot more consumers knew about the option and I wish a lot more was on the table informing, not scaring them.

There were no further questions from the committee.

Steven Washington, Life Equity, spoke in opposition to the bill.

Washington: We are an Ohio based licensed life settlement provider and we are also a member of LISA and also a member of a small association of institutes and finance providers. One of the issues that we face in our industries is that people don't understand typically what life settlement providers do. It is frequently the case and I meet with regulators and have to explain to them and as a result it makes it much more difficult in these conversations to actually talk about instituting regulations because people don't understand what we do. We think too that likewise consumers often don't understand the different players in this industry and as a result we too favor regulation. We think it's a great way to level the playing field and it's a great way to get rid of bad conduct. We think that is the right way and we believe the consumers should be protected because they should understand who the different players are and we do support the consumer protection disclosures embodied in this act. My company is actually very involved too in detecting fraud and we work closely with investigators and regulators because we believe that that's also very important way to level the playing field and get rid of bad conduct. I do take great exception to statements that have tried to characterize the industry based on the allegations against one company. I really don't think that's appropriate and I would just like to make that comment. We were actually present and participated in the NAIC process so we are very familiar with that. From our prospective, this is not a question of whether in fact we care about whether we oppose regulation or more regulation. We think that it would be fine to impose additional regulation, we just want the regulations to be reasonable. We think that people should be aware of the options of life

settlements. This is a capital markets based economy. People should be aware that the company policies do have value separate and apart from what insurance carriers are selling to their policies. We are not suggesting that life settlements are (can't understand). We simply think that for those people who become seniors who have policies that they are considering surrendering or lapsing that they should be aware of the option. Just on the stoli issue, I think my concern with the definition of stoli statute is that it is really limited to this concept of knowing recourse for financing. I am not sure that is correct. I actually think that it's recourse or non-recourse is not the issue, I think it's at the inception of policy for those who should be looking at the arrangements that is actually entering into or agreeing on the side to enter into with potential some investor who is actually inducing or offering some benefit to enter into it. So that is where I would prefer the focus to be. I think that there are those existing laws to deal with that and I don't think that the way this statute is being reworked is essentially everything falls into the five year rule and then you are back out.

Rep. Zaiser: In addition to what Rep. Keiser talked about, in terms of identifying those items that were added late, I was wondering if you couldn't do the same thing that we asked of Mr. Head in terms of what elements of the Commissioner Poolman's bill you agree with and which ones you don't agree with.

Washington: Look there's a lot of good stuff in the bill. Don't get me wrong. We actually participated in and agreed it was interesting because when the proposal first came out, neither the life insurance industry nor we took it very seriously. It was actually thrown out as an idea. We were asked to submit our respective comments on bills and neither saw it actually as put into a bill the five year transfer restriction period until in September of last year.

Rep. Zaiser: I do agree that Commissioner Poolman has stepped up to the table and at least begun to address this but I would like to be able to prepare the differences your group has with Commissioner Poolman.

Rep. Kasper: Does your company through brokers or directly do any company or broker initiated stoli products?

Washington: We don't do premium financing so we don't really have a dog in that fight. We just do life settlements. That is all and we work with brokers come to us with policies and the clients and it's a very competitive market that the circumstances concerning the allegations and it's difficult for me to explain because from our perspective we actually know when competition is out there and we know that we put out an offer on a policy, we put out what we call a fair offer because we assume that somebody else is going to be bidding too. In fact when somebody calls me and it does occasionally occur if someone would call me directly, someone who is talking about what we were before and even though it's really not in our best interest.

Rep. Keiser: I have to say it amazes me that everybody is against stoli's but I have yet to meet anybody who says they support them. To think they are illegal and everyone supports consumer protections and doesn't have much problem with most of the bill and actually doesn't oppose regulation, you said all of those things. Do you anybody who opposes those things?

Washington: No, I think that it's a very complex issue to try and regulate. I am not going to dispute that. I think that we all have to and that's the difficulty of wrapping our minds around this is how do we affectively come up I think that the Life Aid committee did try to come up with a simple solution however, I think it's over broad in it's application and it will affect consumers considerably. I think that what we should be looking at and what was done actually is that the distinguishing features of the stoli is what makes it different from let's say company owned life insurance, what makes it different? There is a scheme that was actually defended at NAIC

where there were insured to take out insurance but the policy would be some inception that put into a trust controlled by investors. The insured's would be entitled to five percent of the net death benefit. When this was questioned, the response that was given by Commissioner Poolman was well that's not a problem because those policies don't actually change hands. They don't change ownership. I am not so sure I agree with that. I think that is an argument.

Rep. Keiser: If we were to accommodate your suggestion and say we are going to not exclude and allow that to be done for the policy, then, other than, if we take that out, we don't need the exceptions really too much anymore. And if we don't need, but we could have everything else in the bill.

Washington: What we had proposed as an alternative was a set of disclosures to consumers and certifications by consumers to make sure that they were aware of the impact of a finance transaction to acquire the policy. It would reduce their insurability and it could have tax consequences to that. There is a whole litany of disclosures that we have proposed. There is also a certification by the individual to say this is not a list of transactions it actually is intended to disclose. That proposal was actually never debated or considered.

Rep. Keiser: One thing I have not heard today is if we were to leave at two years all types of policies, what about the potential for a look back of three-five years to allow companies to say you know what, they did buy it they did premium financing and it was insurable interest etc. etc. We think it was a legitimate deal that there wasn't a stoli going on but, and if there wasn't there would be no problem but allowing a look back.

Washington: I think it raises two issues in my mind. First is that I am not sure that insurance carriers are really necessarily going to have any more information five years down the road or four years, than they already have at the beginning of the policy.

Rep. Keiser: Theoretically I agree with you, but in the two years comes up and now its clear.

For whatever reason, years three or four, something is and we become aware that their intent was the contract as it was wrong.

Washington: I guess the only other concern I have I think that to entertain that we would need to be very clear about the information that we required and the level of information that would be required to prove fraud. But I think from an investor prospective the question it raises is the level of certainty that they have that a transaction used.

Rep. Keiser: There is some risk if it is a stoli so you both better be sure on both ends, both at the inception and at the time of transaction.

Washington: It's an interesting concept and again I think that we should be exploring different options which I think that the NAIC did not adequately do.

Rep. Kasper: Do you think stoli arrangements that should be prohibited?

Washington: Yeah, but I think you have to define it and that is the issue is that it is not defined at the NAIC and so the way it has been objectified in this bill and as opposed to the amended by the NAIC if it's really thrown into this non-recourse premium financing realm.

Robert Harms, Imperial Finance and Trading, LLC, spoke in opposition to the bill. See attached testimony, labeled number three.

There were no questions from the committee.

There was no further testimony in support or opposition to the bill. The hearing was closed. No action was taken at this time.

2007 HOUSE STANDING COMMITTEE MINUTES

Bill/Resolution No. SB 2268

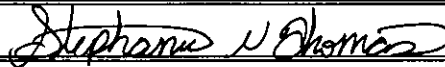
House Industry, Business and Labor Committee

☐ Check here for Conference Committee

Hearing Date: March 14, 2007

Recorder Job Number: 5071

Committee Clerk Signature



Minutes:

Chair Keiser opened the discussion on SB 2268.

Jim Poolman, Insurance Commissioner: I'm not sure what the committee's intent, or where they may have problems with, so what we have told members of the committee when asked is that we understand Mr. Chairman you had a problem with the potential moral hazard of a couple of the exemptions. If you'd like us to draft an amendment to take a couple of those exceptions out, we're happy to do so to accommodate your concerns. Those exceptions are in current law, but if you want us to take them out, we're happy to do so. One of the other concerns that has been brought up has been maybe some confusion on the bonding section, that the bonding requirements they think as are worded is going to require a separate \$250,000 bond for each state if that viatical settlement broker was to do business. We don't agree, but we're happy to modify the language, if possible to take that concern off the table, because it is not meant to be an inhibitor to do business here, it is meant to provide some consumer protection if necessary.

See handout A.

Doug Head: This is a simplified effort to give you a thought that we did not contain in the amendments, but which we think you should consider, and which the department may want to consider in terms of their responses, or how we go forward.

See handout B.

Steve Washington: See proposed amendment in handout C. (Amendment is highlighted in yellow on the handout)

Rep. Keiser: Is this section tied to the broker with some of that liability?

Steve: If you go back to section 22.1, yes. What it requires is prior to initiating a transaction that the life settlement provider or a life settlement broker must fully disclose to ensure the plan and transaction, and seers the transactions to originate a new, and continue a beginning of in advert to an insurance policy. We had some concerns about that provision. It said we're a life settlement provider for in states. What does this great standard disclose what does that require? It presents opportunity for, it carries to slow down the process. The concern also that we raise is an antitrust issue of the Commissioner's, that it can be collectively used by the employers. We as a life settlements provider have concerns, because we by definition continue policies, when a policy is life settled, and don't understand why that should be subject to criminal liability in a settlement. We disclose to the carriers when a transaction occurs, so that they know a transaction is occurring, so it just doesn't seem to make sense that is should suddenly be subject to criminal liability.

Rep. Kasper: Is the criminal liability potentially to the viatical company, or the broker, or both?

Steve: It imposes the obligation on each of the brokers and the provider. So, they're both subject to liability.

Rep. Keiser: I have to be a resident in the state to sell the policy, right?

Doug: You have to be a resident. If you leave ND and go the Arizona for 6 months, and you become a resident of Arizona, then you can sell the policy in Arizona. If you assign it to a trust in another state without moving, in order to sell it, that would be a prevalent act.

Rep. Keiser: Why do you object to this?

Doug: We just want to point out that the provision does not have a law similar to this chapter, and it is vague. We're not sure if that applies to SD, Minnesota, or to another state. To date, this would be the only state that has identical to this law. So, that may be an issue.

Rep. Kasper: On line 24, it goes on to say for the expressed purposes of evading or avoiding the provisions of this chapter. Isn't it just a narrow area?

Doug: Very narrow. That narrows what's going to potentially happen here, but then we're into the matter of a jury to determine intent.

Rep. Keiser: So, the solution of the proposed amendment is just to delete this, rather than correct the language.

Doug: Yes. My thoughts are it's going to be very difficult to use by anybody, and it sufficiently encumbers the right to consumers in the state that you ought to consider deleting.

Rep. Zaiser: Is one of the issues there the definition of qualified institutional buyers?

Steve: No, it was a new provision. It was added without explanation, and we'd like to know what it's for.

Rep. Keiser: So, you're saying there is no loophole. I'm assuming that's a concern to cover the entire basis here that I see with the viatical settlement provider, and it can't be a sub city area, to somehow transfer this piece.

Steve: You have to have a license. The provider has a license to negotiate, and enter into a contract with the seller. So, no one else has that license.

Rep. Kasper: The striking on line 7, is that something that you struck out of the bill, or that was struck out?

Steve: It was added language, and ours is to indicate our preference to amend.

Rep. Kasper: So, your giving us your suggestion that line has been struck. It's currently in the bill, but your suggesting this.

Steve: That's correct.

Rep. Keiser: It seems to me that you can't read line 14 without reading 16-22, and to deal with the two are part of the same issue.

Steve: 16-22 were moved down. So, item #2 should be listed as #1. It should be renumbered.

Re. Keiser: So, the number one has been struck?

Steve: It has been moved down, and is actually excluded now from the viatical settlement contract definition.

Rep. Keiser: You're saying that the OCC requirements would obligate us to the new lines 16-22?

Steve: No. The OCC did a memorandum of their suggested changes. This is one of the suggested changes that they made, because they said this is going to interfere with the banks traditional premium plans lending.

Doug: At the top of the next page where I attempted to move it to, I left the strikeouts. There are a series of lines that are stricken there, and they should not be stricken, that is a clerical error. That is on page 7; lines 1-8 would be un-stricken. Then we believe the amendments correspond to the suggestions made by the OCC.

Rep. Keiser: We as a state can make a determination. Do viatical settlements or life settlements get into a grey area? We have, I think decided that it's in the insurance domain.

Doug: It's my understanding that the Commissioner of Securities has been to see you about the bill. It's my understanding that she feels that the investment in a settlement is an area for appropriate jurisdiction by the securities regulators.

Jim: We have worked this deal out with the Securities Commissioner. She has no problems with the jurisdictional issues related to this bill, she had amendments that we both prepared on the Senate side, and have been agreed to by both parties, and it's a done deal.

Rep. Keiser: So, this subsection 3 is not in the bill, you're proposing to bring it back in?

Steve: Correct.

Rep. Kasper: Is the unintended consequence of adding that language back in there to not allow a life insurance company that is selling life insurance policies to be able to become a viatical settlement company?

Steve: They would not be deemed to be a viatical settlement provider by virtue of that activity.

Rep. Johnson: Is there somewhere in statute that talks about what an accredited investor is?

Steve: It is defined in rule 144A under the Federal Securities Act of 1930.

Rep. Kasper: What I think this means is that a viator, which is the company that gives into viatical settlements?

Doug: No. The viator is the owner of the policy.

Rep. Kasper: What is the reason for that?

Doug: The argument is that these wealthy, well informed individuals do not need the support, and the assistance of the state in all provisions of the law.

Rep. Kasper: So, that would mean that accredited investors, most of whom sell these policies are credited investors by the definition of accredited investor. This whole chapter does not apply to them at all?

Doug: Generally speaking, yes. The licensing provisions would apply to us; the disclosure provisions would apply to the brokers. An individual selling the policy, which is the high net worth, and by definition a sophisticated investor does not need the protections of this chapter. Now, when you say that much of the industry is in this area, you are correct that much of our industry is dealing with people who have \$10 million policies. This provision would allow them to not be protected by this law, or not be mandated to do all of these things by this law. Do you really want to get into the business of protecting these multimillionaires?

Rep. Kasper: If the big market is the credited investor, and they're trying to pass legislation to protect consumers, whether their credit is invested or not, why would we want to say but you don't have the protection?

Doug: My only argument is that traditionally these individuals, states that have known that they have an obligation to protect people who are not informed, and this is a traditional area of these people can invest in hedge funds, but they can't sell their policies.

Rep. Zaiser: I'm still not clear why you need to insert this, because whether they need protection of the state, I think everybody ought to be obligated.

Steve: My Company actually thinks this should not be in there.

Rep. Zaiser: If we include it, we're not really having equal protection under the law, and we're using means as a measurement.

Steve: Correct.

Rep. Kasper: However, this also allows the Insurance Commissioner, and the public to know who really has applied to be licensed as a viatical settlement broker, and it also allows maybe some scrutiny, if scrutiny is needed by just that narrow band of people who are selling viatical settlement products, as opposed to the 9,000 people who are licensed, so this would be maybe an easier way to track what's going on.

Doug: The first state to adopt this was the state of Maine. They were looking to simplify licenses, making it more direct, to not having 9 different licenses for activities. The states are considering reciprocity, the capacity to recognize the ND license may go to Minnesota, and visa versa.

Rep. Keiser: The problem here is really that E&O doesn't cover fraud.

Steve: I'm not going to belabor that. If you don't want to add it, we're fine with it.

Rep. Keiser: This section is going to protect the consumer. We're dealing with \$1 million policy, and if there is fraud, it's more then \$25,000 with all likelihood.

Steve: It's a damages issue. You're not talking about the face value of policy for damages, it's a concept question, so the question is how much did the consumer use, relative to how much could have gone to somebody else, perhaps. So, I think the question is do you know, and think that's going to be significant? Is it going to be much greater then \$25,000? I think that you need obviously, the protection to go against that contract, and I think you've got that under the statute. It's unlikely that you're going to have such an extreme in outcomes if there's not the competition. That's what we're trying to promote is competition in the marketplace, so that consumers actually get the best price for their policies if they want to file their policies.

Rep. Kasper: Why would this even be a concern to the companies who are selling it if this is dealing with the brokers to protect the public?

Doug: The brokers who are my members tell me that the \$250,000 provision in this state, if it goes forward will be so high that they simply will not do activities in the state. So, the consumer will not be represented by a broker, or if what I hope you be an authority of a producer to helping sell a policy, because they simply won't get that bonding. It's way above what they are required under current insurance law, and it's way above what is required in any other state.

Rep. Zaiser: Could you provide a little more specifics in terms of your members, in terms of the amendment, because I to don't really understand why.

Doug: A broker filing in for example, he has the automatic right, because he's the life producer to you. He has an errors and omissions policy appointed by \$1,000. If he makes a mistake in designing the policy, and there is unhappiness by the end of the deal, or impropriety at the end of the deal, the Commissioner has the authority to examine, unwind, beat up, and take away licenses, but also typically to unwind the transaction, and by doing that can stop the abuse. So, I think that the damages that can occur are no greater then those that can occur in the sale of a policy where somebody had an error in the policy, and it's not covered for a risk that they thought they were covered for.

Rep. Zaiser: I was talking about folks, and you were talking about members of your organization. Is there every state represented? How many have said this?

Doug: The consensus on the brokers from their leadership, and within our organization, kind of a brokers caucus they comprised upon all these comments through a few people, and they tell me that this is such a big amount of money for a relatively small market that they would be disinclined to engaging law.

Rep. Kasper: Let me give an example where I think the broker could harm a customer, that's why we need more. Let's say I approach one of clients that have a \$3 million policy, and say I have a deal for you, let's sell it. Then I say after you sell it, you've got more insurable net worth, we'll go buy another \$3 million policy. It sounds good to me, let's go ahead and do it. They sell the policy, then they apply for the \$3 million in life insurance with the new insurance company, and they find that the fine is uninsurable, because they found let's say a heart murmur. Now the broker initiated the sale, the client was expecting something that he didn't get which was much more then \$25,000. There's where I see where a broker would be liable

for that type of advice to the person selling the policy, and that's why I think you need a bigger farm.

Doug: The customer could not get any insurance, and the big bond is \$250,000 and enough to cover that, and how does the state go about reimbursing whatever grievance? I guess it would be a matter of litigation, and that publicly the policy could be unwound by the authority to purchase on that.

Rep. Ruby: Wouldn't that be considered fraud already, because you can't buy another insurance policy, if you've already sold one in ND, correct?

Doug: No, you can buy another policy. A great many of translations that are occurring involved someone who has a policy that was purchased 15-20 years ago. They are an expensive policy, and the cost in premiums are going up, and they find that by selling that policy, they can get better insurance, cheaper, and more insurance working with their agent, which is one of the reasons I support the producer authority provision. They can wind up with a much better financial situation then they had before.

Rep. Keiser: If you have a \$25,000 in California, and you need a \$250,000 here, if that's your standard.

Doug: That is the provisions of this law. Right now California has no bond, but I could anticipate a situation where California might deem it appropriate to have a bond, or to upper producer authority, but a very nicer hand would be in ND.

Steve: This is a very high standard in ND.

Rep. Kasper: I think there is a spelling error on line 15 on page 16.

Steve: Should be one.

Rep. Keiser: On lines 13 and 14, if we don't grant this general license to producers, this language just comes out?

Steve: Correct.

Rep. Keiser: Life settlements is a different kind of issue, why not give them more time?

Steve: That amount of time seems efficient for exhibits. It's operated perfectly fine up to date. There has never been any report of any problem with those provisions, so it just suddenly changes. Our concern is some of the provisions, how they will react, and sort of slow down the process of life settlements. Life settlements are a very time consuming process. It's looking at a multi month process, from evaluating to application, to analysis of the policy, to submission and review of document, completion of documents, and then to the mission to the insurance carrier. You are looking at a 3-4 month process. We're trying to point out the areas where we don't think that's appropriate, or necessary.

Rep. Thorpe: I think citizens of ND like to think things out quite thoroughly, and I believe they should have a little extra time on this type of a contract. I feel pretty comfortable with the extension on here.

Steve: I think 60 days is a very long period of time.

Jim: 30 days is standard on medic sub policy for seniors. Many companies already offer 60 days, and that is what this is patterned after. 30 days is mandated on a rescission to buy a Medicare supplement policy. A viatical settlement contract is a much bigger decision then buying a Medicare supplement policy, when you can switch companies.

Rep. Kasper: In your experience with your company, how many clients, once the policies have been made, ask to rescind within 30 days? Has anybody asked to rescind after the 30 day period that you would say sorry, you won't get your money back?

Steve: We haven't had that.

Rep. Kasper: So, therefore this might be inconsequential to the whole system?

Steve: It could be. The issue is when this actually comes up is that once a transaction has closed, and you have that rescission period, what could happen is that another provider could come in, and basically unwind that deal. They don't often disclose what they are actually willing to pay, and also commissions, how much that does pay.

Rep. Thorpe: It makes me feel more comfortable with the language we've got, because it's going to give the customer a better deal and the ultimate deal in the end, maybe.

Doug: I'm inclined to believe that people will just hang back from making offers. They'll say why even bother to engaging the market until the rescission period is kicking in, then I'll make offers that are real.

Rep. Kasper: If we keep D, line 19 where it talks about broker's compensation being frozen, what is the difference between keeping D, and striking E?

Doug: That has to do with the percentages. Probably not a lot, because we're asking for written disclosure upon request, you ask for it, and get it.

Rep. Kasper: On page 34, item number 4, the borrower has an insurable interest in the insured. Other than the loan amount, how does the borrower have an insurable interest in the insurer?

Steve: They should have an insurable interest. We don't care that they had insurable interest up front.

Doug: Your nephew may borrow money to take out an insurance policy on you, and thereby has a considerable interest, and yet it is borrowing the money to buy the policy.

Rep. Kasper: In certain instances it's correct, but the viatical settlement company is borrowing me the money.

Doug: Loaning you the money. The viatical settlement company would have no insurable interest.

Rep. Keiser: How do you certify me?

Steve: A notarized statement. I'm not buying this to engage in any illegal contract, and you require them to certify.

Rep. Keiser: This is the main issue?

Doug: This is the meat and potatoes of dealing with Stoli, as Stoli has been described.

Rep. Keiser: In working with the 3 year period, what this is trying to accomplish is for medical reasons we could, by signing the policy before 2 years, this would allow access to the medical records to determine whether this is appropriate?

Steve: Under statute the way it works is that there are very limited circumstances where somebody could actually viaticate a policy before a 2 year period. There are very limited grounds like divorce, lost your job so it caused a heart attack, and in those circumstances you want to make sure that the person isn't actually committing fraud. They won't actually allow the carrier to have access to the medical records, because if you're inclined within that testability period, they can verify what they got from the medical records.

Rep. Keiser: On line 13, if that exclusion stays in, or the or becomes a problem, and beneficiary is singular, and there may be multiply beneficiaries, children for example, so how do you clean that language up?

Steve: The strikeout at the bottom of the page, beginning on line 24 through the end is a 5 year provision that we've taken out.

Rep. Ruby: Under the prohibited practices, you're saying that this time prior to the application you have to put your influence in policy, which is subject to viatic settlement contract. Is this somehow allowing, so that at some point there is an arrangement?

Steve: What this is saying is that you can't sell a policy for 2 years. You can't have an agreement upfront to sell the policy. That is prohibited.

Rep. Ruby: So, this doesn't allow Stoli's at anytime, at a certain period of time?

Steve: By definition there should be upfront. By definition with the underlying process that occurs, there should be actually old information available at the beginning, and carrier's currently are actually taking very vigorous action, and often look at policies up front, are actually reporting, their company tells that there are public interested investors that they are actually doing this, and that they are actually no longer beneficiaries to old policies. We're concerned about arrangements from the get go of policies, where a person has an improper, has been induced, or given some other improper reason for taking a life insurance policy by the investor. Those arrangements, we believe go to the heart of insurable interest, and can be addressed, and should be addressed in policy exception. You think that you can address this partly through the consumer disclosures and certification, but we also agree that it says right here you cannot prior to the application, or issuance of the policy. Sell the policy, it's already there.

Rep. Kasper: How are you able to reach over into another area of contract law, or an insurance producer has contract with an insurance company where both parties agree to the contract, so it would have exclusion in there like this. You're saying that can't be so, and again in my instance with my broker dealer, a license and securities broker, insurance broker, and my broker dealer prohibits me from entering into a viatical settlement for anybody. I have signed my contract with them, and I'm a willing signer.

Steve: It's unlawful for an insurance company to do these things.

Rep. Kasper: So you're saying an insurance company cannot stop their brokers from selling.

Steve: Currently what happens is a lot of carriers have actually sent out bulletins, or notices to their own producers that they are not allowed to engage in viatical settlement contracts.

Rep. Ruby: In the discussion on that pre insurance, for instance could there be some advertised that would imply that they don't have to if it's financed?

Steve: Yes. There should not be advertisement that says free insurance.

Rep. Thorpe: It seems to me that we quite extensively covered the legal financing. Are we all comfortable that the laundered money isn't going to be getting in here? Are we OK that the laundered money couldn't get in here?

Steve: All financial institutions that are in the lending business are regulated entities that are subject to any money laundering provisions that are dealt with in laundering and banking legislation, or your premium finance legislation. When they created Graham Leach Bliley it was done after 911, so the money laundering issue was very bluntly expanded.

Rep. Ruby: Are you now OK with all the advertising language?

Doug: We never had a concern with the advertising language. We thought it was fine. I only required that the insurance code gives the Commissioner authority to set up rules on it, and if you want to reduce the volume of this legislation, that's an area you can do it.

Bruce Fergeson, ACLI: Support SB 2268. ACLI supports the bill as it is written, and would like to see you move forward with it without many of these substantial changes. If I might point to a couple of changes here, because it points to an overall pattern of changes that I think are being made that dilute the key consumer protections of the bill, and from our perspective, the Stoli provisions of this bill are quite important to us, and they would take out from the reach of the law many of the transactions that we think ought to be addressed, and prohibited within this piece of legislation. If you look at the changes on pages 3 and 33, they are just subtle changes, but they in affect would eliminate requirements that a settlement provider disclosed to an insurer a series of transactions that are designed to result in a viatical settlement contract. What we've seen is evidence of cloaking going on here, coaching applicants not to

respond truthfully to applications, not to give the full information about what sort of premium financing might be behind the policy, so that the company then issues the policy thinking insurable interest exists, only to find out after 2 years has elapsed that the policy is being the subject of a settlement. A solid change, but one that I think again is part of an overall pattern here. Look at the deletion of the language on page 6, the highlighted words that would be deleted from the definition of viatical settlement contract, which means an agreement between a viator, and a viatical settlement provider, or any affiliate of the viatical settlement provider. That language was put in there to make sure that the provider could not do indirectly that which it is prohibited from doing directly, and we've seen affiliations between viatical settlement providers, in fact some have relationships, or even own banks that might be doing this type of transaction. It's not the settlement provider doing it directly; they would escape the definition of viatical settlement contract, and therefore regulation under this piece of legislation. The addition of the phrase accredited investor on page 11, many of you discussed how that might be a loophole. If you look at the definition which comes from the FCC Act, it would apply to, and therefore include an individual whose net worth is \$1 million. That is a pretty low threshold for an individual to be able to be involved as a viator in these types of transactions. I'm trying to address the changes that were made, because in their totality from our perspective, they really do under mind the key fundamental purpose of this legislation which is to address Stoli transactions, and to provide meaningful consumer protections in all areas of the life settlement industry. I wanted to talk briefly about those types of transactions that were designed from the get go to result in a settlement. We would agree that those are problematic transactions, and ought to be addressed in this piece of legislation, but what we found is there are other types of transactions that don't necessarily have a pre agreement to settle, but the transaction is structured in a way that really leaves the individual with no choice but to relinquish the policy at

the end of the 2 years, or 5 years. You either have the choice of repaying the policy premiums plus interest, which for a high net worth individual on a multi million dollar policy could be several hundred thousand dollars, plus interest, or walking away from the transaction without any recourse, and those are the types of transactions that while not necessarily arranged at the get go to be a Stoli transaction really have nothing other then an economic incentive for the individual to walk away from that transaction. So, we carefully crafted a provision here that we think very narrowly focuses on those types of transactions that are designed at the inception to resolve in the settlement contract.

See handout D

Rep. Ruby: If an insurance company determines that after that period that there's a Stoli agreement that was put into place at some point before the two years, or after the 2nd year, can they deny paying out of the claim?

Bruce: I believe it depends on the states insurable interest law. For example, ND's insurable interest law says that there has to be insurable interest at the time of inception.

Rep. Ruby: So, why do we need the 5 year period then?

Bruce: I think in trying to distinguish between what a company can do, with respect to determining existence of insurable interest at the time the policy is sold, versus the 5 year waiting period where an individual, while they may be legitimate insurable interest at the time of inception, but really what's happening here is the financing is being provided by a party whose intention is to acquire that policy once either the 2 year period, or the 5 year period as last. Simple insurable isn't going to get to all of these transactions that we've seen.

Rep. Keiser: If there was non insurable interest at any point that 10 years, 20 years later they could still deny it?

Bruce: No. I think your question may be doesn't insurable interest have to exist at the time the policy is issued, verses the time the claim is paid.

Rep. Keiser: No when it was issued. So, 10 or 20 years later if there was no insurable interest, and they could document that despite the fact they had many trading agreements over the 9, the insurance company can say no.

Bruce: Correct.

Hearing closed.

2007 HOUSE STANDING COMMITTEE MINUTES

Bill No. SB 2268

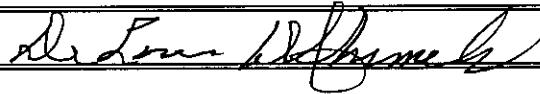
House Industry, Business and Labor Committee

☐ Check here for Conference Committee

Hearing Date: March 19, 2007

Recorder Job Number: 5268

Committee Clerk Signature



Minutes:

Chairman Keiser opened the hearing on SB 2268.

Jim Pollman presented the proposed amendment. (See proposed amendment). I would like to go to our amendments, which will relate somewhat to the amendments that were presented to you previously. Went over the proposed amendment. We had a discussion about what the OCC was accepting and what they weren't accepting. The amendments that have already been accomplished in the Senate side already accomplished what the OCC has suggested so further amending in this area is not necessary. I will again go back to the OCC letter that was sent and basically it says, we note that many of these amendments are identical or similar to those adopted unanimously by the ND Senate in its consideration of SB 2268. A bill that is similar to the model so we have already accomplished what we are trying to accomplish with those amendments so not further amending is necessary in that area.

Chairman Kesper: Because of the OCC rulings and concerns any type of financing in this bill will not be prohibited, but what your bill would do is sent up any policy that is financed would have to wait five years before the ownership would be transferred to the biotical settlement company and that is way of protecting against transactions.

Jim Pollman: I think you just asked the same question that the chairman just asked. Yes, all the financing under this bill is perfectly legal. If you start limited what financing is legal and what it is you are inhibiting the banks or other financing arms ability to lend money which you can't do because then the OCC would have problems. Continued with amendment. On page 11 a credited investor, we can't go for that. Obviously on credit investors any body that is a million dollars or more, it really takes a lot in people in ND out of the biotical settlement act. Page 11 lines 22 to 31; this goes back to the changing of the licensing structure for biotical settlement brokers. I have already made my argument in that case.

Rep. Kasper: I related to you from my clients my concerns about group life insurance. When I bid a companies group life insurance I will probably bid it to 12 or 14 insurance companies. In my commitment to my client, I will disclose to them all the offers from the insurance companies; however, during the course of my negotiation with the insurance companies I am discussing back and forth what the rate is trying to get the best rate from all the companies from my client. There are verbal things going back and forth. I might talk to Minneapolis to say if you want this case I need it at 10 cent. I stay to send me an email saying that you are going to ten cents. I would be happy to disclose my final best offer, but I certainly don't want to get into the position where I have to disclose every verbal offer during that process until I get to the final best offer. So if there would be some way in here where we would disclose the final best offer, even if it is verbal, as opposed to having to try to figure out all these verbal offers that may be the end result of the best offer. I am concerned the brokers will be so confused at the end they won't know where they are in this whole process.

Jim Pollman: I think the customer or consumer should have all the information going in. There aren't that many offers that are out there. They may be conflicting offers but I think if the

consumer has as much information as possible before selling off their death benefit they should have it.

Rep. Kasper: How do we know for sure the verbal offer is a good offer unless you have something in writing?

Jim Pollman: I guess that is a question for the broker. The bottom line is does the broker know that is the best offer to give to the consumer so I think it plays on both sides. We need to put guidelines in state law how everyone should do business.

Rep. Boe: We talked about the New York accusations. When emails went out and said with a co brokering fee I won't throw an offer in; how does this law protect the consumer in an instance like that?

Jim Pollman: First of all the company would be required to disclose all related third parties that they are dealing with on this particular contract so the customer would have the information that others may be involved in compensation or other pieces. In the New York case the company was accused of paying off somebody else not to specifically provide an offer that may be competing against this particular companies offer. The amendments proposed last week changes the five years back to two years and there are many different sections in here that make those changes that we don't think are appropriate. Went through all the remainder of the amendment. Also we do not think brokers should not be able to contact clients on the phone and ask them how healthy they are and when are you going to die. We think brokers should not be contacting the folks that sold their policies to check on the status of their health. That piece we thing should be left in there on page 38.

Rep. Kasper: On page 43 #3 what are you saying you want and what are you saying you don't want on that?

Jim Pollman: Our amendment accomplish the following: If you look at the last piece of that, engage in any transaction act or course of business or doing what is fixed limits or impairs in any way the lawful transfer of ownership, change of beneficiary or assignment of a policy etc. We agree with keeping that in and our amendments accomplish that.

Rep. Kasper: Could the commissioner put together his engrossed bill with his amendments and what he wants in the amendments and what he wants out so we could see in a copy like the biotical settlement companies gave us in the bill in the form he would like.

Chairman Keiser: What we want is the senate engrossed bill, put in his amendments and note these are my suggested amendments and their placement and then also put in the amendments proposed by the biotical people and bracket them or do something so that we could see the entire bill with both sets.

Rep, Kasper: Yes, I know it is a lot of work, but that would sure make it easier for me.

Jim Pollman: How about I offer a compromise. We highlight in the engrossed bill our amendments and then you can compare it to the piece that was handed out last week?

I will work with legislative counsel to produce this bill so that you can follow the bill better.

Rep. Nancy Johnson: There is another minor correction to be done.

Chairman Keiser: Color code so that changes can be recognizable.

Hearing closed.

2007 HOUSE STANDING COMMITTEE MINUTES

Bill No. SB 2268

House Industry, Business and Labor Committee

☐ Check here for Conference Committee

Hearing Date: March 20, 2007

Recorder Job Number: 5324, 5350

Committee Clerk Signature



Minutes:

Chairman Keiser reopened the hearing on SB 2268.

Jim Poolman: Handed out a new graph and a new set of amendments. (See first engrossment engrossed SB 2268). That set of amendments makes a couple of minor changes. I will talk through and show you the areas of disagreement. Basically in the pink color are areas where both sides have agreed. The area of yellow is where the life settlement companies and other interested parties that have offered amendments want to continue to pursue those amendments. The area of blue is areas where the North Dakota Insurance Department has amended the bill and we continue to pursue those amendments. Those amendments are still included in that packet of amendments. Page #5 you will notice the word or is in blue, everything else has been accepted by both sides. Then we go to the bottom of page 5 and we have some language on the bottom of five and six in relationship to the definition of a special purpose entity; go all the way to page 27 and that is where we get into the decision of periods of time where a consumer can change their mind. One is the disclosure of those and the other is the actual rescission period. Then we move on to page 29; the intent of this piece is to get after some of the allegations in this picture and basically the third parties that we are dealing with. If you decide to take our amendments and then take

other amendments, we would in turn agree to that amendment today on page 29 that is yellow. We believe that basically the content that is closest to the consumer is already addressed by the broker and the broker's compensation. So we would in turn agree to that. Then I would go to page 34; we have a disagreement to the disclosure to the insurer so you notice that is in yellow and that is one of their amendments. Page 36 is the rescission period that the settlement companies would like to continue to pursue in reducing that. Then we get into the heart of the five year vs. the two year period and we have discussed that to death. On page 39 the exceptions and the hardship provisions as you will see we have in blue, at the chairman's concern taken out; the viator vs. spouse and the viator retire. The settlement companies want to keep that in and the settlement companies want to add a couple other hardship provisions that are also in yellow that we have not agreed to. Page 40 the settlement companies want to take out #3 and we have not agreed to that. Then we get into a whole bunch of pink. That is the entire advertising section that we are pulling out of the bill to be able to promulgate by rule and regulation the pieces of advertising that would be regulated by the insurance department. The effective date on page 56; we could not agree to that date. We don't think this should be a pre-pass for all insurance policies that are issued before the effective date. So that is it.

Rep. Kasper: This is the end bill you would like to see the end product. Your amendments are to the engrossed bill. This is an example just for our purposes, but we would not amend the sample, we would amend the engrossed bill.

Jim Poolman: Yes, that is absolutely right. As you will notice the engrossed, but color coded bill is not the engrossed bill because there are other pieces of language that are not officially in the bill added to it.

Rep. Clark: Just for my knowledge, as far as all these amendments has it been equal 50-50 in agreement?

Jim Poolman: You might get a different opinion no matter who you ask. Let me give you my opinion. I thought we started off with a very good product to put in front of you to protect the people in front of you to protect the people of ND in the life settlement business when people want to sell their policy. I think those are still there and I think the bill will continue to protect ND consumers. I agree there is a legitimate secondary market that provides value to consumers but they just need the consumer protection and those are still in the bill.

Tom Kelsch: On the yellow on page 5 & 6? When we sent over our changes we indicated we do not know if we are opposed to this language, but we don't just understand what it means? Who is that covering? That doesn't need to be stricken out.

Jim Poolman: The reason it was put in there to not provide a loop hole for defining this viatical settlement provider so it can not be used by a provider to circumvent the law.

Rep. Johnson: On page 6 should the lines not be through it and they remain in?

Jim Poolman: The yellow pieces of it is what they would like stricken so now that the explanation has been given again, then the lines would be taken off and definition would prevail.

Rep. Kasper: Line 3 page 5 delete all of subsection e you don't need an or there. It is not a dispute.

Tom Kelsch: Concerned about the time period and it takes time. We think the 15 and 30 days is sufficient. (See proposed amendments #1)

Rep. Kasper: We discussed the possibility here to solve the float problem of setting up a trust account that would hold the funds and the viatical settlement company would keep the

earnings of the trust account until it was actually delivered to the person you had in the policy?
Is that still something that might work yet for the viatical companies?

Tom Kelsch: I think that would work.

Rep. Keiser: Discussed time period and how it should be handled.

Tom Kelsch: There will be disclosure of what the broker makes on the deal, what the rider makes they may not make it until 6 months later or a year later when they actually sell their product to somebody else or until the person passes away. All the disclosures and for the consumer protections we agreed to. We do have a concern about what fully disclosed means and we think it goes beyond everything. Who is it protecting? Is it a way to find out how we operate our business and get our trade secrets information so they get a competitive over our companies? If you feel there has to be some type of disclosure we feel that it should be more narrowed; not to every transfer of a policy within five years, but will limit it to how you define the holder in this case. In this disclosure there is no limitation. We think the information should be tied back to a specific contract within the first two years and maybe the disclosure should be limited to what you are really trying to get at.

Rep. Keiser: Maybe the disclosure should be limited to what you are really trying to get at?

Tom Kelsch: If we disclosure it to the insurer that likely in some cases provide the opportunity for the insurer to go back to their client and say is there some cash value here or there are other alternatives. There is a period of time so the insurer can go to their client that is insured and say we may have a better deal for you and make some type of offer. What information do they need to know from us? On 36 it is just a continuance of the 30-60 days. 38 is the 2 and 5 year and that is one we haven't been able to agree on. Went over pages 38 and 39.

Rep. Ruby: To go back to the 2 year and 5 year difference; is there any way that we could sell it in two years, but it can't be operational for five, the sale? So as a consumer I have a right to

sell it in 2 years plus, but for 5 years, they can recover their money. But for 3 years if there are investors invested, they are at risk. I am trying to find a way for consumers to have a right for property to sell it, but then also to protect against things?

Rep. Keiser: You heard one of the comments yesterday from one of the life providers. They indicated if you pass this what may very well happen is you might have a situation like that where a company may finance the premium payments, but instead of financing it for two years, they may finance it for five years or take a loan out for five years. Then it could be transferred under the current bill and the affect of that might be that the insured may get less money at the end of five years than they would of at of the end of two years because the provider would have paid in five years of premiums and interest and gotten it back.

Chairman Dosch: If all parties could agree so that you could actually sell it in two, but it would not be operational for five. I want to know how. So we strike up a deal where you buy my house today, but I get to live there for three more years? When you move you get that back.

Jim Poolman: The companies have looked into that and their concern is that if you go to five years and there is a look back to that five years you have basically moved the period of contestability of that policy for five years so a company may enter into some sort of financing of the premiums for that period but probably won't enter into an actual contract until that five years would be up. That is the concern.

Rep. Keiser: Discussed page 40 (1) and (2). So you are not being prohibited when the five years are met. Am I correct?

Jim Poolman: Then you have to add the (3) one in which we struck, that even if you bought your policy and paid cash for it, but in two years you had your policy or you yourself evaluated for settlement you couldn't sell it within the five year period. All three of those requirements have to come into play.

Rep. Kasper: Go back to page 38 on line 23 I think that is what we are talking about. It is in violation of the statute for any person to enter into a viatical settlement contract at any time prior to the application. We don't have a problem with that, but it says or within a five year period so you can't enter into a viatical settlement contract before the policy application and we have no problem with that. When it says or within a five year period. That is where we are saying it is going beyond just a solely situation because you could take out a policy and buy it yourself and pay cash for it and you can't sell it within five years; if within two years under 3 on page 40 you have been evaluated for a settlement. So you could have a legitimate one where you are paying cash on your premium, and then you check with your agent they check for you and now you are barred for five years from selling it. If 3 on page 40 are stricken, then on page 38 we are a little closer to what you could live with?

Tom Kelsch: If your policy has not been funded exclusively with unencumbered assets, including an interest in the life insurance policy being financed under subsection d (1) lines 8-13 within the first two years of your policy, then if you borrowed money that wasn't exclusively that then you would again fall within that five year period.

Jim Poolman: Will you know more in two years or five years?

Tom Kelsch: In five years it doesn't matter because you can do anything you want to. There was a lot of discussion on the time period. All the changes in 42-48 those are on advertisement and that is up to the committee. We are in agreement, if you want to take them out and let the commissioner do it or leave it in there that is in the original bill, which ever the committee prefers policy wise. On Page 56 our concern with the effective date of this is if somebody does have some type of a contract with an individual on their policy and this law would come into affect and basically prohibit the selling of a policy for a 5 year period there

could be a gap there that could impact current contracts or current agreement with people and so our request is that that be effective now.

Rep. Steve Zaiser: All the disclosure and everything else in the bill does not apply to policies that are already in force and that to me is totally unacceptable. This bill is also consumer protection. So saying any old policy after this date isn't covered by the bill and that is not logical.

Tom Kelsch: I would agree on that. My concern is I think the disclosure should apply if there be any way to convert over from the two to five on existing policies. If you have laws that are retroactive to whatever, the concern with this industry is when is the affective date when you enter into a contract and if later you do sell and the sale didn't happen yet, so is it when the sale happens or when it is the original contract? Generally you can't affect the original contract.

Robert Harms, Imperial Trading and Finance: (see Proposed Amendments to Engrossed SB 2268 #2). Went over the proposal.

Chairman Keiser adjourned

Chairman Keiser reopened the hearing on SB 2268. Job #5350 lets try to work with the official color coded copy that was handed out today. I am not sure the amendments apply to it but that is OK. We received this afternoon two special amendments; one which I labeled the Kelsch amendment, (testimony #2) and (testimony #3) to go over. I would suggest we take the color copy and the committee walk through it. Went over color coded amendment proposal and decided on changes.

Rep. Kasper: I got an email from Pullman that says the law doesn't need to change to do that. Each viator settlement company could require it as part of the contract that the funds be placed in escrow since they can do it with a settlement contract. When they enter the agreement they

are going to have to take the million dollars and put it someplace and reserve it. If they have to give it to the person then obviously they have to give them a check in hand. If you put in an escrow account you don't have a check in your hand. What I am saying is you apply for a policy you got a viatical deal in place, you got a stoic and if that is going to occur prior to the time the policy is issued or during the five year period that the policy is in issued from the date of issue the viatical settlement company must notify the insurance company that this is what is going to happen.

Rep. Keiser: Maybe that should say prior to the issue of the viatical settlement or transaction or series of transactions the viatical settlement broker shall disclose to the insurer?

Rep. Steve Zaiser: What does fully disclose mean? That is a pretty wide open arena there. Do we need to define that further?

Rep. Keiser: There is another section in the bill that says they do inform the insurance company if the client if they plan to do something. Is the intent of this section that I am going to inform them I am going to buy some ones policy? I know they already have to tell the insurance company if they plan to do something. Is that what this section is?

Tom Kelsch: In the following section 09 general rules; after the fact, it does require under b within 20 days after the buyer signs the documents, then they have to be provided to the insurer and in c talks about what needs to be provided there. If the committee wants to give some type of notice to them we did craft a better definition.

Jim Poolman: When disclosing a plan or a series of transactions that include financing, the purchase of a policy and specifically turning around and then making the agreement to vitiate a policy that is the disclosure we are trying to get at to the insurance company. In no language in this particular amendment requires the disclosure of commissions or any proprietary information.

Rep. Kasper: If the language were modified to read on line 13 prior to the initiation of a viatical settlement offer and or acceptance the transaction or series of transactions or the plan?

Jim Poolman: All these transactions would take place before the actual viatical settlement would occur so that is why you do it up front when the policy is being purchased because there is a plan set out to accomplish all these different transactions to get the policy purchased and the agreement put in place.

Rep. Keiser: I think you are asking for a whole lot more information and I think it is pretty encompassing. Any transaction that occurs has to be disclosed?

Rep. Kasper: The bill allows stoic if they wait five years. So this would say tell us up front how it is going to work so we know right now at the point of application. So we take that into consideration on our underwriting guidelines for this life insurance policy.

Rep. Boer: With this knowledge the insurer, can they deny me the policy based on knowing that I was intending to sell it?

Rep. Keiser: Sure.

Rep. Steve Zaiser: Are we talking around stoic, maybe we should be just a little more forth right and talk about a stoic there?

Rep. Steve Zaiser: This would be a means why which you could monitor these plans.

Jim Poolman: I think your right. This is an attempt to handle it. How would you keep track of all these things and monitor these plans? We are trying to do this bill to have the insurance companies know that they transactions have taken place.

Rep. Steve Zaiser: This is giving information to the insurer to allow them to manage their business because they can't currently manage their business now because those transactions are hidden.

Rep. Kasper: I have some amended language right there I want to throw out. Prior to the initiation of a viatical settlement plan a viatical settlement transaction or a series of viatical settlement transactions or viatical settlement provider shall fully disclose to an insurer the details of the plan, transaction, or series of transactions in writing to which the viatical settlement...did you get that Jordon? I just wanted to throw it out to see if it destroys or disturbs?

Tom Kelsch: (see proposed amendment #1) while is waiting to get the other one drafted. We are concerned about the fully disclosed for us and if we are financing it through some other company with our money then is that something we have to disclose to them as well? With our amendment we would disclose, if we have a plan to originate or finance a life insurance policy we have a duty to disclose that to the insurer.

Rep. Keiser: When would you have a plan. What is your definition of a plan?

Tom Kelsch: It would be when ever we have the contract or agreement with the insured to either finance it or originate a policy that is when our duty to disclose it to the company is.

Rep. Kasper: If there is a plan finally put into affect does the insurer sign the document and say I agree to the plan or is this a verbal plan?

Tom Kelsch: We are talking about a couple of different things there. Some of these are not just in the origination so if you have a policy for three years and I wanted to buy that policy I would have to make this disclosure right now to your insurer. When will I have to make that disclosure, right now it says I would have to disclose that to the insurance company. I may have a financing agreement to finance your premiums and I would have to show you that. Then if I later bought that policy within the 5 year period, I would have to disclose that to the insurance company as well.

Rep. Ruby: Why did you put the word program in there? Why didn't you put the word agreement in there?

Jim Poolman: If the idea was trying to do this as a number of transactions our main concern is why do you disclose it and that it should be applied to the origination or the financing of it. Not necessarily for the continuing of a policy.

Rep. Keiser: I think the problem is you are trying to do a lot in these two paragraphs. We are trying really to do two things and I get confused because of the way it is written. I have the policy already, I own it and it is on me and I have had it from 1, 2, 5, or 10, 20 years, it doesn't matter how long I have had it. At some point I want to sell it, the language here that we expect for disclosure for the insurance company under that situation, if I have owned it for two years and it meets all of our exceptions, then I sell it, should the insurance company be informed?

What the commissioner has expressed and what the committee members have expressed a concern about are what about plans that I now go to Rep. Ruby and say I really want to sell you \$10 million and I want a new premium financing and a whole bunch of other things and what rights does the insurance company have as the underwriter to know that all those things are going on ahead of schedule? That is way different than the plan on me. This section to me gets difficult because it kind of is trying to address both. I do think we need to have disclosure to insure part a and part b. What disclosure do we want and what is appropriate if I have owned the policy. Legitimately there is not a stoic involved.

Rep. Dosch: If you owned the policy already when do you sell it and if you sell it, then the insurance company has to be notified so the ownership of that policy changes. So at that time they are automatically notified in order to transfer ownership so I think that will be taken care of. It is when at stoic is involved before the issue a policy that the insurance company should

have the right to know that there is not an insurable interest and there is a stoic interest. Can I do this within five years without all this disclosure?

Jim Poolman: Not all policies are new policies. Rep. Steve Zaiser may have a million dollar policy and may be approached to say lets increase the value of that policy to five million dollars and then we will finance the difference in premiums on that policy. You have initiated a stoic transaction and Rep. Dosch is absolutely right in the fact that Rep. Keiser wants to sell his policy the disclosure is already made because he had to change the ownership of the policy.

Rep. Kasper: If we go along the lines that you are suggesting then could we state on line 18 after issuance of a new policy or increase the amount of an existing policy and just spell it out.

Rep. Ruby: In a normal two year period with a legitimate life insurance policy that is paid for by the insurer would be included in this? On page 4 of this bill it lists the provisions that are acceptable for the two year period. Under the two year policies if the following conditions are met etc. I was wondering if that doesn't cover this.

Rep. Keiser: To do it legally, not a stoic does this mean we have to disclose all the details of the insurance company?

Rep. Steve Zaiser: How do we track this and what point in time would you enter into this prior to the consumer of the policy, only after they said there is a problem, or would you be actively tracking these things?

Jim Poolman: The information is given to the insurer so they know how to react to the transaction. You buy a policy and are paying the premiums yourself you wait the standard incontestability, under the bill as it stands, if you were to sell your policy to the secondary market, the secondary market would notify the insurer that the ownership of the policy is changing hands, that meets the disclosure on a non stoic transaction the way the bill was written. If there is a plan to finance the policy, to increase the value of the policy or to change

the policy in any way, to not use your own assets the company ought to know that so they can react to that policy to charge the appropriate premium, if they wanted to reject the changes to the policy because they know that policy is a stoic policy, and then Rep. Steve Zaiser, if the company had a problem that the life settlement company was violating the law in its disclosure, they could work with the insurance commissioner to be able to make sure the company was following the law and to make sure both the insurance company, the producer, the broker, were all protected in the transaction.

Rep. Keiser: I would agree 100% with that. So I have a million dollar policy, they want to continue the policy they buy it from me and make the payments and three years into the policy.

Jim Poolman: Under that scenario you just laid out you have the ability to turn around and sell that policy right now because you have got the ability then sell that policy under the current statute as the buyer.

Rep. Keiser: I understand that, but this now requires that disclosure of insurance as required under law.

Jim Poolman: Actually under the bill as it stands, even with this language in there, the disclosure to the change of ownership, which is the plan to change the ownership of the policy to the viatical settlement company which is licensed under this bill even as this language is drafted.

Rep. Dosch: What if you put all non priority, fully disclose all non priority information, wouldn't that solve the issue?

Jim Poolman: The insurance company should not know that a viatical settlement company has paid somebody a certain amount of money to do this transaction. I think if it helps calm the fears of the committee that it accomplishes what we are trying to do I say go for it.

Rep. Kasper: (see proposed amendment #2) Read the amendment into the context of the bill.

I don't know if that is redundant or not.

Rep. Amerman: Listening to the 37 amendments that have been presented just on this one section, I like the language as it is. Just disclose a plan, a transaction or a series of transactions. It doesn't say anything that you have to disclose commissioners or anything like that. I think we should leave the language like it is.

Motion Made By Rep. Dosch, Seconded By Rep. Johnson to adopt an amendment to insert non proprietary information to and insurer plan and to remove the overstrike.

Discussion:

Rep. Steve Zaiser: I think it does make it a little clearer. We have to be careful not to amend it too much.

Rep. Donald Dietrich: It is discretionary how you want to read and I think that will be a problem.

Vote: 8 Yes 5 No 1 Absent **Carrier: Rep. Kasper**

Went over the rest of the bill and the changes they needed to make.

Jeff Poolman: This section is actually in current code, but the bill takes it out.

Motion Made By Rep. Boe, Seconded By Rep. Dosch to reinsert Subsection 7 in the appropriate lines. (On page 39).

Rep. Dosch: If I have a policy and lose my job or get laid off and I can't continue on with my premium wouldn't that be reasonable that I am able to sell my policy?

Jeff Poolman: That is the public policy that you are facing. When we put the bill in we thought it was way too subjective under a transaction that created a loop hole. If you folks decided this is important, I am OK.

Rep. Boe: How long has this been on the books?

Jeff Poolman: The first viatical settlement model act was in 1999 and then we amended it again in 2001.

Rep. Boe: So in the past you have never had to define it?

Jeff Poolman: In my 6 ½ years of being insurance commissioner we have never been confronted with the issue of hardship as it relates to selling the policy in the secondary market for the particular hardship.

Vote: 4 Yes 9 No 1 Absent Motion to adopt failed.

Discussion:

Continued to go over the bill.

Jim Poolman: On lines 18 & 19 remove the overstrike so you can talk to them after the policy is issued. You can't talk to them before the policy is issued. We had a concern this was too broad and this clarifies it. It also preserves the property rights of the owner of the insurance policy. When you buy a policy in that two year period. All of a sudden at the end of two years I want to sell my policy and it wasn't stoic, at the beginning you say you were not evaluated when you bought the policy and during this two year period so it preserves and protects the owner's right to sell the policy.

Motion Made By Rep. Kasper, Seconded by Rep. Zaiser

Chairman Keiser: Further discussion of this amendment.

Discussion: None

Voice vote passed.

Chairman Keiser: On page 56, this chapter shall apply only to life insurance policies issued on or after the effective date. It is not on the original bill.

Rep. Kasper: We are providing consumer protection so all offers are going to be disclosed to the consumer if he or she wishes to sell their policy and all compensation has to be disclosed

to the consumer or seller. If you put that language in any policy that is currently in affect from the affective date of this bill would not have that protection.

Tom Kelsch: Rep. Kasper made that issue and our folks proposed an amendment. We limited the effective part for that provision to 2-5 prohibited portions so all other provisions of the disclosure and consumer information would apply if the committee would do this.

Rep. Keiser: Committee what are your wishes. Seeing nothing I am going to go back from 2-5 years. Rep. Johnson and I met with Senator Kline and Hacker at lunch time and went over the amendments (see proposed amendment #3). Sen. Hacker is working with Rep. Nancy Johnson to draft a new set of amendments and if they do that we can concur instead of go to a conference committee.

Rep. Kasper: The idea was to create an escrow provision where the money would be held in so that is in two different sections of the bill where that is provided. The first is on page 27 of the colored copy version that you have. In this case, the previous was 60 days after the contract was entered into, this is changing it to 30 days after the contract was executed. The money is going to be deposited into the escrow account and the receipts showing the properly completed transfer of ownership, the date when the buyer gives notice so basically they are telling them they want to then receive the proceeds. (Reading the rest of the bill, very quiet)

Rep. Keiser: There was a debate between 15 and 30 days. 30 days after the signing of the agreement, and 15 days after receipt of the money, was the deadline for the individual to rescind the contract. The commissioner's proposal had 60 days after the lesser of 60 days after the signing of the contract or 30 days after receiving the proceeds on which to rescind the contract. The lesser of those two dates. The money will be put in an escrow account and stay there until the individual indicated that he wanted to receive the proceeds. They would have

30 days after the contract was signed by all parties or 30 days after the proceeds have been sent to the viator.

Jim Pullman: I think your right. This is an attempt to handle it. How would you keep track of all these things and monitor these plans?

Rep. Amerman: This is a 50 page bill. I liked the bill as it came originally. What comes out of here we do not get to walk away from. I like the 60 and 30 and that is where I am at.

Rep. Kasper: I think we should give them more time to get the amendments ready. The five year period is the crocks of the whole bill. We heard from all the representatives. They are not in the business of stoic; the five year period makes no difference for their business because they are not doing what the 5 year period helps to slow down. I would hope that we could wait and do this tomorrow after something is drafted.

Rep. Keiser: Is there any motion to go to 2 years? Is there any motion to change the 15 30 and 60 days period?

Rep. Boe: What about 45; compromise?

Rep. Amerman: The escrow, according to the commissioner it is my understanding through a contract they can do that already. If we put the escrow into statue do they have to go into escrow?

Rep. Keiser: No, but it would also affect the timing issue.

Rep. Kasper: I think with the amendments we have already adopted Commissioner Poolman did come in with amendments that we have not seen. These amendments conflicted with the actions we have taken so far.

Rep. Keiser: What are the committee's wishes? Decision made to come back tomorrow.

Hearing closed.

2007 HOUSE STANDING COMMITTEE MINUTES

Bill/Resolution No. **SB 2268**

House Industry, Business and Labor

☐ Check here for Conference Committee

Hearing Date: **21 March 2007**

Recorder Job Number: **5405**

Committee Clerk Signature



Minutes:

Chairman Kaiser opened discussion on SB 2268.

Tom Kelsch distributed a proposed amendment. (See #1—Changes are highlighted).

Chairman Kaiser: On page 28, that would provide a loophole to circumvent the 30 and 60 days.

Kelsch: If you want to take that off, that's fine. We put that in there just for the idea if the viator didn't want it.

Chairman Kaiser: You are comfortable with the 30 and 60 days.

Kelsch: Yes, because the funds are going into an escrow account rather than the viator and the viator wouldn't be able to get it until either 60 days after the contract was done or 30 days after the money was in the account.

Representative Ruby: The language on the bottom of page 37, is that right?

Kelsch: That (later to occur) should be crossed out so it should be "expiration of the any then remaining rescission period." Thank you for catching it.

Chairman Kaiser: On page 27, line 23; you have misspelled "rescission." Mr. Poolman, does this sound right?

Jim Poolman: It sounds reasonable. We think it takes some consumer rights away but if it makes the Committee more comfortable, we are happy to go along with it.

Representative Zaiser: Could you explain what rights it takes away?

Poolman: We believe that the money should actually go viator and not mandate an escrow.

Again, we will go along with using the escrow.

Representative Kasper: I think this is a good compromise.

Representative Zaiser: I Move to adopt the Amendment, not including any portion on page 38 reference to the escrow.

Representative Nottestad: I Second.

A roll call vote was taken: Yes: 12, No: 1, Absent: 1 (Thorpe)

The amendment is on the bill.

Chairman Kaiser: Let's go through the insurance department's new set of amendments.

(The David Marks amendment—Attachment #2). These are amended to the engrossed bill.

We are going to have to work with both as we go through this. We're not going to take a vote on each line; we'll just make a check mark. (The Committee went through each line of the amendment inserting the changes to their mark up copies.)

What happens when the spouse dies, but the children remain? Should they have some review before that policy is sold? That's a question for the Committee.

Representative Johnson: In the beneficiary area. I think it's okay to have that in there.

Chairman Kaiser: The one situation I can see is if two people both have a high income buy a policy and you lose one half of the income, you might want the money from that policy to support the family. You couldn't sell it within the two-year period. These are in the exceptions. What are the wishes of the Committee on this one? Keep it in or take it out? If no one feels strongly about it, we'll leave it in. (The Committee continued through the amendment.)

The next question is on page 34, the addition of "The viator divorces a spouse."

Representative Kasper: I think we should leave it in. (There was no disagreement.)

(The Committee continued through the amendment in an unstructured discussion.)

Chairman Kaiser: Committee members we have the Insurance Department's amendments before us (#2). What are the wishes of the Committee.

Representative Kasper: I move the amendments as discussed.

Representative Johnson: I second.

A voice vote was taken. The amendment was adopted.

Chairman Kaiser: We have not yet discussed Robert Harms' amendments. (Attachment #3)

Robert Harms: Do you plan to take up the 2 yr and 5 yr issue after we do these amendments.

Chairman Kaiser: We discussed that at some length yesterday and a Committee member makes the motion to change from the current engrossed bill.

Harms: I will work off the first engrossment of the bill. I will try to point out some things we would like the Committee to consider. (He went through his amendment.) The definition of fraudulent viatical settlement, it's a subtle change but we think that's it's overly broad and it impacts employees of viatical settlement companies. It includes "or permits its employees or its agents." We're concerned about the impact to the employees of the company.

Chairman Kaiser: We have to look at this in its totality. Any one in the organization who knowingly intend to. . . I don't see the problem there. It's broad, but we want it to be broad.

Harms: That was our concern that it is broad. We think that there is a subtle implication to the employees. We understand the "knowingly" requirement. If you are a regional manager or a district manager, or a staff person working for that kind of manager do you caught up in that kind of language.

Chairman Kaiser: Again, I just want it on the record that is our intent. I don't care at what level you are at. If you know there is fraud going on, you are liable.

Harms: Some provisions listed are a bit punitive and they tend to hurt the market itself in ND.

Another recommendation we have made is on page 3, line 9, where you can't be presenting

any information with respect to how premiums are paid on an insurance policy. We think that is the kind of thing that is problematical.

On the bottom of page 29, we are asking that remove lines 3 and 4 relating to disclosure. We just think that invades the private business relationship the provider and the purchaser that isn't really warranted.

Chairman Kaiser: Let's say I have 10 life expectancy certifications, what this says is that the one that I use, not the ten of them, have to be disclosed. Doesn't it?

Harms: I would read it the opposite of that. It says "disclose all the life expectancy certifications obtained by the provider in the process of determining the price. . ." That's one area that we think gets into private business acts and is not warranted.

On page 2 (of the amendment) we have the same kind of concerns. We are asking that you delete lines 20 to 23. In the middle of the page I would bring to the Committee's attention. Relating to the advertising, we didn't agree to the removal of the Insurance Commissioners recommendations. We didn't agree to those changes on the advertising section. What we think is the better policy is that the Legislature directs the policy with respect to advertising. We recommend that you delete that language.

On page 48 (of the bill), we would ask the Committee to consider the higher penalties presented in this amendment. Those in the original bill are pretty thin.

Representative Zaiser: I move we adopt the Harms amendment relating to the penalties on 26.1-33.3-14.

Representative Boe: I second.

A roll call vote was taken: Yes: 2, No: 10, Absent: 2 (Thorpe and Johnson)

The amendment failed.

Chairman Kaiser: Are there any further amendments to be considered?

Page 5

House Industry, Business and Labor

Bill/Resolution No **2268**

Hearing Date: **21 Mar 07**

Kelsch: Yesterday Commission Poolman made a recommendation and I don't know if it was adopted. It would be on page 40 of the marked up version. It would be on page 35 of the engrossed version, where he requested to add in the language "in connection with the issuance of a policy."

Chairman Kaiser: We captured that. It's on the bill.

Representative Kasper: I Move Do Pass SB 2268 as amended in our discussion.

Representative Zaiser: I Second.

A roll call vote was taken: Yes: 11, No: 2, Absent: 1 (Thorpe)

Representative Kasper will carry the bill.

#1

March 19, 2007

PROPOSED AMENDMENTS TO ENGROSSED SENATE BILL NO. 2268

Page 2, line 1, replace "hypothocating" with "hypothecating"

Page 3, line 18, after the semicolon insert "and"

Page 3, line 20, remove "and"

Page 3, remove lines 21 and 22

Page 4, line 21, after the semicolon insert "or"

Page 4, remove lines 22 through 25

Page 6, line 6, replace "contact" with "contract"

Page 7, line 20, replace "on" with "one"

Page 9, line 19, after "policy" and before the comma insert "that has been or will be the subject of a viatical settlement contract"

Page 11, line 12, after "fee" and before the period insert "for a provider license and a two hundred dollar fee for a broker license"

Page 12, line 10, replace "two" with "one"

Page 12, line 16, replace "two" with "one"

Page 12, line 20, replace "paragraph" with "section"

Page 12, line 25, remove "shall be in the favor"

Page 12, line 26, remove "of this state and" and replace "commission" with "commissioner"

Page 14, line 15, replace "on" with "one"

Page 14, line 27, remove "At the commissioner's discretion, the commissioner may"

Page 14, remove line 28

Page 23, line 29, after "settlement" insert "provider"

Page 26, remove line 1

Page 26, line 2, replace "during the transfer process, and if so, provide" with "Provide"

Page 31, line 30, replace "an absolute" with "a"

Page 34, line 13, after the semicolon insert "or"

Page 34, line 14, remove "The viator divorces a spouse."

Page 34, remove line 15

Page 34, line 16, remove "(5)"

Page 35, line 10, remove "or other party entering into a"

Page 35, line 11, remove "viatical settlement contract with a viator"

Page 36, line 19, replace "No viatical settlement provider shall enter into a viatical settlement contract unless" with "It is unlawful for an insurance company to engage in any transaction, act, or practice or course of business or dealing which restricts, limits, or impairs in any way the lawful transfer of ownership, change of beneficiary, or assignment of a policy to effectuate a viatical settlement contract."

Page 36, remove lines 20 through 30

Page 37, line 1, remove "The purpose of this section is to"

Page 37, remove lines 2 through 14

Page 37, line 15, remove "2."

Page 37, line 24, after the period insert "The commissioner may adopt rules to implement this section."

Page 37, remove lines 25 through 30

Page 38, remove lines 1 through 31

Page 39, remove lines 1 through 31

Page 40, remove lines 1 through 31

Page 41, remove lines 1 through 30

Page 42, remove lines 1 through 15

Renumber accordingly

PROPOSED AMENDMENTS TO ENGROSSED SENATE BILL 2268

Page 30, line 1 after Insurer. Delete "Prior to the initiation of a plan, transaction or"

Page 30, line 2 delete "series of transactions", capitalize "A", and delete "fully"

Page 30, line 3 delete ""plan, transaction, or series of transactions," and replace with "program"

Page 30, line 4 delete "renew, continue,"

Page 30, line 5 delete "engaging in the business of" and replace it with "entering into a" and replace "settlements" with "settlement"

RENUMBER ACCORDINGLY

Proposed amendments to SB 2268
For Rep. Kasper
V.1

Page 34, line 13, after "a" insert "viatical settlement" and after the underscored comma insert "viatical settlement"

Page 34, line 14, after "of" insert "viatical settlement"

Page 34, line 15, replace "a" with "the details of the" and after "transactions" insert "in writing"

PROPOSED AMENDMENTS TO ENGROSSED SENATE BILL 2268

Page 25, line 14 after, remove “including the amount “

Page 25, remove line 15,

Page 25, line 16 remove “includes”.

Page 30, remove lines 1 through 7.

Page 33, line 29, replace “five” with “two”

Page 34, line 2, replace “five” with “two”

Page 34, line 6 replace “sixty” with “twenty four”

Page 34, line 11 replace “five” with “two”.

Page 34, line 16 after (5) insert:

“The viator was the insured’s employer at the time the policy or certificate was issued and the employment relationship terminated:

(6)”

Page 34, line 18 after the semi colon insert:

“(7) The viator experiences a significant decrease in income that is unexpected and that impairs the viator’s ability to pay the premium; or
(8)”

Page 34, line 19 remove “c.”

Page 35, line 5 replace the semicolon with a period

Page 35, remove lines 6 and 7.

Page 49, line 13, after the period insert:

“Section 26.1-33.3-10. Prohibited Practices shall apply only to life insurance policies issued on or after the effective date.”

RENUMBER ACCORDINGLY

Date: 3-20-07
Roll Call Vote #: 1

2007 HOUSE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. SB 2268

House Industry Business & Labor Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken adopt amendment insert non proprietary after disclose
Remove overstrike

Motion Made By Rep. Dosch Seconded By Rep. Johnson

Representatives	Yes	No	Representatives	Yes	No
Chairman Keiser	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Rep. Amerman	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Vice Chairman Johnson	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Rep. Boe	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Rep. Clark	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Rep. Gruchalla	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Rep. Dietrich	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	Rep. Thorpe	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Rep. Dosch	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Rep. Zaiser	<input type="checkbox"/>	<input type="checkbox"/>
Rep. Kasper	<input checked="" type="checkbox"/>	<input type="checkbox"/>			
Rep. Nottestad	<input checked="" type="checkbox"/>	<input type="checkbox"/>			
Rep. Ruby	<input type="checkbox"/>	<input checked="" type="checkbox"/>			
Rep. Vigasaa	<input type="checkbox"/>	<input checked="" type="checkbox"/>			

Total Yes 8 No 5

Absent 1

Floor Assignment Rep. Kasper

If the vote is on an amendment, briefly indicate intent:

Date: 3-20-07
Roll Call Vote #: 2

2007 HOUSE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. SB 2228

House Industry Business & Labor Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken Reinsert Subsection 7

Motion Made By Rep. Boe Seconded By Rep. Dosch

Representatives	Yes	No	Representatives	Yes	No
Chairman Keiser	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Rep. Amerman	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Vice Chairman Johnson	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Rep. Boe	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Rep. Clark	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Rep. Gruchalla	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Rep. Dietrich	<input type="checkbox"/>	<input checked="" type="checkbox"/>	Rep. Thorpe	<input type="checkbox"/>	<input type="checkbox"/>
Rep. Dosch	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Rep. Zaiser	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Rep. Kasper	<input type="checkbox"/>	<input checked="" type="checkbox"/>			
Rep. Nottestad	<input checked="" type="checkbox"/>	<input type="checkbox"/>			
Rep. Ruby	<input type="checkbox"/>	<input checked="" type="checkbox"/>			
Rep. Vigasaa	<input type="checkbox"/>	<input checked="" type="checkbox"/>			

Total Yes 4 No 9

Absent 1

Floor Assignment Rep. Kasper

If the vote is on an amendment, briefly indicate intent:

Date: 3-21-07
Roll Call Vote #: 1

2007 HOUSE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. SB 2268

House Industry Business & Labor Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken adopt amendment #1, not including any portion on page 38

Motion Made By Rep. Zaiser Seconded By Rep. Nottestad

Representatives	Yes	No	Representatives	Yes	No
Chairman Keiser	X		Rep. Amerman		X
Vice Chairman Johnson	X		Rep. Boe	X	
Rep. Clark	X		Rep. Gruchalla	X	
Rep. Dietrich	X		Rep. Thorpe		
Rep. Dosch	X		Rep. Zaiser	X	
Rep. Kasper	X				
Rep. Nottestad	X				
Rep. Ruby	X				
Rep. Vigesaa	X				

Total Yes 12 No 1

Absent 1

Floor Assignment Rep. Kasper

If the vote is on an amendment, briefly indicate intent:

March 20, 2007

PROPOSED AMENDMENTS TO ENGROSSED SENATE BILL NO. 2268

Page 2, line 1, replace "hypothocating" with "hypothecating"

Page 3, line 18, after the semicolon insert "and"

Page 3, line 20, remove "and"

Page 3, remove lines 21 and 22

Page 4, line 21, after the semicolon insert "or"

Page 4, remove lines 22 through 25

Page 6, line 6, replace "contact" with "contract"

Page 7, line 20, replace "on" with "one"

Page 9, line 19, after "policy" and before the comma insert "that has been or will be the subject of a viatical settlement contract"

Page 11, line 12, after "fee" and before the period insert "for a provider license and a two hundred dollar fee for a broker license"

Page 12, line 10, replace "two" with "one"

Page 12, line 16, replace "two" with "one"

Page 12, line 20, replace "paragraph" with "section"

Page 12, line 25, remove "shall be in the favor"

Page 12, line 26, remove "of this state and" and replace "commission" with "commissioner"

Page 14, line 15, replace "on" with "one"

Page 14, line 27, remove "At the commissioner's discretion, the commissioner may"

Page 14, remove line 28

Page 23, line 29, after "settlement" insert "provider"

Page 25, line 14, remove ", including the amount and"

Page 25, line 15, remove "method of calculating the provider's compensation"

Page 26, remove line 1

Page 26, line 2, replace "during the transfer process, and if so, provide" with "Provide"

Page 31, line 30, replace "an absolute" with "a"

Page 34, line 13, after "dies" and before the semicolon insert "or no remaining beneficiaries are then surviving" and after the semicolon insert "or"

Page 34, line 14, remove "The viator divorces a spouse;"

Page 34, remove line 15

Page 34, line 16, remove "(5)"

Page 35, line 10, remove "or other party entering into a"

Page 35, line 11, remove "viatical settlement contract with a viator"

Page 36, line 19, replace "No viatical settlement provider shall enter into a viatical settlement contract unless" with "It is unlawful for an insurance company to engage in any transaction, act, or practice or course of business or dealing which restricts, limits, or impairs in any way the lawful transfer of ownership, change of beneficiary, or assignment of a policy to effectuate a viatical settlement contract."

Page 36, remove lines 20 through 30

Page 37, line 1, remove "The purpose of this section is to"

Page 37, remove lines 2 through 14

Page 37, line 15, remove "2."

Page 37, line 24, after the period insert "The commissioner may adopt rules to implement this section."

Page 37, remove lines 25 through 30

Page 38, remove lines 1 through 31

Page 39, remove lines 1 through 31

Page 40, remove lines 1 through 31

Page 41, remove lines 1 through 30

Page 42, remove lines 1 through 15

Renumber accordingly

A-4 13
Harms

PROPOSED AMENDMENTS TO ENGROSSED SENATE BILL NO. 2268

MARCH 20, 2007

Based on
orig bill

**IBL Committee
North Dakota House of Representatives**

Chairman Keiser and Members of the Committee:

Following are our proposed additional amendments to SB 2268 along with some explanation to assist in your consideration. I have attempted to coordinate these changes with those proposed by other members of the opponents to the bill.

Relating to definition of advertising:

Page 1, beginning at line 15, remove "or any communication by means of recorded telephone messages or

Page 1, line 20, remove "devise, bequest"

Relating to definition of Fraudulent viatical settlement act:

Page 2, line 25 remove "or permits its employees or its agents to engage in"

Page 2, lines 27-28 remove: "or preparing with knowledge or belief that it will be presented"

Page 3, line 10 remove "(d) Premiums paid on an insurance policy"

Page 3, lines 19 and 20 delete "(2) Employing any plan, financial structure, device, scheme, or artifice to defraud related to viatical policies; and"

Page 3, line 24 remove "or permits its employees or its agents"

Page 4, remove lines 12 through 21

Relating to disclosure under proposed 26.1-33.3-07

Page 23 line 23 replace "sixty" with "thirty" (*relating to rescission*)

Page 23 line 24 replace "thirty" with "fifteen" (*relating to rescission*)

Page 29, remove lines 3 and 4 ("Disclose all the life expectancy certifications obtained by the provider in the process of determining the price paid to the viator").

Page 29, remove lines 20 through 23 ("State whether the insurer that wrote the policy has any additional rights that could negatively affect or extinguish the purchaser's rights under the viatical settlement contract, what these rights are, and under what conditions these rights are activated").

Relating to general rules under proposed 26.1-33.3-09

Page 31, line 3 replace "thirty" with "fifteen" (*relating to insurer verification of coverage*)

Relating to prohibited practices under proposed 26.1-33.3-10

Page 36, line 3 insert Any insurer which fails to timely respond to a request for verification of coverage or to timely implement a properly completed request for change of ownership or beneficiary of a policy or otherwise acts to hinder or delay a viatical settlement transaction shall be liable to the purchaser or other transferee for an amount equal to 25% of the policy face amount, together with the costs and fees incurred by the purchaser or other transferee. Nothing in this subdivision shall limit any other rights which a person may pursue against an insurance company.

Relating to prohibited practices/conflicts of interest under proposed 26.1-33.3-11

Page 36, remove lines 5 through 18 and lines 26 through 30.

Relating to advertising under proposed 26.1-33.3-12

Page 37 remove line 17 beginning with "All" through line 24; remove line 28 beginning with "Whether" through line 30.

Page 38, remove lines 1 and 2, 11 through 13, line 16 and line 18.

Page 39, remove lines 5 through 7, and beginning with "represent" remove line 21 through "if any" in line 22.

Page 40, beginning remove beginning with "The" in line 19 through line 20.

Page 40, line 30 remove "trade name"; insert knowingly between "not" and "use"

Page 41, line 7 insert knowingly between "not" and "use"

Page 41, line 20 insert knowingly between "not" and "create"

Page 41, line 25 remove "trade name"

Page 41, line 26 remove "service mark"

Page 42, remove lines 13 through 15

Relating to fraud prevention under proposed 26.1-33.3-13

Page 43, line 8 remove "or a reasonable suspicion"

Page 43, line 11 remove "or a reasonable belief"

Relating to penalties under proposed 26.1-33.3-14

Page 48, line 4 remove "thirty-five-thousand" and insert ten million

Page 48, lines 5 and 6, replace "two-thousand five-hundred" with five million and replace "thirty-five thousand" with ten-million.

Page 48, lines 7 and 8, replace "five-hundred" with one-million and replace "two-thousand-five hundred" with five-million.

Page 48, line 9 and 10, replace "five-hundred" with one-million.

Thank you for your consideration.

Robert W. Harms

The Harms Group

On behalf of Imperial Finance and Trading, LLC.

Date: 3-21-07
Roll Call Vote #: 2

2007 HOUSE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. SB 2268

House Industry Business & Labor Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken adopt amendment #3

Motion Made By Rep Zaiser Seconded By Rep. Boe

Representatives	Yes	No	Representatives	Yes	No
Chairman Keiser		X	Rep. Amerman		X
Vice Chairman Johnson		X	Rep. Boe	X	
Rep. Clark		X	Rep. Gruchalla		X
Rep. Dietrich		X	Rep. Thorpe		
Rep. Dosch		X	Rep. Zaiser	X	
Rep. Kasper		X			
Rep. Nottestad		X			
Rep. Ruby		X			
Rep. Vigasaa		X			

Total Yes 2 No 10

Absent 2

Floor Assignment Rep Kasper

If the vote is on an amendment, briefly indicate intent:

Date: 3-21-07
Roll Call Vote #: 3

2007 HOUSE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. SB 2268

House Industry Business & Labor Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number _____

Action Taken DO Pass, AS Amended

Motion Made By Rep. Kasper Seconded By Rep. Zaiser

Representatives	Yes	No	Representatives	Yes	No
Chairman Keiser		X	Rep. Amerman	X	
Vice Chairman Johnson	X		Rep. Boe		X
Rep. Clark	X		Rep. Gruchalla	X	
Rep. Dietrich	X		Rep. Thorpe		
Rep. Dosch	X		Rep. Zaiser	X	
Rep. Kasper	X				
Rep. Nottestad	X				
Rep. Ruby	X				
Rep. Vigesaa	X				

Total Yes 11 No 2

Absent 1

Floor Assignment Rep. Kasper

If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE

SB 2268, as engrossed: Industry, Business and Labor Committee (Rep. Kelser, Chairman) recommends AMENDMENTS AS FOLLOWS and when so amended, recommends DO PASS (11 YEAS, 2 NAYS, 1 ABSENT AND NOT VOTING). Engrossed SB 2268 was placed on the Sixth order on the calendar.

Page 2, line 1, replace "hypothocating" with "hypothecating"

Page 3, line 18, after the underscored semicolon insert "and"

Page 3, line 20, remove "and"

Page 3, remove lines 21 and 22

Page 4, line 21, after the underscored semicolon insert "or"

Page 4, remove lines 22 through 25

Page 4, line 26, replace "f." with "e."

Page 6, line 6, replace "contact" with "contract"

Page 7, line 20, replace "on" with "one"

Page 9, line 19, after "policy" insert "that has been or will be the subject of a viatical settlement contract"

Page 11, line 12, after "fee" insert "for a provider license and a two hundred dollar fee for a broker license"

Page 12, line 10, replace "two" with "one"

Page 12, line 16, replace "two" with "one"

Page 12, line 20, replace "paragraph" with "section"

Page 12, line 25, remove "shall be in the favor"

Page 12, line 26, remove "of this state and" and replace "commission" with "commissioner"

Page 14, line 15, replace "on" with "one"

Page 14, line 27, remove "At the commissioner's discretion, the commissioner may"

Page 14, remove line 28

Page 23, line 25, replace "paid" with "delivered" and replace "viator" with "escrow agent by or on behalf of the settlement provider"

Page 23, line 28, after "loans" insert an underscored comma

Page 23, line 29, after "settlement" insert "provider"

Page 24, line 3, after "viator" insert "by the later of the expiration of the rescission period or"

Page 25, line 14, replace ", including the amount and" with an underscored semicolon

Page 25, removes lines 15 through 17

Page 26, line 1, remove "State whether the funds will be escrowed with an independent third party"

Page 26, line 2, replace "during the transfer process, and if so, provide" with "Provide"

Page 30, line 1, after "a" insert "viatical settlement", after the underscored comma insert "viatical settlement", and after "transaction" insert an underscored comma

Page 30, line 2, after "of" insert "viatical settlement"

Page 30, line 3, after "disclose" insert "all nonproprietary information" and replace "a" with "the details of the"

Page 30, line 7, after the underscored period insert "Any disclosure required under this section must be in writing."

Page 31, line 30, replace "an absolute" with "a"

Page 32, line 2, replace "viator" with "escrow agent by or on behalf of the viatical settlement provider"

Page 33, line 2, after the second "the" insert "later to occur of the expiration of any then remaining rescission period or the"

Page 33, line 28, after "application" insert "for"

Page 34, line 13, after "dies" insert "or no remaining beneficiaries are then surviving"

Page 35, line 7, after "settlement" insert "in connection with the issuance of the policy"

Page 35, line 10, remove "or other party entering into a"

Page 35, line 11, remove "viatical settlement contract with a viator"

Page 36, line 19, replace "No viatical settlement provider shall enter into a viatical settlement contract unless" with "It is unlawful for an insurance company to engage in any transaction, act, or practice or course of business or dealing which restricts, limits, or impairs in any way the lawful transfer of ownership, change of beneficiary, or assignment of a policy to effectuate a viatical settlement contract."

Page 36, remove lines 20 through 30

Page 37, line 1, remove "The purpose of this section is to"

Page 37, remove lines 2 through 14

Page 37, line 15, remove "2."

Page 37, line 24, after the underscored period insert "The commissioner may adopt rules to implement this section."

Page 37, remove lines 25 through 30

Page 38, remove lines 1 through 31

Page 39, remove lines 1 through 31

Page 40, remove lines 1 through 31

Page 41, remove lines 1 through 30

Page 42, remove lines 1 through 15

Renumber accordingly

2007 TESTIMONY

SB 2268

SENATE BILL NO. 2268

Presented by: Jim Poolman
Commissioner
North Dakota Insurance Department

Before: Senate Industry, Business and Labor Committee
Senator Jerry Klein, Chairman

Date: January 30, 2007

TESTIMONY

*Same
given to
House DBA*

Good morning, Chairman Klein and members of the committee. My name is Jim Poolman and I am the Insurance Commissioner.

Senate Bill No. 2268 deals with transactions involving the sale of a life insurance policy to an investor, or the financing of the purchase of a policy by one or more investors, who speculate on the death of the insured, also referred to as viatical settlement transactions.

The person selling the policy is referred to as a viator. The entity purchasing the policy is referred to as a viatical settlement provider. The transaction between the viator and the viatical settlement provider is often arranged by a viatical settlement broker. The agreement is called a viatical settlement contract.

This bill repeals the existing Viatical Settlement Chapter, 26.1-33.2, and enacts a new Chapter, 26.1-33.3, that adopts the existing law but also incorporates new restrictions on viatical transactions and expands on those provisions that already exist in Chapter 26.1-33.2.

The new restrictions target those policies which are purchased when the investor has no insurable interest in the policy, through the use of non-recourse premium financing, with specific intent to settle for the benefit of investors from the point of purchase. The restrictions do not apply if the viator presents evidence that:

1. The viator is terminally ill.
2. The viator's spouse died.
3. The viator divorces a spouse.
4. The viator retires from full-time employment.
5. The viator becomes physically or mentally disabled such that the viator is unable to work.
6. The viator files for bankruptcy.
7. The policy was converted from a group policy at least five years prior to the transaction.
8. At least two years have elapsed from the date the policy was issued and policy premiums were funded with the viator's unencumbered assets and there is no agreement with another person to reimburse the viator for the payments or to purchase the policy through an assumption of a debt or forgiveness of a loan.

See Section 26.1-33.3-10.

Section 26.1-33.3-01 adopts and expands on certain existing definitions, including the definition of viatical settlement fraudulent act, and includes some new definitions, including those for a viatical settlement investment agent and a viatical settlement purchase agreement, which are adopted from the Securities definitions found in Section 10-04-02.

Section 26.1-33.3-02 expands on existing licensing requirements for viatical settlement providers and brokers to more clearly identify the Commissioner's licensing authority. It also requires that a viatical settlement provider provide either a bond or evidence of financial net worth of at least \$250,000.

Section 26.1-33.3-03 expands on existing provisions relating to the revocation or denial of a viatical settlement provider or broker license to more clearly define the Commissioner's authority to either deny or revoke a license.

Section 26.1-33.3-04 requires that the Commissioner approve all forms used in a viatical settlement transaction and prohibits an insurer from requiring that a viator or others sign a form not approved by the Commissioner or to delay the processing of a change of ownership form for more than 30 days.

Section 26.1-33.3-05 adopts certain provisions relating to protecting the privacy of a viator. It also requires that a viatical settlement provider report information regarding viatical settlement contracts with residents of this state to the Commissioner as requested by the Commissioner.

26.1-33.3-06 expands on existing provisions relating to the examination of the activities of a viatical settlement provider or broker to more clearly outline the Commissioner's authority to examine. It requires that personal information regarding the identity of a viator gathered during an examination be kept confidential. It requires that a viatical settlement provider retain records relating to a transaction for at least five years to facilitate the Commissioner's examination.

Section 26.1-33.3-07 expands on the existing requirement that a viatical settlement provider or broker provide the viator with disclosures relating to the effect of the sale of a life insurance policy. The disclosures protect the viator from suffering adverse financial and other consequences resulting from the sale of the policy. It also requires that a viatical settlement provider or agent provide the viatical settlement purchaser with certain disclosures.

Section 26.1-33.3-08 requires that a viatical settlement broker or provider involved in a viatical transaction plan that is negotiated either prior to or within five years of the issuance of the policy disclose the plan to the insurance company at the time the plan is developed.

Section 26.1-33-09 adopts certain general rules allowing the viator to rescind a contract within 60 days of entering into the transaction or within 30 days of receiving payment or under other conditions. It also requires that the viatical settlement provider provide the insurer with written notice of the transaction and provide copies of supporting documents within 20 days of the transaction, and provides that an insurer respond to a request for verification of coverage within 30 days of receipt of the request, among others.

Section 26.1-33.3-10 identifies certain prohibited practices, including the prohibited sale or financing of a policy prior to its issuance or within five years of issuance as discussed above, and others relating to dealings between the viatical settlement provider and an insurer.

Sections 26.1-33.3-11 and 26.1-33.3-01(10) deal with prohibited practices and conflicts of interest and provide that a viatical settlement broker is the agent of the viator and owes a fiduciary duty to the viator. Section 26.1-33.3-11 also deals with a viatical settlement broker's conflict of interest that results from an affiliation with the viatical settlement provider or another entity involved in a transaction.

Section 26.1-33.3-12 includes detailed restrictions on the advertising related to a viatical transaction.

Section 26.1-33.3-13 expands on the requirement that a viatical settlement provider or broker implement a fraud prevention and control program and that the settlement contract include a fraud warning.

Sections 26.1-33.3-14 and 26.1-33.3-16 reenact the provisions that allows the Commissioner to adopt rules and take certain enforcement actions, including issuing a cease and desist order.

Section 26.1-33.3-15 adopts the existing law that makes a violation of the chapter an unfair trade practice under Section 26.1-04-03.

Section 26.1-33.3-17 provides for an effective date of August 1, 2007.

If you have any questions, I would be happy to answer them. Thank you.

PROPOSED AMENDMENTS TO SENATE BILL NO. 2268

Page 1, line 20, remove "purchase or"

Page 2, line 28, remove the third "viatical"

Page 2, line 29, remove "settlement investment agent,"

Page 3, line 9, remove ", or as a result of a viatical"

Page 3, line 10, remove "settlement purchase agreement"

Page 3, line 13, remove "viatical settlement purchase agreement"

Page 3, line 16, remove ", or viatical settlement purchase"

Page 3, line 17, remove "agreement"

Page 3, line 19, remove "viatical settlement purchase agreement"

Page 8, line 8, after the underscored period insert "A "viatical settlement investment agent" is an agent as defined in section 10-04-02."

Page 9, line 10, after the underscored period, insert "A "viatical settlement purchase agreement" is a viatical settlement contract as defined in section 10-04-02."

Page 10, remove lines 20 thru 27

Page 10, line 28, replace "c" with "b"

Page 11, line 3, replace "d" with "c"

Page 11, line 25, remove "or viatical settlement investment agents,"

Page 14, line 2, replace "or a viatical settlement purchase" with "i"

Page 14, remove line 3

Page 15, line 9, remove "viatical settlement investment agent,"

Page 15, remove lines 17 thru 19

Page 15, line 20, replace "c" with "b"

Page 15, line 23, replace "d" with "c"

Page 15, line 25, replace "e" with "d"

Page 15, line 29, replace "f" with "e"

Page 32, remove lines 22 thru 24

Page 32, line 25, replace "5" with "4"

Page 33, line 10, replace "6" with "5"

Page 33, line 18, replace "7" with "6"

Page 36, line 12, remove "viatical settlement investment agent,"

Page 36, line 20, remove "viatical settlement investment agent,"

Page 37, line 1, replace the second comma with "or" and remove "or"

Page 37, line 2, remove "viatical settlement investment agent"

Page 37, line 6, remove "and viatical settlement purchase"

Page 37, line 7, remove "agreements" and "and viatical"

Page 37, line 8, remove "settlement purchasers"

Page 37, line 10, remove "or viatical settlement purchase"

Page 37, line 11, remove "agreement bought or sold"

Page 37, line 17, remove the second "viatical"

Page 37, line 18, remove "purchase agreements,"

Page 38, line 4, remove "or viatical"

Page 38, line 5, remove "settlement purchase agreement, product or service"

Page 39, line 8, remove ", purchasers, or"

Page 39, line 9, remove "prospective purchasers"

Page 39, line 11, remove "or viatical settlement purchase agreement"

Page 39, line 14, remove "or viatical settlement purchase agreement"

Page 40, line 3, remove "or viatical settlement purchase agreement"

Page 40, line 5, remove the second "or"

Page 40, line 6, remove "purchasers"

Page 40, line 18, remove "or viatical settlement purchase agreement"

Page 40, line 28, remove "or viatical settlement purchase agreement"

Page 41, line 8, remove "or viatical"

Page 41, line 9, remove "settlement purchase agreements"

Page 41, line 10, remove "or viatical settlement purchase agreement"

Page 41, line 11, remove "or viatical settlement purchase agreement"

Page 41, line 22, remove "or viatical settlement"

Page 41, line 23, remove "purchase agreement"

Page 41, line 28, remove "or purchasers"

Page 42, line 4, replace the third underscored comma with "or" and remove "or"

Page 42, line 5, remove "viatical settlement investment agent"

Page 42, line 8, remove "or viatical settlement"

Page 42, line 9, remove "purchase agreement forms"

Page 42, line 23, replace the second "or" with "i"

Page 42, remove line 24

Page 42, line 25, remove "or viatical settlement purchase agreement"

Page 43, line 15, remove "and purchase agreement forms"

Page 43, line 19, remove "or a viatical settlement"

Page 43, line 20, remove "purchase agreement"

Page 47, remove lines 16 thru 21

Page 47, line 22, replace "4" with "3"

Page 47, line 26, replace "5" with "4"

Page 48, line 4, replace "6" with "5"

Page 48, line 10, replace "7" with "6"

Page 48, line 15, replace "8" with "7"

Page 48, line 17, replace "9" with "8"

Page 49, line 26, replace the underscored comma with "and" and replace "and viatical settlement" with "i"

Page 49, remove line 27

Page 50, line 2, remove "and viatical settlement"

Page 50, line 3, remove "investment agents"

Page 50, line 5, replace the first underscored comma with "or" and remove ", or viatical settlement investment agent"

Page 50, line 7, replace the first underscored comma with "or" and remove ", or investment agent's"

Renumber accordingly

March 19, 2007

PROPOSED AMENDMENTS TO ENGROSSED SENATE BILL NO. 2268

Page 3, line 18, after the semicolon insert "and"

Page 3, line 20, remove "and"

Page 3, remove lines 21 and 22

Page 4, line 21, after the semicolon insert "or"

Page 4, remove lines 22 through 25

Page 9, line 19, after "policy" and before the comma insert "that has been or will be the subject of a viatical settlement contract"

Page 11, line 12, after "fee" and before the period insert "for a provider license and a two hundred dollar fee for a broker license"

Page 12, line 10, replace "two" with "one"

Page 12, line 16, replace "two" with "one"

Page 12, line 20, replace "paragraph" with "section"

Page 12, line 25, remove "shall be in the favor"

Page 12, line 26, remove "of this state and" and replace "commission" with "commissioner"

Page 14, line 27, remove "At the commissioner's discretion, the commissioner may"

Page 14, remove line 28

Page 23, line 29, after "settlement" insert "provider"

Page 26, remove line 1

Page 26, line 2, replace "during the transfer process, and if so, provide" with "Provide"

Page 31, line 30, replace "an absolute" with "a"

Page 34, line 13, after the semicolon insert "or"

Page 34, line 14, remove "The viator divorces a spouse;"

Page 34, remove line 15

Page 34, line 16, remove "(5)"

Page 35, line 10, remove "or other party entering into a"

Page 35, line 11, remove "viatical settlement contract with a viator"

Page 36, line 19, replace "No viatical settlement provider shall enter into a viatical settlement contract unless" with "It is unlawful for an insurance company to engage in any transaction, act, or practice or course of business or dealing which restricts, limits, or impairs in any way the lawful transfer of ownership, change of beneficiary, or assignment of a policy to effectuate a viatical settlement contract."

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Page 40, remove lines 1 through 31

Page 41, remove lines 1 through 30

Page 42, remove lines 1 through 15

Renumber accordingly

Press Releases

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For Immediate Release
October 26, 2006

SUIT REVEALS FRAUDULENT SCHEME IN LIFE SETTLEMENT INDUSTRY

Attorney General Eliot Spitzer today sued a leading financial services company, alleging that it orchestrated a broad scheme to defraud owners of life insurance.

The lawsuit targets the fast-growing "life settlements" industry, where investors buy life insurance policies from policy owners, make premium payments as they come due, and then collect death benefits when the insured person dies. The industry has tripled in size during the last three years and now accounts for more than \$6 billion in revenues, according to industry analysts.

"People in the life settlement industry like to think that they are providing a wonderful new service that bridges the gap between the insurance industry and capital markets," Spitzer said. "But the reality is that too many industry players are cheating policy owners to maximize profits for themselves and their firms."

Spitzer's office began an investigation of the life settlements sector in 2005 after receiving a tip that life settlement brokers were accepting secret commissions that unfairly reduced the amounts owners received for the policies. Such brokers are supposed to represent the interests of policy owners. They are supposed to obtain the highest price possible for their clients' policies through competitive bidding.

The civil complaint filed today in State Supreme Court in Manhattan alleges that the industry leader, Coventry First LLC, based in Philadelphia, PA, made secret payments, dubbed "co-brokering fees," to life settlement brokers. The suit alleges that, in exchange for these payments, the brokers suppressed competitive bids from other life settlement companies.

The suit asserts antitrust violations, fraud, and other state law claims. It cites e-mail and other evidence showing that industry executives were well aware of their illegal conduct.

Typical examples of the bid-rigging scheme are as follows:

*In mid-2003, a 79 year-old widower living in Hawaii decided to sell his \$400,000 life insurance policy. A Florida-based broker representing the widower had an offer from one of Coventry's competitors. In a March 5, 2003 e-mail, a senior employee at Coventry wrote to Coventry's Executive Vice-President, Reid Buerger: "[The broker] said he spoke with you a while back about co-brokering the . . . case. He is frustrated that we have not gotten it accepted. He said he is sitting on a [a competitive offer] and can probably get more."

Later, in exchange for a co-brokering fee from Coventry, the broker refrained from presenting the widow with the other offer.* In 2004, a New York trust decided to sell a \$4.9 million policy insuring the life of an 80 year-old woman. Coventry offered \$705,000. When Coventry officials learned that a broker had a higher offer from another life settlement buyer, they contacted that broker's President to work out a deal.

An internal e-mail by a senior Coventry employee reported: "[The broker's President] claims he would go well over \$1M. He asked for 1.5 pts. I offered .5 pt. do we want to do that much?"

Ultimately, Coventry and the broker worked out a deal. In exchange for a secret payment of \$49,000 (or 1 point) from Coventry, the broker never presented the trust with the higher offer from Coventry's competitor.

* In 2005, a broker informed Coventry that he had a competitive offer for a policy insuring the life of an 85 year-old man living in Florida. To ensure that Coventry won the deal, a senior Coventry employee arranged for the broker to receive a \$5,000 co-broker payment in exchange for sitting on the other offer. The Coventry employee boasted: "I bought insurance for 5k."

In addition to the co-brokering fees, the lawsuit alleges that Coventry routinely induced brokers to violate their fiduciary duties to policy owners through so-called "gross offers," which provided a separate financial incentive for brokers to convince their clients to take as little as possible for their insurance policies.

As a result of the incentives created by gross offers, policy owners routinely, but unknowingly, paid brokers extraordinarily high commissions. To date, the on-going investigation has uncovered more than 200 Coventry cases nationwide where brokers were paid undisclosed commissions of 50 percent or more of what the seller received.

Spitzer said the conduct outlined in the complaint showed a dramatic lack of ethical standards in the new industry.

"It is not a defense to claim that even with corrupt practices clients are still getting more through life settlements than if they surrendered their policies to their original insurers for cash," the Attorney General said. "The situation cries out for both greater regulatory scrutiny and serious soul-searching by the industry and its advocates."

The lawsuit seeks injunctive relief from the court, restitution and appropriate damages from Coventry.

The Attorney General's case is being handled by Assistant Attorneys General David Axinn, Maria Filipakis, J. Jennifer Koh, and Legal Support Analyst Milena Shtelmakher, under the direction of Bureau Chief David D. Brown IV of the Investment Protection Bureau, with assistance provided by Economist Hampton Finer and Economic Analyst Andrew Lichtenberg of the Attorney General's Public Advocacy Division.

ATTACHMENTS:

- Complaint
 - Exhibit 1-20
 - Exhibit 21-40
 - Exhibit 41-60
 - Exhibit 61-78
-

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

THE PEOPLE OF THE STATE OF NEW YORK
by ELIOT SPITZER, Attorney General of
the State of New York,

Plaintiff,

-against-

COVENTRY FIRST LLC, MONTGOMERY
CAPITAL, INC., THE COVENTRY GROUP, INC., and
REID S. BUERGER,

Defendants.

COMPLAINT

Index No. .

1. Plaintiff, the People of the State of New York, by Eliot Spitzer, Attorney General of the State of New York (the "State"), complaining of the above-named Defendants, alleges upon information and belief, that:

PRELIMINARY STATEMENT

2. This case arises from pervasive fraud in what is called the "life settlements" business, where investors buy life insurance policies from owners at a discount, pay the premiums as they come due, and ultimately collect the death benefits for a profit. Defendant Coventry First LLC, a wholly-owned subsidiary of Defendant Montgomery Capital, Inc. and an affiliate of Defendant The Coventry Group, Inc. (collectively "Coventry"), is one of the major purchasers of life settlements, and Defendant Reid S. Buerger ("Buerger") is its Executive Vice President and son of its founder Alan Buerger. The Defendants and other participants in the life

settlement business prey on the owners of life insurance policies through two main schemes.

3. First, Defendants and brokers specializing in life settlements pretend to conduct auction-style bidding to get the highest price for owners considering selling their life insurance policies. In fact, the bidding is often rigged, with Coventry paying the brokers undisclosed fees, euphemistically called "co-brokering fees," to "sit on" or reduce competitive bids from other buyers. In a typical case involving a trust-owned policy insuring an elderly New York couple, Coventry offered \$880,000 in October 2004 in return for the 80 year-old woman's life insurance policy, which would pay \$4.9 million on her death. Shortly thereafter, Coventry learned that another buyer, acting through a broker, AllSettled Group, Inc. ("AllSettled"), was ready to offer over \$1,000,000 for the same policy. Coventry offered AllSettled a \$49,000 "fee" to suppress this competing bid, sending AllSettled an encoded email on November 2, 2004 stating "for [initials of insured], the number is 49." In return for this secret payment, AllSettled never informed the policy owner of the higher offer and closed its file on the matter. This Office's investigation has revealed dozens of similar examples involving Coventry making payments to suppress competing offers.

4. Second, Coventry systematically participates in breaches of fiduciary duty by life settlement brokers that hold themselves out to policy owners as faithful agents who will go to the market and obtain the highest possible prices for their clients' insurance policies. In a typical transaction, Coventry secretly provides these brokers with what is called a "gross offer" for the seller's life insurance policy. The gross offer is a lump-sum amount to be divided between the broker and the seller at the broker's discretion. It is never disclosed to the seller.

Unbeknownst to the seller, the less the seller gets, the more the broker keeps. The broker thus has every incentive to convince the owner that his or her policy is worth as little as possible. The results are not pretty: in one instance a broker took a gross offer of \$822,500 for a policy purchased by Coventry and convinced his client to take \$365,000 as a purchase price, keeping \$457,500 for himself as a "commission."

5. In most states, including New York, Coventry makes no disclosures about its gross offers. If a seller asks about broker compensation, Coventry typically refuses to answer. In states where the law requires disclosure, such as Ohio and Nevada, Coventry sometimes generates false documents that conceal all or a portion of what the broker is getting.

6. This action seeks damages, including restitution and rescission, on behalf of the owners of life insurance policies who have been damaged by the schemes described above, as well as injunctive relief preventing further breaches of law by the Defendants.

PARTIES

7. This action is brought by the People of the State of New York by the Attorney General based upon his authority under the Executive law, the Donnelly Act, the Martin Act and the General Business Law of New York State.

8. Defendant Coventry First LLC, a Delaware corporation domiciled in Fort Washington, Pennsylvania, is in the business of purchasing life insurance policies from sellers, a process also known as funding of life settlements. Coventry conducts business in New York State and throughout the United States. Coventry First LLC, formed in October 2001, a wholly-owned subsidiary of Defendant Montgomery Capital, Inc., is a privately held company owned by

(1) Alan Buerger, Chief Executive Officer, (2) Constance Buerger, President and Chief Operating Officer, and (3) Reid S. Buerger, Executive Vice President. From 2001 through 2005, Coventry paid annual management fees roughly equaling its profits to Defendants The Coventry Group, Inc. and Montgomery Capital, Inc., which are owned by the Buerger family.

9. Coventry is a leader in the life settlement business and has touted itself as having a market share exceeding 50%. (COV 1029983)¹. It purchases life insurance policies on behalf of institutional investors such as American International Group ("AIG"), Citigroup, Inc. and Ritchie Capital, an Illinois hedge fund. Coventry entered the market in 2002, purchasing 436 life insurance policies representing approximately \$720 million in total death benefits. By 2005, Coventry purchased 1,318 life insurance policies representing more than \$3 billion in death benefits.

10. Defendant Reid S. Buerger is an individual residing in Pennsylvania. Buerger is the Executive Vice President of Coventry. He owns 20% of Coventry directly and through a family trust.

JURISDICTION

11. The State has an interest in the economic health and well-being of those who reside or transact business within its borders. In addition, the State has an interest in ensuring that the marketplace for insurance policies, securities and other financial products functions honestly and fairly with respect to all who participate or consider participating in it. The State, moreover, has an interest in upholding the rule of law generally. Defendants' conduct

¹ Parenthetical citations refer to documents attached as exhibits hereto.

injured these interests.

12. The State sues in its sovereign and quasi-sovereign capacities, as *parens patriae*, and pursuant to Executive Law §§ 63(1) and 63(12), the New York Donnelly Act, General Business Law, § 340 *et seq.*, the Martin Act, General Business Law § 352 *et seq.* and the common law of the State of New York. The State sues to redress injury to the State and to its general economy and citizenry-at-large. The State seeks disgorgement, restitution, damages, including rescission, punitive damages and treble damages, and costs and equitable relief with respect to Defendants' fraudulent and otherwise unlawful conduct.

FACTUAL ALLEGATIONS

I. The Life Settlement Industry

A. Background

13. A "life settlement" is the sale of a life insurance policy in return for a purchase price that typically exceeds the surrender value² of the policy. Such policies are typically involve insureds who are high net worth individuals 75 years or older with more than two years life expectancy. These policies are often owned by trusts or companies, though in some instances the owners are the elderly insured individuals themselves. Owners may want to sell their policies for a variety of reasons, including avoiding high premium payments or getting out of what are in essence poorly performing investments. The buyers are investors who, after buying the policy, continue to pay premiums until the insured dies. Upon the insured's death, the

² The surrender value is a contractual price set forth in a life insurance policy at which a policy owner can return or "surrender" the policy to the life insurance company which issued the policy.

buyers claim the policy's death benefit.

14. The economics of these deals are straightforward: the investor wagers that the value of the future death benefit will exceed the purchase price and costs of paying premiums until the insured dies. In turn, the seller prefers an immediate lump sum payment as opposed to the alternative of paying premiums for an eventual death benefit. Given this simple equation, a life settlement investor gets a higher rate of return the nearer the insured is to death and if the insured has experienced a decline in health since the policy had been issued. In certain transactions, for instance, Coventry makes its life settlement offer "contingent on receipt of letter signed by insured stating they are currently a [c]igarette smoker and how many cigarettes they smoke per day." (COV-1139212).

B. History of Life Settlements

15. In the 1980s, investors began purchasing life insurance policies from terminally ill individuals, often afflicted with the HIV virus and in need of immediate cash, in transactions known as viaticals. However, as HIV medical treatments improved and individuals lived longer, these types of policies were not as profitable to investors. Furthermore, various states moved to regulate the industry to curtail fraudulent practices typically involving middlemen who defrauded the purchasers of policies. Many states, including New York, enacted laws that require strict licensing and disclosure in all cases where the insured has "a catastrophic or life threatening illness or condition." See e.g. N.Y. Insurance Law Article 78.

16. The life settlement industry developed in the late 1990s as an outgrowth of viaticals, involving older individuals who were not on the brink of death. Under an industry

standard that is codified in some states (though not New York), sales in which the insured has two or more years of life expectancy are life settlements and sales involving those with shorter life expectancies are considered viaticals. Many states, including New York, do not require licensing of life settlement brokers or disclosure of compensation practices, and so these transactions largely occur without regulatory oversight.

17. The life settlement industry has grown dramatically in the past ten years. In 2005, for example, investors purchased life insurance policies with death benefits estimated at \$13 billion. One research analyst has predicted that the business will grow more than ten-fold to \$160 billion over the next several years. (Bernstein Research Call, March 4, 2005). An industry newsletter recently compared the industry's fast dollars and lack of regulation to that of the Old West:

Saddle up partner 'cuz your [sic] in for some kind of ride. It's easy to compare the early days of the life settlement industry to the Wild West, with its mad rush for gold, freedom to roam, and cowboy-like bravado. But the industry has changed quite a bit since then. The dust has settled, boundaries have been drawn, and lone rangers replaced by corporate giants. Although the industry is much more sophisticated today, those early promises of golden nuggets still exist. (Cov 1027931).

Similarly, a life settlement broker's website offers a caricature of a prospector in front of a saloon, with a banner overhead reading: "Welcome to Cashville." (<http://www.tecsc.com> (last visited Mar. 29, 2006)).

C. Structure of the Life Settlement Market

18. The life settlement business has evolved into a multi-tiered industry, consisting of Sellers, Brokers, and Buyers. The role of each is described below.

19. First, there is the Seller. As described above, the Seller is an owner of a policy insuring the life of an elderly person with two or more years of life expectancy. In a typical case, the Seller discusses with a financial advisor, insurance agent, estate planner or other advisor the option of entering into a life settlement. If the Seller decides to proceed, the Seller's advisor may hire one or more intermediaries specializing in life settlements ("Brokers") to represent the Seller. In some cases, the Seller's insurance agent or other advisor may team up with the Broker to shop the policy. The Broker(s) submit the policy to different buyers ("Buyers") such as Coventry. If interested, the Buyers bid on the policy. Coventry and other Buyers may use their own capital to purchase life settlements. In most cases, however, Coventry acts as a Buyer for institutional investors. In some cases, Coventry cuts out the middlemen, negotiating Sellers and their representatives directly.

20. In theory, the industry operates on an auction model, with Brokers serving as auctioneers, soliciting bids from competing Buyers to submit to the Seller for the policy. Brokers act on the Seller's behalf to shop the policy to different Buyers. Buyers, including Coventry, will submit what is called a "gross offer" to a Broker, which represents a single lump sum offer to the Broker for the purchase of a life insurance policy. From this "gross" or lump sum amount, the Broker will then determine how much to extend to the Seller as the actual purchase price and how much to keep for itself, the Broker. Although a Broker solicits gross

offers, it usually only presents to the Seller a net price, keeping both the gross offer and the Broker's compensation hidden from the Seller. Like an auction there may be multiple rounds of gross offers submitted by competing Buyers who outbid each other in an effort to win the deal.

21. Buyers may seek to differentiate their bids by touting their superior credit risk or ability to close transactions quickly, but as in any auction, the main driver for the Seller is the selling price. When the Seller is satisfied that he or she has the highest offer the auction ends. If the highest offer is inadequate, the Seller may decide to keep the policy or offer it for sale in the future. If the offer is accepted, the Broker informs the Buyer of that fact and of how the gross offer will be divided between the Seller and the Broker. The Buyer then pays the selling price to the Seller.

22. In a typical case, a Broker submits a life settlement application to Coventry. Coventry's Financial Analysis group processes the actuarial data, estimates life expectancies and determines the pricing for the policy. The policy is then sent to the Financial Underwriting group, headed by Defendant Buerger. Buerger and his team then determine the gross offers. As described above, the gross offer encompasses broker compensation, however any special compensation arrangements, including co-broker payments and bonuses, are approved by Buerger himself. As one email explained, "Eileen [Shovlin, Coventry regional manager] talks to [the Broker] about their cases and Reid [Buerger] about co-brokers." (COVID 00022580).

23. Brokers owe a fiduciary duty to their client, the Seller. According to an industry association: "It's important to recognize that the broker has a fiduciary role to represent

the seller by law...the bottom line is that the broker's job is to fully represent the interests of the policy seller." (Life Insurance Settlement Association White Paper "Cashing in on Unneeded Life Insurance Policies," Aug. 22, 2006). Brokers hold themselves out as representatives of the Seller working to obtain the highest purchase price on his behalf. For example, AllSettled states on its website: "A broker works for you. A broker will check with several providers to find the best offer for you." (<http://www.allsettled.com/sellerguide.html> (last visited Apr. 27, 2006)). Another broker's website, Advanced Settlements, Inc. ("Advanced"), states: "Having developed relationships with more than 20 funding institutions, the company works with financial professionals, attorneys and charitable organizations to obtain multiple offers on the secondary market in pursuit of the highest possible settlement for the client." (<http://advancedsettlements.com/assets/pages/about.php> (last visited Apr. 3, 2006))³.

24. Coventry recognizes that Brokers owe their clients a fiduciary duty. When it is advantageous to Coventry, it steps in to ensure that duty is fulfilled. For example, on May 6, 2005, a Broker refused to present Coventry's offer to the Seller. In response, a Coventry regional vice president suggested, "perhaps I could push the fiduciary duty button and force him into presenting the offer to the client." (COVJD 00031940). In a similar situation earlier in 2005, Coventry was informed that another Broker would not present its higher offer to the Seller. Alan Buerger, Coventry's founder and CEO, directed that the Broker be reminded that it "is to act as a fiduciary for the client and we would be both disappointed and surprised if they chose not to act

³ Advanced is one of the largest life settlement Brokers. It is a wholly-owned subsidiary of National Financial Partners Corporation, a publicly traded Delaware corporation headquartered in New York.

as a fiduciary . . . This is all the more relevant given all Coventry's recent conversations with [the Broker] about Spitzer, disclosure and liability. . . you may quote me!" (COVJD 00021726).

II. Coventry's Bid Rigging Scheme

25. In fact, the above auction model bears little relation to what really happens in the life settlement industry. Coventry has undermined competition in the life settlements business through a variety of schemes - - the most egregious of which involves rigged bids for insurance policies.

26. In late 2001, Coventry entered the life settlement industry as a Buyer (it had previously been a Broker). By early 2002, it had begun to pay undisclosed compensation, called co-broker payments, to Brokers who in exchange refrained from submitting bids, refrained from soliciting competitive bids or squelched higher bids, thus guaranteeing that Coventry won the "auction." A senior Coventry employee, Neal Jacobs, aptly described these payments as providing Coventry "insurance" that it would win the auction. (COVNI 00012957). Some examples of the scheme are set out below.

A. A 79 year-old widower living in Hawaii

27. In mid-2003, a 79 year-old widower living in Hawaii decided to sell his \$400,000 life insurance policy. The policy was ultimately sold to Coventry on April 16, 2003 for \$102,000 - - the Seller received \$78,000 and his Broker received \$24,000.

28. The Seller was not aware that another Broker, Florida-based Life Settlement Alliance ("LSA")⁴ had a gross offer of \$108,000, surpassing Coventry's, but refrained from presenting it in exchange for a co-broker fee. In a March 5, 2003 email Jim Dodaro, Coventry's Vice President of Financial Underwriting, wrote to Buerger:

[Jim Nutt, a senior employee of LSA] said he spoke with you a while back about co-brokering the . . . case. He is frustrated that we have not gotten it accepted. He said he is sitting on a 27% gross offer [\$108,000] from Mutual and can probably get more. If we can't close he said he could and pay us a co-broker fee. (COV 1136766).

Ultimately, Coventry closed with a gross offer of \$102,000 (\$78,000 to the Seller and \$24,000 to his Broker) and, as arranged by Buerger and Nutt, LSA received a co-broker payment of \$12,000 for not submitting the higher bid. LSA's sole contribution to the life settlement transaction was to "sit on" a competing offer to the detriment of the Seller. The co-broker fee was not disclosed to the Seller as part of Coventry's Purchase Agreement. (COV2 0006025).

29. In September 2006, Buerger invoked the Fifth Amendment when asked whether he approved the co-broker payment to LSA in exchange for LSA to sit on the higher offer.

⁴ LSA dissolved in mid-2005 after the U.S. Securities and Exchange Commission ("SEC") alleged that Mutual Benefits Corporation, a life settlement and viatical Buyer that was shut down by the SEC in 2004, violated an asset-freeze order by diverting \$2.8 million from Mutual Benefits to LSA. In May 2005, LSA's three senior officials left LSA and started a new Broker called Life Insurance Settlements, Inc. ("LIS") which continues to do business with Coventry.

B. A trust-owned policy insuring a New York woman in her eighties

30. In another case, a family trust decided to put a \$4.9 million policy insuring an 80 year-old woman on the market through a Broker. The Broker solicited bids directly from Coventry as well as from AllSettled, a New York Broker⁵. In September 2004, Coventry made a gross offer of \$705,000 for the policy. (COV 1142334). Coventry learned in October 2004 that it was competing against an offer from another Buyer of \$880,000 submitted by AllSettled. Neal Jacobs, Coventry's Director of Financial Underwriting, contacted AllSettled's President, Michael Krasnerman ("Krasnerman"), to work out a deal. According to an October 28, 2004 email from Jacobs, Krasnerman requested a payoff of 1.5 percent of the death benefit to step aside in the bidding process. Jacobs reported, "[Krasnerman] claims he would go well over \$1M. [H]e asked for 1.5 pts. I offered .5 pt. [D]o we want to do that much?" (COVNI 00027506). Ultimately, Coventry and AllSettled reached an agreement that Coventry would pay \$49,000, equal to 1% (or 1 point) of the death benefit of the policy and in exchange AllSettled would close the file. The agreement was memorialized in an encoded email from Jacobs to Krasnerman on November 2, 2004, stating "for [insured's initials], the number is 49." (COVNI 00008934). On November 11, 2004, Lenore Saracino, AllSettled's Vice President of the Life Settlement Division, wrote by hand on the Status Report "[c]lose file[.] Have a co-brokering fee with Coventry." (AS 001166).

⁵ At times, AllSettled is the Buyer itself, purchasing policies through vehicles such as AllSettled Assets LLC and National Consolidated Funding LLC II, which share common ownership.

31. On December 28, 2004, the trust received \$800,000 for a policy and the Broker received \$142,500 as compensation. Unbeknownst to the Seller, Coventry also paid AllSettled \$49,000 in exchange for stepping out of the bidding process. (COVNY 00013466).

C. A family-owned policy insuring a 79 year-old man

32. In another transaction in late 2004 involving the policy insuring a 79 year-old man from New Jersey owned by a family member, Coventry offered directly to the Broker (the Seller's financial advisor) a \$3,100,000 gross offer for a policy with a \$10,000,000 death benefit. On December 15, 2004, near the end of the bidding process, AllSettled's Saracino forwarded Neal Jacobs a competing offer of \$3,525,000 she had received from another Buyer. She added in her email to Jacobs: "Call Michael Krasnerman on Thursday." Jacobs immediately forwarded AllSettled's offer to Buerger with the message: "see below for what he says is his latest offer on [case name]." (COV 441616). Rather than compete with AllSettled and raise its gross offer by at least \$425,000, Coventry took the cheaper way out, entering into a side deal with AllSettled: AllSettled would receive \$200,000 in co-broker fees in exchange for not presenting its higher offer. Using the shorthand Coventry and AllSettled had developed for such matters, Jacobs sent an email to Krasnerman on December 16, 2004, stating "number is 200" (COVNI 00010364) then followed up a few minutes later with an email to Coventry's accounting department: "[AllSettled is] now co-broker for \$200K." (COV 441517). By paying AllSettled a co-broker payment of \$200,000 for not competing, Coventry ensured that its gross offer remained unchanged at \$3,100,000. The purchase closed on December 28, 2004 with the Seller receiving \$2,946,947 and the Seller's original Broker receiving an additional \$153,053.

The Seller never learned that another Buyer was willing to pay \$3,525,000 for the policy, nor that AllSettled received a co-broker payment for \$200,000. (COV2 0009660, COV 441517).

D. A trust-owned policy insuring an 81 year-old man

33. In a transaction involving the sale of a trust-owned policy with a death benefit of \$2.4 million policy, Stuart Kosloff ("Kosloff"), President of the East Coast Settlement Company, a Florida-based Broker, contacted Dodaro on October 13, 2004 and informed him that he had a \$900,000 bid that had not yet been submitted to the Seller. Kosloff suggested that the two parties "work together" to ensure that Coventry would win the business. (COV 1132940). Dodaro sent an email on November 15, 2004 to Buerger seeking approval over the terms of the deal: "I told Stuart [Kosloff] we could pay 1 pt (24k). He said that wasn't enough (has around 920k gross) and asked for 50-60K." (COV 1132946). Three days later, having not heard from Coventry, Kosloff sent the following email to Dodaro threatening, "I need to hear a yes or a no before the end of the day or I have to up my offer to them." (COVJD 00025246). Dodaro repeated his request for Buerger's approval, and within a few hours, Buerger wrote back: "ok." (COV 1132946).

34. Kosloff kept up his part of this collusive arrangement by not communicating this higher bid to the Seller and dropping out of the bidding. In a December 15, 2004 email from Kosloff to Dodaro, relating to a conversation Kosloff had earlier that day with the Seller's advisor, Kosloff wrote that the advisor "called this morning asking if I was all done bidding on [case name]. Told him I hated to say it but he should go with you." (COVJD 00017552). Coventry purchased the policy on January 31, 2005 for \$825,000. As agreed,

Coventry then paid Kosloff \$50,000. (COVJD 00025357). The Seller was never told about Kosloff's higher offer nor the co-broker payment to Kosloff. (COV2 0007151).

35. In September 2006, Buerger invoked the Fifth Amendment when asked about the purpose of Coventry's payment to Kosloff.

E. A company-owned policy insuring a 79 year-old woman

36. In a transaction involving a company-owned policy insuring a 79 year-old woman living in New Jersey, Coventry initially bid \$620,000 on December 16, 2004. A few days later on December 22, 2004, Coventry increased its offer to \$865,000. (COVNJ 00010495). Subsequently, Dodaro sent an email to Buerger on December 28, 2004 informing him that Pete Gaynor, another senior employee at LSA, told him: "We [Coventry] were one of 2 funders that offered on it. [A competing Buyer] was the other and are over 1M. Said he needs to hear from us by today or he is offering." (COVJD 00018719). In other words, LSA demanded to hear from Coventry or else it would compete with the higher offer it had from a competing Buyer. Even though LSA was not the Broker of record, it received \$65,000 from Coventry in exchange for not presenting the higher offer. This payoff was directly approved by Reid Buerger. (COVJD 00022656). Ultimately, Coventry closed the deal on February 4, 2005 for a gross offer of \$930,000, which was below the competing \$1 million gross offer noted by Gaynor. (COV 1194765). Once again, the Seller was not informed of the payoff made to LSA. (COV2 0007161).

F. A family-owned policy insuring a couple in their eighties

37. In April 2005, Coventry extended a gross offer of \$650,000 to the family owners of a variable life insurance policy insuring a Florida couple in their eighties with a \$4 million death benefit. (COVJD 00032741). On or about May 17, 2005, Jason Wyatt, Vice President of Advanced, contacted Dodaro and told him he had a higher offer from another Buyer and followed up with an email proposing a co-broker payment of 1 percentage point, or \$40,000. (COVJD 00032741). That same day, Dodaro reported the conversation to Buerger: "I told [Wyatt] 20K (½ pt). His offer (710K he says) is from [another Buyer] and we have a ton of room." (COVJD 00032741).

38. Advanced's Wyatt continued to press for a full percentage point co-broker fee but Dodaro responded: "take the bird in the hand" because "a bird in the hand is worth two in the bush." (COVJD 00032760). In other words, a guaranteed one-half percentage point, \$20,000, would be worth more to Advanced than submitting to the vagaries of actual competition, which could result in no commission to Advanced if Advanced failed to win the bidding war. Dodaro added: "I think what I offered is a no brainer for you." (COVJD 00032760).

39. Two days later, on May 19, 2005, Dodaro reached out to Wyatt, asking: "we good?" On May 23, 2005, Wyatt responded: "I guess I will take the bird in the hand. I will call him Larry. I will send Eileen [Shovlin, Coventry Regional Vice President] the file so you can put us down for 20k. Good job!" (COVJD 00033623). Even after Wyatt agreed to the payment, doubts remained. Dodaro wrote to Neal Jacobs: "I am nervous that Advanced will try

to pull a fast one. Please make sure the regional [manager] stays on top of this -- I want to know if Advanced tries anything to win the case." (COVJD 00033539). Both parties kept their word: Coventry closed the deal on July 18, 2005, Advanced received a co-broker fee of \$20,000 (AS 0008072), and the Sellers never learned that Advanced had received a co-broker fee and had sold them out. (COV2 0005404).

G. A 79 year-old man living in California

40. In another transaction in 2005, Coventry offered \$135,000 to a California Broker on a policy belonging to a 79 year-old California man with a death benefit of \$1.2 million. Upon learning that LSA had a higher competing gross offer for \$185,000, on May 5, 2005, Dodaro sent an email to Buerger asking him, "Do you want me to work out with LSA or let them have it?" (COVJD 00033016). The following day, Dodaro sent the following email to Coventry's accountant, "2 pts to LSA - co-broker." (COVJD 00033116). In return, LSA's higher offer was not presented to the client. LSA did in fact receive a co-broker payment of 2 percent of the \$1.2 million death benefit, or \$24,000.

41. Prior to closing this case, on May 20, 2005, Jacobs emailed Dodaro that a third Broker, Trinity Financial Services LLC, also had a higher gross offer of \$150,000: "Trinity has 150k and want to cooperate...I think I could get away w/5k..." (COVJD 00033131). Like LSA, Trinity received a co-broker payment of \$5,000 for "cooperating" with Coventry. (COVJD 00035057).

42. With LSA and Trinity satisfied, Coventry purchased the policy on June 22, 2005 for a gross amount of \$140,000. The Seller never learned that two higher offers were made

or that LSA and Trinity both received payoffs in exchange for suppressing the higher bids. (COV2 0007162).

H. A company-owned policy insuring an 83 year-old man

43. In another case, Coventry and Advanced (acting on behalf of another Buyer) were competing to purchase an \$800,000 life insurance policy insuring an 83 year-old Florida man. In June 2005, Advanced had a bid from another Buyer for \$231,000, higher than Coventry's offer at that time of \$204,000. (AS008117). Scott Kirby, Co-President of Advanced, contacted Eileen Shovlin, Coventry's Regional Vice President, to discuss the policy. On July 20, 2005, she sent an email to Buerger and Dodaro noting that although Coventry and Advanced had been competing for the policy, "now that we are talking...they called me to discuss." Seeking approval of a co-broker payment to Advanced, she wrote: "Scott thinks 2 pts is fair on this. Pls advise." Dodaro responded by asking Jacobs whether there was any "room" to pay Advanced, and Jacobs replied "you can throw them [a] little cash." (COVJD 00009237-38). That same day, Dodaro sent an email to Shovlin and Coventry's accounting department, "1.5 pts to Advanced – Co-broker." (COVJD 00038350). Coventry purchased the policy for less than Advanced's \$231,000 competing offer on September 8, 2005: it paid \$185,000 to the Seller and \$19,000 in compensation to the Broker who closed the case. Coventry did "throw cash" to Advanced, specifically Coventry paid Advanced \$12,000 (1.5% of the death benefit). Not surprisingly, the payoff to Advanced was not disclosed to the Seller. (COV2-0001267).

I. A policy insuring an 85 year-old man

44. In January 2005, Coventry made a gross offer of \$135,000 on the policy insuring an 85 year-old Florida man with a \$400,000 death benefit. (COVNI 00028146). On February 8, 2005, Dodaro emailed Jacobs stating that LSA, representing a competing Buyer, had received a higher offer for the policy: "LSA can beat our 135K. How confident are we?" (COVNI 00012075). Jacobs explained that he lacked confidence that the Seller would close with Coventry if LSA did indeed have a higher offer noting, "Is LSA offer still good? if so, this guy would switch in a second so [I am] not very confident." (COVNI 00012075).

45. To ensure that Coventry would close the deal, Dodaro arranged for a \$5,000 co-broker payment to LSA and for Coventry to close the deal through another Broker, telling Jacobs, "I bought insurance for 5K." (COVJD 00023061, COVNI 00012075). The \$5,000 payoff, or "insurance," guaranteed that LSA would not submit a competing offer and therefore allow Coventry to close the deal at the original gross offer of \$135,000. Jacobs responded, "good idea even if they were bluffing." (COVNI 00012075). Coventry then purchased the policy on March 28, 2005, paying the Seller \$120,000 and the Broker who closed the deal \$15,000. Coventry also paid \$5,000 to LSA as a co-broker payment. The \$5,000 payment to LSA was never disclosed to the Seller.

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46. The above are illustrative cases; this Office's investigation has revealed literally dozens of other examples of bid rigging by Coventry and Brokers. Coventry has concluded that, in many cases, it is cheaper to pay off corrupted Brokers than to engage in

marketplace competition.

III. Coventry's Right of Last Offer

47. Until 2005, Coventry required nearly every Broker with which it does business to sign an agreement (never disclosed to Sellers), providing among other things that the Broker will provide Coventry with a "right of last offer to contract for a Life Settlement in respect of such Policy on terms that with respect to purchase price of the policy are more favorable to the seller than those set forth in the Competing Offer." (AS 020704). By exercising this provision, Coventry has the right to hold back in early stages of the bidding process, and then swoop down at the last moment with a matching or better offer. Under the terms of Coventry's contracts, and in violation of duties owed by the Broker to the Seller, the Broker cannot then return to the market to shop for a higher offer. As one Coventry manager put it: "We will always get right of last offer. The bidding system is simply for aesthetic reasons." (COVID 20709). In September 2006, Buerger invoked the Fifth Amendment when asked whether the purpose of the right of last offer clause was to prevent Brokers from soliciting competitive offers after Coventry invokes this right.

IV. Coventry's Corrupt Broker Compensation Practices

48. Coventry's gross offers corrupt the Broker-Seller relationship by undermining the Broker's duties to the Seller and creating perverse incentives to negotiate lower, instead of higher, selling prices for Sellers. While the Broker may profess to represent the client, in many cases the Broker conceals its conflict of interest and hides the fact that both the Broker and the Seller are competing for a slice of Coventry's gross offer. Coventry benefits from this

scheme by obtaining lower prices for the policies it purchases and by creating incentives for Brokers to steer additional business to it.

49. For example, if Coventry extends a gross offer of \$100,000 to purchase a life settlement, the Broker may decide to pass on \$70,000 to the Seller and keep \$30,000. However, if the Broker wishes to increase its compensation, it may try to convince the Seller to accept only \$60,000 for the policy, leaving \$40,000 for the Broker. In many cases, the Seller is never informed of the full amount or mechanics of Coventry's gross offer, and so never learns the full amount that Coventry was willing to pay for the policy or the amount of compensation taken by the Broker.

50. In one case already noted above, Coventry extended a gross offer of \$3.1 million to the Seller of a \$10 million life insurance policy. On or about December 6, 2004, prior to making the offer, a Coventry regional manager wrote to Neal Jacobs, asking whether the Broker, Eikonglobal, Inc., a New York City financial advisor, could allocate the \$3.1 million gross offer as \$2.8 million to the Seller and \$300,000 to the Broker. However, in a prior communication the Seller had demanded \$3,000,000 for his policy and Jacobs replied: "what happened to the client needing 3m." The Coventry regional manager replied: "I just want to let him [Eikonglobal] know whether he can keep the difference if [he] gets the offer accepted for less." (COV 462713). The next day, the Coventry regional manager updated Jacobs: "Client is holding out for 3m. [Eikonglobal] doesn't want to do the case for 100k comp. He is still trying to get client to take less." (COV 462717). Ultimately, Eikonglobal was successful in persuading the Seller to take less and thereby allowing Eikonglobal to take more: Coventry paid out a total

of \$3.1 million, the Seller received \$2,946,947 and Eikonglobal received \$153,053 in compensation. Coventry induced and participated in Eikonglobal's breach of duty to the Seller and no disclosure was made to the Seller regarding the Broker's compensation. (COV2 0009660).

51. To sweeten the offer, on or about December 8, 2004, Coventry also promised Eikonglobal another \$50,000 in deferred compensation contingent on Eikonglobal agreeing that it would not use Coventry's offer "to entice competitors to beat this offer." (COV 441505). Eikonglobal accepted the no-shopping language and Coventry made a record to pay Eikonglobal another \$50,000 on the next case it closed for Coventry. (COV 1119841, COV1 10137).

52. Brokers frequently negotiate gross offers for their sole benefit when they know they have reached an agreeable offer in the eyes of the Seller. In one case involving a family trust-owned policy on the life of a 77 year-old Nevada woman, Coventry was finalizing the contracts on a life settlement in which the Seller would receive \$275,000 for two policies and the Broker, Cavalier Associates, would receive \$31,000 in compensation. On or about June 20, 2005, Cavalier Associates emailed Coventry, stating "I just got an offer from Advanced [working on behalf of a competing Buyer] at 400K for both policies. . .this is enough for me to stop the Coventry paperwork. . .and start with [sic] over with the new offer. . .I don't need you to match it. . . but I do expect you to increase your offer to something close to that. . .I need to know today. . . this is a great file and I know you have room. . .let me know asap." (COVNI 00021301). Not wanting to risk losing the case to the higher offer, the next day, Coventry increased Cavalier

Associates's compensation from \$31,000 to \$100,000 and also paid Advanced \$100,000 as a co-broker payment. (COVNI 00024690). All the while, the Seller's compensation remained the same and no disclosure was made to the Seller of the co-broker payment or the higher offer. (COV2 007156, 007165).

53. Ostensibly to prevent Brokers from grabbing the lion's share of the compensation in every case, Coventry has adopted general "guidelines" that limit Broker compensation to the lesser of 6 percent of the life insurance policy's death benefit or 50 percent of its offer to the Seller. However Coventry frequently pays Brokers amounts in excess of these limits, using hidden deferred compensation or bonuses. Deferred compensation has two purposes: it allows Coventry to exceed its guidelines and it incentivizes Brokers to steer future clients to Coventry in order to collect the payoff.

54. In one case, Coventry extended a gross offer of \$2.535 million to purchase three policies with an aggregate death benefit of \$8 million insuring the lives of a couple in their eighties. The Broker, Cale W. Carson (also known as "Kit" Carson), divided this amount between himself and the Seller, and ultimately offered the Seller \$1,625,000, keeping \$910,000 for himself. Carson's proposed compensation, however, exceeded 6 percent of the \$8 million death benefit, and in a December 28, 2004 email, Reid Buerger told him that Coventry would not pay him more than 6 percent of the death benefit. Carson retaliated in an email to Coventry: "You are hereby notified that you are not to proceed further (send change forms to the carriers) on the above case until we speak, and get this situation clarified." (COV 1120238).

55. Rather than lose the deal, Buerger wrote back the next day: "as a follow up to our conversation compensation for the above case will be 6%, or 480k. In addition, per our conversation we will be paying the 120k." (COV-1102963). Coventry's internal accounting records show that Carson, indeed, received \$480,000 compensation plus an additional \$120,000 in bonus for a total of \$600,000 for the transaction. Coventry also awarded Carson an additional \$75,000 in deferred compensation, for a total compensation package of \$675,000. (COV 32402-32403). Notably, Coventry's records provide no indication that the Seller was informed that Coventry was actually willing to buy the policy for \$2.535 million (as opposed to \$1.625 million), and that at least \$675,000 was siphoned off in Broker compensation. (COV2 0009657-58). In September 2006, Reid Buerger invoked the Fifth Amendment when asked why he agreed to pay Carson above the 6% guideline.

56. In certain instances Broker compensation in fact exceeded the selling price offered to the Seller. The egregious nature of such deals was not lost on the participants in the life settlement. In an email dated October 20, 2004, a representative from Berkshire Hathaway, one Coventry investor, wrote to AIG, another Coventry investor, to question Broker compensation on a life settlement negotiated for them by Coventry: "Can I get a little color on this one, please. \$130,875 to the seller, and \$857,500 of commissions??? Am I missing something?" In separate emails, AIG and Coventry's CEO Alan Buerger responded, noting that deducting Coventry's \$400,000 customary fee, Broker compensation was only \$457,500, and taking into account a premium reimbursement payment, Seller's compensation would be

\$365,000. (COV. 1066288). After these adjustments, Coventry still paid the Broker \$92,500 more than the Seller.

57. Coventry and its founder Alan Buerger are familiar with gross offers because prior to becoming a Buyer, Coventry benefitted from gross offers as a Broker. In 2000, Coventry, as a Broker, worked out an arrangement whereby it would split 50-50 with a Buyer any savings it obtained by negotiating a lower sales price with a Seller of a policy insuring a 66 year-old man from California. Thus, in the September 2000 transaction, where Coventry negotiated a \$20,000 reduction in the purchase price, the Buyer wrote Coventry: "On the 2mill policy we gave you an offer of \$450,000 you negotiated [sic] a new purchase price of \$430,000 split 50/50 extra 10k to you." In other words, since Coventry convinced the Seller to take \$20,000 less than what the Buyer offered, Coventry and Buyer would split the difference and each walk away with an extra \$10,000. Not content with his 50 percent cut on the reduced purchase price, Reid Buerger responded, with a copy to Coventry's CEO Alan Buerger, "We were not supposed to split this one 50/50, it was to be 100% to us." The Buyer, confused by this departure from the usual practice of evenly splitting the savings, replied: "Why would we not split this one. Our policy was everything negotiated [sic] down we always split 50/50. Who approved this!!!" (COV-1032560).

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58. The above, again, are illustrative cases; this Office's investigation has revealed literally hundreds of examples of gross offers extended by Coventry and other Buyers.

In more than 200 cases, the Broker receives half or more of what the Seller receives. The use of gross offers has become pervasive in the life settlement business.

V. Coventry Creates False and Misleading Documentation

59. Coventry touts itself as having "exact[ing]" due diligence and "conduct[ing] our business transparently." (COV1 00322). However, in many instances it directly participates in the Broker's breach of its duty to the Seller by failing to disclose Broker compensation to the Seller and by falsifying any paperwork the Seller sees to show less compensation than is actually paid.

60. Coventry has two major incentives not to disclose the full measure of compensation to the Seller: (1) providing sweetheart deals to Brokers incentivizes Brokers to continue to do business with Coventry, and (2) disclosing compensation, especially when compensation is high in relation to the purchase price, may cause a Seller to reconsider closing a deal or rescind a deal that is still within the rescission period⁶.

61. Coventry's standard practice when the Seller or a representative of the Seller inquires about Broker compensation is to direct the Seller to the Broker. For example, on April 22, 2003, the trustee of a New York life insurance trust contacted Coventry seeking information about how much Advanced, the Broker on the deal, would be paid on the life settlement. Reid Buerger responded: "just tell him this is not information we are at liberty to

⁶In most states, life settlements and viaticals are subject to a two-week rescission period, during which the Seller can unwind the transaction for any reason. (National Association of Insurance Commissioners (NAIC) model regulations providing for a fifteen day rescission period.)

provide.” (COV 1113128). In September 2006, Buerger invoked the Fifth Amendment when asked about this matter. In another email dated March 25, 2003, a Coventry Regional Director wrote to a Broker: “Compensation disclosure is determined by state regulation. Assuming the policy owner resides in the state of Wisconsin (life settlements are not regulated in Wisconsin), there would not be any compensation disclosure. Coventry First would direct any inquiries by the policy owner and/or insured regarding compensation to your office.” (COV-1112858).

62. When pressed, Coventry has agreed to falsify documents. In one example, involving a policy insuring an 80 year-old New York man, the Seller received from Coventry \$317,000, the primary Broker received \$11,250 and another Broker in the distribution chain received \$3,750. (BIS002136). On July 27, 2004, Coventry sent offer sheets to both Brokers *reflecting the agreed-upon compensation. The next day, both Brokers signed and returned the offer sheets to Coventry, marking the end of the bidding process.* (COV2 0009420-9425). Subsequently, one of the Seller’s advisors contacted the first Broker and inquired as to the amount of compensation that he was to receive. In response to this inquiry and at the first Broker’s request, Coventry falsified the offer sheets making it appear that the first Broker had only received \$1,250 in total compensation instead of the \$11,250 he actually received. In fact, the first Broker received the remaining \$10,000 as an undisclosed “bonus.” (BIS002207-2209). To cover up the scheme, on August 31, 2004, Coventry also emailed the falsified offer sheets to the second Broker for his signature. The second Broker signed and returned the new offer sheets to Coventry on September 2, 2004. (COV2 0009430). The false offer sheets were explicitly created to hide the full measure of compensation paid on this policy.

63. Even in so-called "disclosure states"⁷ where Coventry is statutorily required to disclose Broker compensation to the Seller, it often understates or misleads the Seller as to the Broker's compensation. This investigation has uncovered numerous occasions where co-broker fees and/or deferred compensation was not disclosed to the Seller. It was not until July 20, 2006 - - a year after this Office's investigation began - - that Coventry put in writing a policy requiring disclosure of all Broker compensation in such states. (COV2 0009661-662).

64. For example, in one case involving a family-owned policy insuring an 87 year-old man from Nevada (which requires disclosure), Coventry agreed to pay a total of \$42,000 in compensation, \$21,000 to LSA and \$21,000 to Advanced. Coventry, however, did not want to disclose the entire \$42,000 in compensation on the Exhibit A disclosure form attached to the Purchase Agreement, and so, on December 22, 2004, Jim Dodaro emailed Reid Buerger and others at Coventry, suggesting that they could keep \$22,000 off the Exhibit A by calling it deferred compensation and co-broker fees: "Total comp is 42K to LSA (they were paying Advanced 21K of it). Looks like we have to do a new Ex A disclosing comp. Can we lower the gross offer by 22K, put 20K comp on the Ex A, defer 1K to LSA and pay 21K to Advance as co-broker?" (COV 1120443). Following Dodaro's suggestion, Coventry disclosed only \$20,000 on the Exhibit A to the Seller. The remaining \$22,000 was paid to the Brokers as deferred compensation and co-broker payment and never disclosed to the Seller. (COVJD

⁷ States currently requiring disclosure of Broker compensation include Arkansas, Florida, Indiana, Kansas, Kentucky, Nebraska, Nevada, North Carolina, North Dakota, Ohio, Pennsylvania, Tennessee and Utah. Statutes in these States, though not uniform, generally require that the Buyer of a life settlement disclose to the Seller the amount of Broker compensation being paid.

00025548, COV2 0007152). In September 2006, Buerger invoked the Fifth Amendment when asked why he agreed to alter the Exhibit A.

FIRST CAUSE OF ACTION

(Fraudulent business practices – Executive Law § 63(12))

65. The acts and practices alleged herein constitute conduct proscribed by § 63(12) of the Executive Law, in that Defendants have engaged in repeated fraudulent or illegal acts or otherwise demonstrated persistent fraud or illegality in the carrying on, conducting or transaction of business.

SECOND CAUSE OF ACTION

(Anti-Competitive Behavior – Gen. Bus. L. § 340 *et seq.*)

66. Beginning no later than 2001 and continuing through in or about 2006, Defendants and others conspired unreasonably to restrain trade and commerce in violation of General Business Law § 340 *et seq.* by, among other things: (1) providing owners seeking to sell their life insurance policies in the secondary market with collusive, fictitious or otherwise non-competitive bids or other terms of sale; (2) allocating the opportunity to purchase, and the purchase of, life insurance policies to particular Buyers and Brokers; and (3) creating a scheme to pay Brokers to participate in and implement the unlawful conspiracy.

67. As a result of this conspiracy, Sellers received cash settlements on terms less favorable than would have been available in a competitive market and were denied to opportunity to offer their life insurance policies for sale, and to sell their policies, under free and open competitive conditions.

68. Defendants' acts are *per se* violations of General Business Law § 340 *et seq.*

69. Various persons, not named as defendants, participated as co-conspirators in the violations alleged and performed acts and made statements in furtherance of that conspiracy.

THIRD CAUSE OF ACTION
(Securities Violations – Gen. Bus. L. § 352 *et seq.*)

70. To the extent that Defendants engaged in life settlement transactions involving variable life insurance policies, the acts and practices of Defendants alleged herein violated Article 23-A of the General Business Law, in that Defendants engaged in the artifice, agreement, device or scheme to obtain money, profit or property by a means prohibited by § 352-c of the General Business Law.

FOURTH CAUSE OF ACTION
(Common Law Fraud)

71. The acts and practices of Defendants alleged herein constitute actual and/or constructive fraud under the common law of the State of New York.

FIFTH CAUSE OF ACTION
(Unjust Enrichment)

72. By engaging in the acts and conduct described above, Defendants unjustly enriched themselves and deprived policy owners and the investing public of a fair market place.

SIXTH CAUSE OF ACTION
(Inducement of Breach of Fiduciary Duty)

73. By engaging in the acts and conduct described above, Coventry aided and

abetted, participated in, and benefitted from Brokers and others' breach of their fiduciary duties to their clients.

WHEREFORE, Plaintiff demands judgment against the Defendants as follows:

A. Enjoining and restraining Defendants, its affiliates, assignees, subsidiaries, successors and transferees, their officers, directors, partners, agents and employees, and all other persons acting or claiming to act on their behalf or in concert with it, from engaging in any conduct, conspiracy, contract, or agreement, and from adopting or following any practice, plan, program, scheme, artifice or device similar to, or having a purpose and effect similar to, the conduct complained of above.

B. Directing that Defendants, pursuant to section 63(12) of the Executive Law and the common law of the State of New York, disgorge all gains and pay all restitution and damages as provided by law and caused, directly or indirectly by the fraudulent and deceptive acts complained of herein;

C. Directing that Defendants, pursuant to section 63(12) of the Executive Law, offer the right of rescission to all Sellers who entered into Purchase Agreements with Defendant Coventry from 2001 to the present;

D. Directing that Defendants pay punitive damages;

E. Directing that Defendants pay three-fold damages;

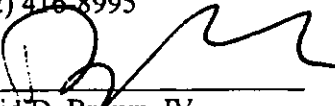
F. Directing that Defendants pay Plaintiff's costs, including attorneys' fees as provided by law;

G. Directing such other equitable relief as may be necessary to redress
Defendants' violations of New York law; and

H. Granting such other and further relief as may be just and proper.

Dated: New York, New York
October 26, 2006

ELIOT SPITZER
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December 17, 2006

Late in Life, Finding a Bonanza in Life Insurance

By CHARLES DUHIGG

Marvin Margolis, an 80-year-old Manhattan financial consultant, is looking for investors willing to bet on when he will die.

Two years ago, Mr. Margolis bought a large life insurance policy. Now, he's considering selling it to a group of investors, a deal that should give him as much as \$2 million to enjoy in his final years. In return, the investors will get the policy's \$7 million payout when he dies — which they hope will be soon, so they can stop paying his premiums.

"This is a wonderful opportunity to use my body as an asset," Mr. Margolis said. "I deserve to be able to benefit in some way from my age."

Trading in life insurance policies held by wealthy seniors has quietly become a big business. Hedge funds, financial institutions like Credit Suisse and Deutsche Bank, and investors like Warren E. Buffett are spending billions to buy life insurance policies from the elderly. Other investors are paying seniors to apply for life insurance, lending them money to buy the policies, and then reselling them to speculators.

This nascent market illustrates one way that investors are hoping to make money from a large and wealthy generation of Americans as they reach retirement age. These aging baby boomers and those even older offer both opportunities and risks for many companies, investors and swindlers seeking to capitalize on their final years.

Insurance executives, for instance, say transactions like Mr. Margolis's may cripple their industry and make it harder for the average senior to buy life insurance in the first place. Insurers are worried because they count on many customers canceling their policies before they die, usually because their children grow up and no longer need the financial protection, their pensions kick in or premiums become too expensive. If far more policies result in payouts, the insurance business becomes much less profitable.

Indeed, industry analysts say they expect the cost of life insurance to rise as companies prepare to pay out more claims.

"If payouts increase, the cost of insuring people is effectively going up, and that will definitely increase the price of policies," said J. David Cummins, a professor at the Wharton School of the University of Pennsylvania.

While that may be the case, many people have come to rely on selling their policies to provide urgently needed money for medical care and living expenses when their bank accounts run dry. However, insurance executives say that the market that has emerged could be ruinous.

"Life insurance is a way for individuals to protect their families," said C. Robert Henrikson, the chief executive of MetLife. "If someone profits from a stranger's death, it stands the whole purpose of life insurance on its head. Anything that disrupts the economic processes underlying this industry will drive the cost of life insurance through the ceiling."

Policies like Mr. Margolis's cause particular concern. It was originally paid for with a loan from speculators who will get their money back, plus a profit, if it is sold to another group of investors, according to public documents. Even if Mr. Margolis does not sell, the loan will be repaid from the death benefit when he dies.

Such policies are known as speculator-initiated life insurance, or "spin-life" policies. Investors estimate that spin-life policies worth as much as \$13 billion will change hands next year.

The deals are so lucrative that older people are being wooed in every fathomable way. In Florida, investors have sponsored free cruises for seniors willing to undergo physical exams and apply for life insurance while onboard.

For insurers, such cruises are a financial Titanic. Over the next decade, the insurance industry could be forced to pay out unexpectedly more than \$100 billion in death benefits as spin-life policies come to maturity, investors estimate.

In Minnesota, according to lawsuits brought by insurers, an 82-year-old named John R. Paulson bought life policies worth \$120 million from seven companies and resold many of them before insurance companies realized what was going on and sued, saying that Mr. Paulson had lied on his applications.

Life insurance companies, in particular, rely on policies lapsing before the policyholder dies. Last year, for instance, insurance companies reduced their financial exposure by \$1.1 trillion when 19.8 million policyholders stopped paying premiums, according to the Insurance Information Institute. In comparison, the industry paid death benefits on only 2.2 million policies.

If those lapsed policies had been sold to investors rather than canceled, insurance companies could have eventually paid out as much as a trillion dollars, say analysts.

In an attempt to mitigate such risk, some insurance companies are trying to make policies for seniors harder to buy. The biggest insurer in the United States, American International Group, earlier this year increased prices on some universal life policies for buyers more than 70 years old in an effort to thwart spin-life deals.

"We don't want this business, and we're taking steps to discourage those purchasers from coming through our doors," an A.I.G. spokesman said.

But such moves may be too late. The market for purchasing life insurance policies from seniors is an outgrowth of the so-called viatical industry that began in the 1980s, when investors bought up life insurance policies of AIDS patients. In the last two years, as interest rates and stock market returns have declined, the number of buyers seeking seniors' policies has soared.

That growth was fueled this year when the Financial Accounting Standards Board issued rules permitting investors to record purchases of policies immediately as a profit, rather than forcing them to wait until the policyholder died.

Critics contend the industry punishes the young and healthy, by driving up prices, but many people who have sold their policies say it offered their only way to avoid calamity.

"If I hadn't been able to sell this policy we would have lost our house, all of our savings, everything," said Andrew Schneider of Kaysville, Utah. Seven years ago his wife, Karen, learned she had breast cancer. Her expenses exceeded the Schneiders' medical insurance by half a million dollars. Mrs. Schneider sold her life insurance policy for about \$250,000 and used the money to buy medicine and pay bills, he said. The investors who bought her policy received a \$500,000 death benefit when she died last year.

"Selling that policy extended her life for years," said Mr. Schneider. "If this market hadn't existed, we would have become financially destitute."

Finding enough life insurance policies to satisfy investor hunger has proved difficult. So, in addition to the free cruises in Florida, investors including one large hedge fund have hired a California telemarketing company to call elderly citizens and ask if they would apply for life insurance in exchange for a paycheck.

The insurance industry has begun to fight back. Legislatures in New Jersey, New York and nine

other states have proposed laws intended to outlaw spin-life investments or make it more difficult for investors to get payouts, according to the Life Insurance Settlement Association.

Insurance companies have also sued to cancel policies, contending that payouts benefiting outside investors violate the legal requirement that beneficiaries have an "insurable interest" in the policyholder's life.

But many advocates for the elderly and industry insiders worry that seniors will lose their legitimate ability to sell life insurance policies they have held for years.

"We've put billions of dollars in the hands of seniors who were getting thrown out of their homes or needed medication, and their only asset was a life insurance policy," said Scott Page, chief executive of the Lifeline Program, a company that helps investors buy life insurance policies from the elderly and infirm. "If you make it harder to sell these policies, you're taking money out of the hands of people who have nothing else."

Another risk is that seniors hoping to sell their life insurance policies will be stuck in bad deals. In October, the New York attorney general, Eliot Spitzer, filed a lawsuit accusing one life insurance speculator, Coventry Financial, of bid-rigging and other fraud in acquiring more than \$3.6 billion in life insurance policies. Coventry said it would fight the suit.

A lawyer who has helped the elderly set up spin-life arrangements worth more than \$300 million said that often the terms of the deals prevented his clients from profiting.

"Investors say, 'I'll loan you money to buy a new policy, and in a few years I'll buy it from you,'" said Larry Brody, a partner at the law firm Bryan Cave. But a few years later, when the seniors sell the policy, they owe so much in interest and fees on the loan, he said, "it eats up all the profit. And what's more, they can't buy another insurance policy, because insurers are unwilling to give them more coverage."

But those risks are worth the trouble, according to some buyers and sellers. In 2004, Irene Randall, a life-settlement broker in Albuquerque, N.M., set up an \$8 million spin-life policy for her 82-year-old uncle with investors who agreed to lend him money for the premiums. In return, she said, the company hopes to buy the policy next year, paying her uncle \$1.5 million.

Ms. Randall called it a great deal and said she was setting up a similar arrangement for her 82-year-old mother. She expects both her mother and uncle will live long enough to enjoy the windfall. "The one thing we know is that everyone is going to die at some point," said Ms. Randall. "If someone is willing to pay you because you're old, why not try and live it up before

then?"

Jenny Anderson contributed reporting.

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December 19, 2006



Legal & General America, Inc.

The Honorable Jim Poolman
Commissioner of Insurance
North Dakota Insurance Department
State Capitol, Fifth Floor
600 East Boulevard Avenue
Bismarck, ND 58505-0320

1701 Research Boulevard
Rockville, Maryland 20850
(800) 638-8428

Re: STOLI Amendments to Viatical Settlements Model Regulation

Dear Commissioner Poolman:

On behalf of the Legal & General America Companies--and as a fellow native of North Dakota and graduate of the University of North Dakota with several family members in North Dakota--I wanted to take this opportunity to express my sincere appreciation for your recent efforts in guiding through the recent adoption of some important amendments to the Viatical Settlements Model Regulation. Your accomplishments on this subject represent an important step in eliminating these abusive practices.

As you know, true life insurance serves an important social benefit by helping families and businesses upon the death of a loved one or key business partner. I firmly believe that such Stranger-Originated Life Insurance threatens this vital function, and is subject to multiple forms of abuse. Some of these abuses are being publicly debated, but others are less well known but have the potential to result in great personal tragedy. Set forth below is a description of how these practices can result in situations with potentially terrible consequences.

Our subsidiary, Banner Life Insurance Company, recently received an order from the U.S. Attorney's office in West Palm Beach, Florida, working with the Department of Homeland Security, requiring the forfeiture and change of ownership on life insurance policies once owned or partially owned by a now-defunct life settlement company. This case involves cocaine trafficking and money laundering, as investigations have revealed that Colombian narcotics cartels have been hiding and laundering money through investment accounts and life insurance policies.

In November 2001, almost exactly 2 years after its original sale (two years being critical to avoid the standard contestable clause), a Banner Life Insurance Policy issued on the life of an elderly gentleman in Florida was sold to Mutual Benefits Corporation ("MBC"). MBC is a now defunct Florida-based life settlement company that is currently in receivership. Unknown to Banner Life or any of the other life insurance companies whose policies it had purchased, MBC sold certain policy interests to persons involved with cocaine transporting and distribution operations and Colombian narcotics cartels

with their corresponding money-laundering activities. I would be happy to provide you with a copy of the government's Forfeiture Complaint that describes the actions that could have endangered the lives of policyholders across the country.

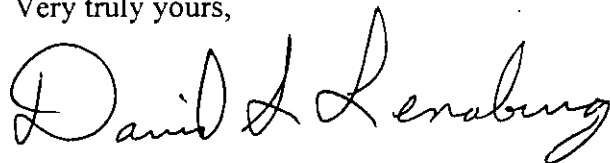
It should be instructive to everyone that before law enforcement stepped in, the result of this STOLI transaction--which given its timing was almost certainly intended from inception--was that our insured, an 86-year old retired Lake Worth, Florida resident, sold his policy and apparently ended up with a drug cartel owning a vested interest in his early demise. The insureds from the other carriers also sold their policies, indirectly and unknowingly, to a drug cartel with a vested interest in their premature death. Nothing good can come of this, and the potential for tragedy is shocking.

Fortunately, in this case, Banner Life stands, at worst, to suffer only a significant, but sustainable, financial loss, and our insured appears to have been fortunate that the ownership of the policy has been forfeited to the United States Government and is no longer owned by anyone who might seek to do him harm. The next person insured in any similar scheme might not be so lucky. I cannot think of a good reason for such transactions, and I strongly urge you to continue with your attempts to end these abusive practices. Such action could well serve to prevent a tragedy.

I applaud your efforts in this area and hope that you share my concerns about the potential abuses that seem to be part and parcel of STOLI policies. The Legal & General American Companies fully support your initiatives in attempting to eliminate these reprehensible business practices.

I would welcome the opportunity to discuss the matter with you. Please feel free to contact me at (301) 279-4817 or our general counsel, Bryan Newcombe at (301) 294-6968 at your convenience should you need any further information about this matter.

Very truly yours,

A handwritten signature in black ink, reading "David S. Lenaburg". The signature is written in a cursive style with a large, stylized "D" and "L".

David S. Lenaburg
President and Chief Executive Officer

PROPOSED AMENDMENTS TO SENATE BILL NO. 2269
(Sponsored by the North Dakota Bankers Association)

Page 2, line 2, remove "or other agreement"

Page 7, replace lines 1 through 5, with "A loan made by a bank or other licensed financial institution in which the lender takes an interest in a life insurance policy solely to secure repayment of the loan or, if there is a default on such loan and the policy is transferred, the further assignment of such a policy by the lender, provided that the default itself is not pursuant to an agreement or understanding with any other person for the purpose of evading regulation under this chapter."

Page 8, line 19, after "credit union" insert a semi-colon and, remove "other"

Page 8, line 20, insert "(2) A" before "licensed"

Page 8, line 24, replace "(2)" with "(3)"

Page 8, line 25, replace "(3)" with "(4)"

Page 8, line 28, replace "(4)" with "(5)"

Page 8, line 31, replace "(5)" with "(6)"

Page 9, line 1, replace "(6)" with "(7)"

Page 9, line 2, replace "(7)" with "(8)"

Page 9, line 3, replace "(8)" with "(9)"

Page 9, line 4, replace "(9)" with "(10)"

Page 34, line 5, after "provider", insert "or it is otherwise conclusively shown by the viatical settlement provider"

Page 34, line 22, replace the semi-colon with a period and, remove "or"

Page 34, line 23, replace "(6)" with "c."

Page 34, lines 23 through 27, adjust margins

Page 34, line 25, after "viator", insert "in default."

Page 34, line 28, replace "c" with "d"

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#7. *AK*

Renumber accordingly

2268
#2



**STATEMENT OF FRANK A. KEATING
PRESIDENT AND CEO
AMERICAN COUNCIL OF LIFE INSURERS**

**MADE TO THE
LIFE INSURANCE AND ANNUITIES (A) COMMITTEE
OF THE
NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS
AT ITS HEARING ON
"PREMIUM FINANCING OF LIFE INSURANCE, LIFE SETTLEMENTS AND
THE RELATIONSHIP WITH STATE INSURABLE INTEREST LAWS"**

**May 3, 2006
Westin Times Square Hotel
New York, NY**

2268
#3

**STATEMENT OF FRANK A. KEATING
PRESIDENT AND CEO
AMERICAN COUNCIL OF LIFE INSURERS**

Good afternoon, Chairman Poolman, Superintendent Mills and members of the Committee. My name is Frank Keating, and I am President and CEO of the American Council of Life Insurers (ACLI). ACLI is a national trade association whose 377 members account for over 90 percent of the life insurance in force in the United States. I am delighted to participate in today's NAIC hearing on "Premium Financing of Life Insurance, Life Settlements and the Relationship to State Insurable Interest Laws."

Life insurance provides guaranteed financial security for millions of American families. It serves a critical social purpose – enabling families to sustain financially if a breadwinner dies, and allowing businesses to continue to operate when owners and key employees die. Congress has long afforded special tax treatment for life insurance benefits in recognition of the important role the product plays in our society.

An essential precept of life insurance is the owner of a policy must have an interest in the continued life of the insured person, and will suffer an economic or financial loss if the insured person dies. The doctrine of "insurable interest" has been recognized for centuries and remains one of the most fundamentally important principles of the life insurance today.

Recently, however, we have witnessed the proliferation of certain investor-initiated life insurance transactions in which speculative investors, who have no relationship to insured persons and no interest in their continued good health, are allowed to profit from the insured's death. Clearly, these types of transactions abuse the social purpose of life insurance, circumvent the letter and spirit of insurable interest laws, and threaten the viability of a product that has provided essential financial security to generations of Americans.

Before I elaborate further on so-called "investor-initiated" or "stranger-owned" life insurance transactions, allow me to say up front that we have no quarrel with traditional, legitimate viatical settlements or life settlements. We understand that policyholders who face extraordinary medical expenses or whose financial protection needs have changed may, after considering the ramifications, decide to sell their policies in the secondary market. Nor do we believe that legitimate premium financing arrangements, which permit consumers to afford or maintain important life insurance coverage that would otherwise be beyond their reach, are inherently bad.

Rather, our strong objection is with those schemes initiated by some investor groups that are designed to generate life insurance policies for sale in the secondary market.

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There are many variations of "stranger owned" or "stranger initiated" life insurance transactions. These transactions are often referred to by the acronym of "STOLI". STOLI transactions are designed to allow outside investors to own life insurance policies on the lives of strangers, thus circumventing state insurable interest laws. Most often, older high net worth individuals (typically 70 or older with a net worth in excess of \$1,000,000) are offered the chance to obtain substantial amounts of life insurance without cost. These individuals are sought because of their relatively short life expectancy and their ability to qualify for a substantial amount of life insurance. Here are the distinguishing features of STOLI:

- Each program provides some form of incentive to the insured for participating and has some mechanism to make sure that the insured incurs no cost for the program.
- Incentives provided to the insured include free insurance for a period of time and, in some programs, cash compensation, either at the start or on a later sale of the policy in the secondary market.
- Generally, the insured is loaned the money to pay premiums for a certain time, usually 2-5 years. The 2-5 year period generally is chosen to ensure that the policy is no longer contestable after transfer. Some programs offer the insured more cash than necessary to pay premiums.
- A key feature is that the insured is able to walk away from the debt without cost and without any liability.
- If the insured survives the initial 2-5 year period, he or she typically is given the option of repaying the loan, or transferring ownership of the policy in complete satisfaction of the debt. Realistically, the STOLI arrangement is designed so that the insured will transfer the policy to satisfy the debt, because the cost to repay the loan plus other fees and charges is so high that it is infeasible economically to pay.
- If the insured dies during the 2-5 year period, the net death benefit (death benefits reduced by loan repayment) is generally paid to the insured's

beneficiaries. However, the lender is betting that the insured will live longer than the initial period, resulting in the proceeds being paid to the lender.

- An alternate program design (loan for life) does not require the transfer of the policy after an initial term. While the insured may continue as named owner of the policy, this program requires the assignment to the lender/investor of upwards of 90% of the death benefits, even though only a single annual premium may have been borrowed and paid on the policy.
- Each arrangement is designed to achieve one goal: to allow investors without an insurable interest to own policies on the lives of strangers.

Although the details of these programs vary, they fundamentally are at odds with the spirit and intent of the centuries-old insurable interest principle, which dictates that the owner of a life insurance policy must have an interest in the continued life of the insured person, and not a mercenary, investment interest in the person's death.

I would also note that STOLI programs differ from traditional premium financing in significant ways. Under STOLI, the policyholder is not at risk for paying premium out of pocket or from assets (other than the life policy) posted as collateral, which is typically not the case with traditional premium financing. Additionally, under STOLI the potential investment return to the lender/investor is often significantly greater than is the case in traditional premium financing because the return to the STOLI investor is tied directly to mortality. Finally, a STOLI transaction is initiated by the lender/investor and is structured specifically to result in the eventual acquisition of the policy by the lender/investor.

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Mr. Chairman, we understand that one of the many purposes of this hearing is to begin the process of determining how to tighten the NAIC Viatical Settlement Model Act to prohibit "stranger-owned" and "investor initiated" life insurance transactions. Over the past few months, representatives from numerous ACLI member companies have worked through our committee process to develop amendments to the NAIC Model Act to prohibit abuses of the life insurance product that may be facilitated through loopholes in the settlement laws. During this process we worked closely with the life insurance producer community, and I am pleased to report that these amendments enjoy the support of the Association for Advanced Life Underwriting (AALU), the National Association of Insurance and Financial Advisors (NAIFA), and the National Association of Independent Life Brokerage Agencies (NAILBA). A mark-up of the NAIC Model Act reflecting the amendments we propose was distributed to NAIC staff yesterday.

In essence, the amendments we offer for your consideration expand the definition of "viatical settlement contract" in Section 2 of the Model Act to include stranger-owned life insurance transactions such as those I have just described. By defining these transactions as viatical settlement contracts, they become prohibited practices under Section 10 of the Model Act if they are entered into at any time prior to or within two years after issuance of the life insurance policy. Additional amendments tighten Section 10 by eliminating loopholes that further facilitate the speculative use of life insurance. We look forward to working with

you and members of the Committee as your process moves forward so that these important amendments can be incorporated into the NAIC Model Act.

As you consider these amendments, I strongly encourage you and your fellow regulators to look beyond the Model Act for ways to crack down on abuses of the life insurance product by speculators in the marketplace. I would like to take this opportunity to express our appreciation for the leadership on this issue shown by New York Superintendent Howard Mills, who recently issued an opinion concluding that a certain type of stranger-owned life insurance transaction lacked insurable interest because it appeared that the arrangement was intended "to facilitate the procurement of policies solely for resale." Insurance regulators can and should undertake a review of their state's insurable interest laws as an important step toward determining, as New York has done, that STOLI transactions violate the letter or spirit of these laws.

Mr. Chairman and members of the Committee, I thank you for inviting me to speak this afternoon, and I appreciate the opportunity you gave me to present our members' views on this critically important issue. We are eager to work with you as you take appropriate steps to address the misuse by speculators of a product that is vital to the financial security of millions of Americans.

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Stranger-Owned Life Insurance: Killing the Goose That Lays Golden Eggs!

By Stephan R. Leimberg

Stephan R. Leimberg is CEO of Leimberg Information Services, provider of information and commentary on recent cases, rulings, regulations, and legislation involving estate, financial, employee benefit, retirement, asset protection, charitable, and elder-care planning. He is co-author with Howard Zaritsky of *Tax Planning With Life Insurance and Tools and Techniques of Life Insurance Planning* with Robert Doyle. Leimberg is co-creator of NumberCruncher Estate Planning Software.

This article has been updated and expanded from the version originally published in *Estate Planning Journal*, January 2005. It is reprinted here with the author's permission.

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The Something-for-Nothing, 'No Risk' Pitch

"Yo, Buddy, want some free life insurance? Better yet, we'll not only pay all the premiums on the policy, but we'll also pay you!"

Promoters are placing huge policies on the lives of strangers, people on whose lives they have no insurable interest — no previous economic or family relationship or interest in the continuation of the insured's life — with a pitch that goes something like this:

"You purchase \$10 million of insurance on your life.¹ We'll advance the premiums for two years at an interest rate



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of 12 to 15 percent and take a collateral assignment on the policy. You pay nothing. You don't even have to pay any interest — it accrues with the loan. At the end of two years, if you want to continue the coverage, you pay us the interest you owe and repay the principal. It's a nonrecourse loan. That means you risk nothing. If you don't want the coverage at the end of two years, no problem

— we'll take over the policy and you have no liability. You owe nothing. Or you can sell the policy on the open market for cash to a so-called life settlement company. Best of all, we'll pay you \$250,000 in cash upfront² to sweeten the deal."

Of course, this "free insurance for two years," a/k/a "non-recourse premium financing" scheme, is a thinly disguised attempt to skirt state insurable interest laws³ and create a market for huge amounts of insurance on foolhardy individuals' lives (Would you allow a stranger or group of unknown individuals to purchase a \$10 million policy on your life? How about a \$1 million or \$100,000 policy?).⁴ Investors are now treating people's lives as fungible assets, just like stocks and bonds are assets, and they are in essence paying the insured to use their insurability. Adviser David Howell summed up the deal this way: "One of several risks to the insured is that he alone hopes he lives a long time. He has no control over who eventually will own the contract on his life, and he should understand that the return on their investment varies inversely with the number of years he lives."

¹The insured is paid an upfront "settlement" to take out a policy on his or her life. A bank or life settlement company takes a collateral assignment of benefits and pays the premiums for two years — a loan with interest. The insured gets the insurance for two years but then must decide whether to keep the policy. If so, he or she must pay the bank or life settlement company back with interest. This is an effort to skirt the standard two-year prohibition against viatication. It also raises many of the same policy issues as charitable SOLI described below.

²Sometimes the proposed insured is offered a share in the amount in excess of the loan when the policy is sold at the end of the 2 years, or 28 months in some cases, to a viatical company.

³If an insurance company finds that a policy was purchased with no insurable interest, the policy will be void from the time it was issued.

⁴Are these products rigorously competitive (or even sufficiently flexible) designs that insureds would likely want to purchase just in case they want to keep the insurance? Is there a disclosure issue here?

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Is this a form of split dollar? Is the lender sharing the commissions with the agent on either the front end or on the life settlement? Is the policy deliberately rigged so that it will be unappealing or unaffordable to keep it after the "free insurance" period (thus making it an almost sure thing that the insured will choose to allow it to pass to the investors)? Once the debt has been extinguished, will the insured have taxable income? If there is an upfront "sweetener," is it an illegal rebate? Is it reportable as ordinary income by the recipient? Does the rate of interest charged violate state usury laws? Is this an unregistered security? What liability do those involved have if it is? Will the issuance and continued existence of the policy significantly reduce the insured's ability to purchase needed insurance in the future? Is there a transfer for value? Has the insured who fails to disclose the true and complete nature of the life insurance purchase engaged in a fraud on the insurance carrier? If so, can the carrier rescind the policy based on a misstatement of a material contract fact? These and other questions are seldom covered by promoters of the "non-recourse premium financing" scheme, which looks more like a bridge for strangers who want to own insurance on the lives of strangers.

Here's what Jefferson Pilot, a major insurance carrier, had to say about stranger-owned life insurance (SOLI):

Jefferson Pilot Financial (JPF) has become increasingly concerned that individuals are being recruited to consent to the purchase of life insurance and annuities on their lives. In some instances, the individual is told that a charity will receive part of the death benefit at no cost to the charity. In other instances, the individual is told that they can receive "free" insurance coverage for a year or two, with the option to retain the policy by repaying the loan. Some concepts also contemplate a life settlement of the policy. Because the "strangers" or "investors" financing these programs are not interested in long-term investments, these programs typically target an older individual with high net worth that can qualify for large amounts of insurance.

We all have a stake in protecting our franchise, our reputation and our industry — including the tax-favored status of our products. For all these reasons, and until a change occurs that would merit reconsideration of our position, JPF will no longer accept applications for life or annuity policies sold under SOLI or IOLI [investor-owned life insurance] programs. If you know or should know that a SOLI or IOLI program is involved, you are asked and instructed not to submit applications to a JPF insurer. Submission of an application and violation of this policy will result in disciplinary action, up to and including, termination for cause. There are numerous variations on SOLI and IOLI, and Jefferson Pilot Financial is not interested in selling life insurance or annuities as part of any of them.

The life insurance industry, including NAIFA, AALU and the ACLI, is united in opposing this new approach to selling large amounts of insurance. Further, there are rumblings in state legislatures about changes to insurable interest laws, and proposals circulating in Washington that specifically target these programs. The President's budget for fiscal 2006 and the Treasury Department's proposal include a nondeductible 25 percent excise tax (effective February 7, 2005, not 2006) levied on the proceeds of life insurance received by the private investors in transactions ostensibly designed for charitable purposes.

Underwriting and issuing life insurance where the primary recipient of the life insurance proceeds does not suffer an economic loss at the insured's death strikes at the heart of our needs-based selling and our underwriting process. Our reinsurers do not want this business, citing lack of financial need, and concerns over insurable interest and the targeting of older consumers.

Our position is consistent with our commitment to be a leader in the sale of life insurance for business, family, financial planning, and estate planning purposes — where insurance is a key element in the financial solution for your clients. We will continue to support all you do for us and for your customers in this regard, and we recognize that in some cases funding the premium obligation through borrowing is in your client's best interest. This communication is not about these types of sales.

Lincoln Financial Services also echoed Jefferson Pilot's position and added a requirement that, at the time of an application, the agent disclose whether the sales materials or conversations with the proposed insured or advisers (or whether the sales materials and conversations with the proposed insured and advisers) included a description of any aspects of life settlements or a finance-to-life settlement program. The insurer also made it clear that it would not issue any of its products when any parties to the transaction know or understand that the primary intent of the transaction is to transfer the policy to the life settlement market.

ING's statement reads: "There have been instances in which viatical transactions have been employed to defraud investors, insurance companies, and others. The risk of fraud is particularly great when policies are purchased with the intention to viaticate them — or are viaticated shortly after they are initially sold.

In those settings:

- Life insurance is not being purchased for its primary purpose — protecting the insured against the consequences of death.

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- Applicants may have an incentive to conceal illnesses — in order to obtain coverage which may be viaticated on favorable terms.
- Investors who finance viatications are exposed to the risk that policies from which they will be repaid will be voidable, resulting in the loss of their investments.

For these reasons, ING life insurance companies have adopted the following policies, applicable to sales of policies issued by all of its life insurance companies:

Life insurance policies should not be sold to applicants intending to viaticate them. In order to assure that this policy is observed:

a. Agents are expected to determine that the insurance will serve an appropriate purpose other than viatication.

b. The Agent section of the new common application requires the agent to answer the question: "To your knowledge, does the owner intend to change ownership of the policy after its issuance — e.g., to a trust, viatical company, or other person?"

As in situations in which the insured dies during the contestable period, the viatication of a policy during the contestable period will trigger an investigation into the accuracy of medical information provided when the policy was underwritten. If state law permits viatication during this period, only under specified conditions (e.g., a decline in health), the investigation will also address whether those conditions have been satisfied."

The central distinguishing characteristic of SOLI is the absence of a legitimate and significant insurance reason for the transaction — other than the creation of an insurance sale and its commission for the agent, a profitable loan transaction for the lender, and a profitable life settlement for the stranger/investor. Stranger-owned life insurance⁵ is a rapidly spreading virus that is infecting both individuals and charities. The result is likely to be a lose-lose-lose for the public, the insured, their families, and the insurance and estate planning communities. In fact, everyone is likely to lose — except the promoter-marketers-brokers and third-party investors they assemble to finance what is clearly a way around centuries-old insurable interest laws.

A Little History Lesson on Insurable Interest

The legal concept of insurable interest dates back to early 18th-century England. Back then, people did not generally purchase policies on their own lives. The beneficiary usu-

ally owned the contract and often purchased the coverage — often without the knowledge or consent of the insured.

By the mid-18th century, purchasing policies on strangers had become a popular form of gambling. Investors often placed their money into "dead pools" insuring the lives of well-known public figures, particularly those with such problems as gout, alcoholism, or those who were likely to be challenged by political enemies and engaged in duels. Those "investors" would often offer targeted insureds lavish dinners and "a drink or two on me" — or use other means to ensure the certainty and accelerate the realization of gain on their investments.

In 1774 the English Parliament enacted laws to put an end to such gambling on human lives. In the United States, similar laws were adopted.

Although the insurable interest laws vary widely from state to state⁶, in general they deal with three main issues when a policy is purchased on another person's life:

(1) The owner must have an insurable interest in the insured when the policy is purchased (but unlike property and casualty insurance, the interest generally is essential only at the time the policy is issued and need not exist when the death benefit is paid);

(2) The informed written consent of the insured is required in most states before the insurance can be purchased; and

(3) The buyer must have a reasonable expectation of benefit or advantage from the continued life of another person. A child, for example, would have an insurable interest in the life of a parent.

SOLI in a Charitable Context

Here, the promoter's claim is that the arrangement is "a life insurance windfall for charity — without buying a policy or paying anything at all." These are complex and speculative arrangements in which investors "borrow" the insurable interests of charities to purchase insurance coverage on the lives of the organization's older, wealthy, charitable-minded, and generous donors. (In some cases, those who allow the purchase of insurance on their lives are allowed to name personal beneficiaries of a relatively small amount of "free coverage" as an additional incentive).⁷

⁶Leimberg Information Services Inc. (LISI) has insurable interest laws for all states. Log into LISI at <http://www.leimbergservices.com>. There is a free-look button if you are not already a member. Once logged in, click on the State Laws tab at the top on the right. The topic of insurable interest is covered in more detail in Tax Planning With Life Insurance (800-950-1216) and Tools and Techniques of Life Insurance Planning (800-543-0874).

⁷White papers and detailed discussions on this topic can be found at <http://www.leimbergservices.com> in Estate Planning Newsletters # 619, 676, 672, and 671.

⁵The National Conference of Insurance Legislators passed a resolution opposing expansion of state insurable interest laws to permit SOLI.

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Although there are numerous variations on this charitable "win-win" theme, essentially it works like this:

STEP 1: An investment bank issues securities — such as bonds — that investors purchase.

STEP 2: The money from the sale of the securities goes into a trust established by the participating charity.

STEP 3: The trustee uses trust funds to buy single-premium immediate annuities on the lives of wealthy — and typically older (ages 72 to 90) — donors provided by the charity.

STEP 4: The stream of annuity payments is used to buy life insurance on the same donors' lives.

STEP 5: Supposedly the annuities will produce sufficient income to not only pay the life insurance premiums but also provide a sufficient current fixed return to the investors on their investment — at least until the donor dies and the insurance proceeds are paid.

STEP 6: At the death of an annuitant or insured, the "life only" annuity payment ceases.

STEP 7: The insurance proceeds are paid to the trust.

STEP 8: The investors recover their investment from the death proceeds received by the trust.

STEP 9: If there is any death benefit remaining at that point, it is paid to the charity. Promoters estimate that the charity's share will be between 5 and 7 percent of the initial face amount. (Yes, that's not a misprint — the charity — gets between 5 and 7 cents on the dollar, at most!)

[NOTE: Under steps 3 and 4, the investment bank and participating insurance agents receive fees and commissions usually years before the charity can hope to receive any meaningful amounts.]

Why Would a Charity Get Involved?

There are many reasons why charities are at risk of willingly or unknowingly becoming parties to sophisticated life insurance transactions that are not in the best (and long-term) interest of either the charities or their patrons (or the general public, for that matter). Many charities became involved with charitable split dollar and charitable reverse split dollar. There are several reasons why others may be in danger of doing so with these new too-good-to-be-true arrangements.⁸

⁸Testimony of J. J. MacNabb to Senate Finance Committee, June 2004. "Hearings on Charity Oversight and Reform: Keeping Bad Things From Happening to Good Charities," 108th Cong., 2nd Sess. (June 22, 2004) (Committee Print), Doc 2004-12925, 2004 TNT 121-29 (June 22, 2004).

First, we are in an era when donations for many charities have dropped — in some cases precipitously. There are many causes for this phenomenon — undoubtedly, stock market uncertainty and volatility of the past few years have greatly slowed or reduced the rate and size of charitable contributions.

Second, stock market weakness has diminished, and in some instances ravaged, the value of charities' own investment portfolios, particularly those heavy in telecommunication — (read WorldCom) and energy — type (read ENRON) stocks.

Third, competition among charities for donors' dollars has increased significantly. There are more worthy (and some not so worthy) charities and causes than ever before — all aggressively seeking money.

Fourth, reduced staff coupled with shrinking investigative budgets have crippled many federal and state regulatory agencies. Often other governmental problems and priorities have overshadowed the need, or dampened the will, to provide the necessary oversight of charities and policing of charitable abuses. This was highlighted by consumer advocate J.J. MacNabb in June 22, 2004, testimony at Senate Finance Committee hearings. Promoters of edgy schemes know there is statistically minimal risk of serious regulatory audits. (Although that is likely to change soon.) On the state level, not a single state is equipped with sufficient competent staff or legal authority to provide formal or specific regulation of these transactions and therefore there is no oversight agency keeping track of who the investors are, checking to see whether the proposals made to charity can actually work, or following up to make sure the charity receives what has been promised.

Fifth, of all financial tools, the life insurance product is among the most complex and least understood. Almost none but the largest charities have staff with sufficient time, knowledge, and experience to investigate both tax and nontax implications of the many new life-insurance-related plans and arrangements that have been presented to them recently. Few charities have — or can afford — either the highly competent in-house or outside counsel, or other professionals needed to adequately evaluate and judge the efficacy, workability, and risks involved in every scheme that someone wants to sell to them or their supporters. That is particularly true when, in schemes such as charity-based SOLI, it would require high-powered legal, accounting, actuarial, and investment expertise to judge the credibility and potential viability of the proposals.

In difficult economic times, it is easy for a charity to be seduced by possible profits from life-insurance-related schemes and "rent out" its charitable insurable interest and tax-exempt status to unscrupulous marketers and promoters. All too easily, ethical and moral elements of the decisionmaking process may be subverted in favor of what looks like a free and easy ride to boosting a charity's finan-

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cial bottom line. And the charity may easily ignore or never see how, or to what extent, third-party participants (investors) benefit from the "partnership" — and the risk it is taking by allowing its precious tax-exempt status to be used to enable that upfront private enrichment.

Life Insurance as a Charitable Planning Tool

There are dozens of legal, ethical, and creative ways life insurance can be used to benefit charities.⁹ They range from the simple and easy naming of a charity as sole or partial revocable beneficiary to the sophisticated but code-sanctioned use of life insurance inside (or in conjunction with) a charitable remainder unitrust or charitable lead trust. Often individual life insurance owned by a charity on the life of a key supporter will be a wise and prudent investment. But broad-based SOLI goes well beyond the normal — and does *not* vest either ownership or the right to be the policy beneficiary in the charity.

Diving in the Shallow End of the Dead Pool

Although many charitable uses of life insurance may be both legally and ethically proper, some raise concerns. SOLI empowers complete strangers to engage in what amounts to statistical gaming, gambling on the rate of deaths of the insureds, and it would fast-forward us ahead to the past — to a super-size modernized and sanitized version of the long-outlawed dead pool.

By sidestepping or in some cases instigating changes to insurable interest laws (which have, for sound public policy reasons, survived for hundreds of years), big-moneyed, high-powered investor groups hope to make life insurance into a mass commodity investment. The investor groups form vast pools of insured lives (namely, supporters of various charities) to capitalize on the unique benefits of life insurance and profit enormously from it.

In most of these so-called dead pool arrangements, there is a certainty that third-party groups of institutional investors (primarily investment banks, insurance companies, and hedge funds) will receive their share of the "return on investment" sooner — in an obscenely greater amount — than the charity for which the arrangement is ostensibly designed.

Under such an arrangement, the annual guaranteed payments to investors assure them of gain, almost without exception, long before any money is ever paid to the accommodating charity. Yet without participation by the charity (and

the "rented" insurability of its supporters), the net financial gain enjoyed by the private investors, promoters (their upfront fees), and insurance and annuity sellers (in commissions), would be unlawful, socially unpalatable (reprehensible? unconscionable?), and therefore unachievable. (A professional fundraiser for a well-known eastern school has described the arrangement as "smarmy.")

How the Game Works

There are infinite varieties of the ploy. But in every one, after the promoter and the seller of annuities and life insurance policies receive their upfront fees and commissions, the investor pool, the nameless private individuals and companies who finance the initial purchase of annuities (and subsequent life insurance policies), receives a steady stream of fixed income. Eventually, *if* the life insurance policies perform as illustrated, *if* the insureds die as predicted, and only *after* the investors recover their capital investment, the charity *might* receive a (relatively small) percentage of the insurance proceeds.

Some variations give the insured the right to name the beneficiary of a small portion of the death benefit as an inducement to allow the purchase of the policy on his or her life. Promoters claim that "the insureds pay nothing, and it is possible for the charity eventually to receive a large amount of money for what amounts to brokering a 'rent-a-life' arrangement on a mass basis."

Seldom do the promoters fully disclose to the charity or the insureds the names of the initial (or secondary market) investors, what is in it for them, or the full range of risks and potential costs to both the charity and its insured patrons, and the opinion letters rarely if ever offer comment on the probability of the charity's economic success.

Life Insurance/Annuity Combinations

As noted above, one of the variations involves annuities and life insurance on the same individuals. The money raised from the sale of bondlike securities is used to purchase single premium immediate straight-life ("life-only" payout option) annuities on the lives of supporters of the charity. The income from these annuities is then used to buy life insurance on the lives of the same individuals.

The promoters may try to obtain annuities with exceptionally favorable "impaired risk" rates by presenting those individuals as having lower than standard health. Then they approach a different insurer to purchase life insurance on the same individuals from a different company, and by showing them in the most favorable light, try to negotiate the lowest possible life insurance premiums. Part of the financial success of the dead-pool arrangement depends on this actuarial arbitrage. Another part of the financial success of this combination annuity-life insurance arrangement de-

⁹See, e.g., Tools and Techniques of Charitable Planning (800-543-0874) and Leimberg and Gibbons, "Life Insurance as a Charitable Planning Tool: Part I," *Estate Planning*, March 2002, Vol. 29, No. 3, Pg. 132 and "Life Insurance as a Charitable Planning Tool: Part II," *Estate Planning*, April 2002, Vol. 29, No. 4, Pg. 196.

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depends on the favorable tax treatment of the annuity and life insurance as separate.

The charity — if it sets up the insurance trust and is the recipient of the annuity income — benefits by receiving the tax “arbitrage” from the program. That is, the untaxed annuity income received by the tax-exempt trust created by the charity is — at least according to promoters — certain to be greater than the cost of the life insurance premiums paid each year, as well as sufficient to provide an annual payment of fixed income to the institutional investors. So in essence, the charity is sharing its tax-exempt status to ensure a sufficient level of payments to the private lender/partners in the arrangement.

Charity as the Very Limited, Very Junior Partner

It is important to remember that this entire transaction would not be sanctioned by law or the courts or hope to enjoy a favorable public opinion if it took place in another context (such as the corporate or government sector). We learned from cases such as *Wal-Mart*, *Rice*, and *Mayo*¹⁰ — and from scathing and pejorative comments about “dead peasants” and “janitors’ insurance” in *The New York Times* and *The Wall Street Journal*.¹¹ Less publicized, but equally disturbing are reports in the Houston and San Antonio newspapers that Texas proposed to meet the shortfall in the state’s Teachers Retirement System by insuring its retired teachers under a group life insurance contract, a scheme that some newspapers (cited below in footnote 13) called “The Dead Teachers Society” and the “Teacher Pension Plan that Depends on Death.”

None of these third-party institutional investors could engage in this transaction in most states without the protective cloak of the charity. In essence, the promoters act as brokers in “renting” what insurable interest the charity has to the investors in return for a possible eventual payment to the charity of an exceptionally small percentage of the investors’ overall investment return. It’s almost as if the promoter were paying the charity a paltry commission to enable what — without the charity’s being involved — would in most states be illegal and in all states would be considered unsavory or even unconscionable. Stated another way, the arrangements are 95 percent about facilitating investment by private investors in life insurance contracts and 5 percent about furthering a charity’s exempt purposes. (It’s hard to see the difference between SOLI and the now banned charitable split dollar. Each was made to seem as if it were a char-

itable benefit — and neither benefited the charity more than was absolutely necessary.)

(It should be noted that the U.S. District Court for the District of New Hampshire dismissed the case of *Rice, et al. vs. Wal-Mart*. Although a discussion of the case is beyond the scope of this commentary, I do not think that the legal outcome changes the disconcerting notion that a third party (known or unknown) may own significant life insurance coverage on an unrelated insured and benefit from the insured’s death.)

So What Is Wrong With a Charity Leasing Lives of Supporters?

Two central themes of charitable tax law are: *charity is about giving, not taking, and the tax exempt status of a charity is not for sale or private benefit*. To qualify as — or to remain a tax-exempt entity, an organization or entity must operate **exclusively** for **exempt** purposes. A charity’s tax-exempt status is not to be used to enrich or benefit anyone other than those for whom the charitable status was granted and intended. That group does *not* include wealthy private investor groups who have no familial or business loss at the insured’s death and have no interest in the insured’s continuing life. Yet clearly these arrangements provide benefits to private investors that would not otherwise be available without the involvement (complicity) of the charity.

Nonetheless, the argument is that the charity will now receive money that would be otherwise unavailable: “If you don’t go along with this arrangement, you’ll get nothing.”¹² That sounds all too similar to the phrase used by promoters of the now extinct charitable split dollar, specifically banned by code section 170(f)(10).

Don’t Worry About the Law — We’ll Get It Changed!

The amounts of money involved are so large and the players are so powerful that they are willing and able to spend the money and time to convince lawmakers to change state insurable interest laws that are not flexible enough to accommodate their dead-pool schemes.¹³

¹⁰These cases are reported on in detail in *Tax Planning With Life Insurance*: (800-950-1216) and in Leimberg Information Services (<http://www.leimbergservices.com>) Click on the Free Look button if you are not a member.

¹¹See also *Tamez v. Certain U/W*, 999 S.W.2d 12 (Tex. App.- Houston 1999).

¹²Baskies & Samuels in “Aggressive Viatical Settlement Transactions: Gambling on Human Lives,” 28 *Est. Plan.* 76 (Feb. 2001). Mayer, Brown & Platt, *The Financial Services Regulatory Report*, Vol. 8, No. 2 (March/April 2001). J. Blattmacher, “Assigning Insurance Policies to Charities,” *CPA Journal* (New York Society of Certified Public Accountants), 1997.

¹³“Disbelief greets state plan to profit from Dead Teachers Society,” *San Antonio Express News* 12/13/2003; “Betting on the Lives of Teachers,” *Houston Chronicle* 12/11/2003; “Texas Could Turn a Profit by Insuring Dead Teachers Society,” *San Antonio Express News* 12/10/2003; “Former Senator Proposes Teacher-Pension Venture,” *Knight Ridder* 12/05/2003; “Texas Considers Teacher Pension Plan That Depends on Death,” *Houston Chronicle* 12/05/2003.

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Promoters of the plans have been lobbying at the state level to have officials loosen insurable interest laws to allow the programs. We are talking about a huge investment in which a group of third-party investors stands to financially gain on policies on a large number of unknown, unrelated individuals' lives — and not a single one of those insureds has ever met the investors — or even knows who he or she (or they) is or are! And, of course, even if the investor pool is ethical, honest, and well-meaning, there is no guarantee that — failing a reasonable profit (perhaps because deaths are not occurring in the real world at the same pace they were assumed to statistically happen) — their interest may be sold to others who are even more estranged (and perhaps less ethical and well-meaning) strangers. There is not a single state with a law to prevent such a sale or to provide specific oversight to protect charities' interest (not to mention the privacy and security of the persons being insured). And even if there were, few states have sufficient personnel with the actuarial and legal competence to adequately police these transactions.

If state governments manipulate the laws to circumvent the consumer protection purpose behind the rules, it is a game we all lose.

Potential Adverse Financial Statement Effect on the Charity

Ohio State University decided not to go forward with a SOLI program when their auditors told them that the debt in the SOLI trust would have to be consolidated with the university's own financial statements. Combining that debt would have lowered and potentially damaged the university's bond rating.

For example, Enron, days before its demise, was the world's wealthiest corporation. It failed not because of a flawed business strategy, poor investment decisions, or competition from creditors, but because of the calamitous, almost overnight forfeiture of investor trust. That loss was precipitated by disclosures that Enron had hidden its losses and liabilities in a series of so-called "special-purpose entities [(SPEs)]."

SPEs are entities formed to conduct a specified business activity used to raise financing for large projects, often — as in SOLI — used to make loans and pay returns to investors and then repay their capital. SPEs are also a complicated web of structured finance arrangements with a lack of transparency that enabled Enron's massive balance sheet and income manipulation. Enron was using SPEs to hide several billion dollars of off-balance-sheet debt. SOLI is just that — a form of off-balance-sheet financing. The whole thing is financed with massive loans.

From the beginning of their use, off-balance-sheet SPE's have led to controversy in the accounting world — and about whether the entity was truly independent from its sponsor.

So to prevent manipulation — so-called financial engineering — and to address lack of disclosure transparency and to help monitor the financial impact of off-balance-sheet debt (and the potential for misuse), GAAP requires a consolidation of the SPE's finances with those of its "sponsor."

With SOLI, in some variations, the charity puts up a modest amount to fund the trust (for example \$100) so it's "the charity's trust." Everything else — millions of dollars loaned to pay premiums — is borrowed! That trust (and its huge debt to third-party investors) must be combined with the charity's books for financial statement purposes. The charity therefore must show a whole lot of debt on almost no equity. In the case of Ohio State, its auditors told them that would have ruined the university's bond rating."

ACLI, AALU, NAIFA, and Insurers All Speak Out — Loudly

In an unprecedented move, three of the largest U.S. organizations dedicated to advancement and support of life insurance sales people, spoke out strongly — against an arrangement that would sell life insurance and annuities.¹⁴

They did so with good reason! All three organizations have roundly criticized moves made by state legislators to loosen insurable interest laws. The American Council of Life Insurers, joined by the Association of Advanced Life Underwriters and the National Association of Insurance and Financial Advisors, has made it clear they oppose state law changes that would allow third-party institutions with no familial or other relationship to the insured to use charities to enable the purchase of life insurance on individuals in mass numbers.

Those three organizations have stated, in no uncertain terms, that life insurance contracts should be issued only to persons or parties with a familial or recognized economic relationship with the insured, and that the issuance of life insurance should not be perverted and allowed to become a mere commoditized investment process.

The proposed state legislation would weaken modern-day insurable interest laws to the point that they could no longer serve any meaningful, practicable purpose. The proposed state legislation would facilitate transactions that purport to benefit participating charities when in fact they provide large, upfront fees to the promoters and annual guaranteed payments to investors, long before any money is sure to be paid to the charity.

Ironically, the promoters of the schemes claim that insurers who have refused to sell SOLI and who have fought a weakening of insurable interest rules are being anticompetitive — a strange and baseless claim, considering there is nothing spe-

¹⁴http://www.naifa.org/frontline/20040615_nfi_1.html

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cial about the policies themselves any insurance company could not duplicate — if they chose to do so.

Risking the Tax-Exempt Status of the Charity

Promoters of the arrangements have no stake in the long-term success of the charities other than as facilitators of their sales efforts. So the loss of a charity's tax-exempt status is of no personal and immediate concern, once the sale is made.

Charities may believe there are no adverse income tax consequences as a result of their participation. However, the charities, as tax-exempt entities, may unwittingly be imperiling their tax-exempt status or incurring unrelated business income tax (UBIT) unexpectedly. At a minimum, questions have arisen as to whether the charities are compromising their ability to attract major supporters who can make significant donations to the organizations with which they have relationships.

Does (or Can) This Arrangement Really Work? And at What Cost?

No one has yet proved that this ploy will really benefit a charity — or to what extent.¹⁵ Some have serious doubts.¹⁶ They question if the policies are, in fact, "priced right,"¹⁷ to ensure that the investor receives a return *and* provide a significant payoff to charity. In other words, for money to be left over for charity, it would take (at least on a present-value basis) a death benefit that is higher than the premiums paid.

Yet for the insurer to survive and pay its shareholders a profit and its agents a commission, it would have to charge sufficient premiums to account for expenses and leave a profit margin. Stated differently, the insurer would have to take in at least as much in premium dollars — and preferably more — than it pays out.

Here are some threshold questions:

- Where does the money to service the investor's debt come from? How about the promoter's fee? How can everyone win?

¹⁵For an extensive guideline in the banking field that provides many of the same questions that should be asked in the charitable area, see OCC Bulletin 2000-23, "Bank Purchases of Life Insurance: Guidelines for National Banks," dated July 20, 2000, OCC 2002-19 Unsafe and Unsound Investment Portfolio Practices.

¹⁶Debra Blum, "For Charities, a New Twist in Raising Money: Corporate Investors in Life-Insurance Policies," *Chronicle of Philanthropy*, August 12, 1999. Theo Francis and Ellen Schulz, "Dying to Donate: Charities Invest in Death Benefits," *The Wall Street Journal*, February 6, 2003; Tom Gascoyne, "Death Dividends or Creative Financing?" *Chico News and Reviews*, February 20, 2003; Stephanie Strom, "Charities Look to Benefit From a New Twist on Life Insurance," *The New York Times*, June 6, 2004.

¹⁷Some of the life insurers participating in SOLI have lapse support assumptions. Those policies are unlikely to lapse and may as a result be underpriced.

- Can this work *only* if the policy is mispriced (or underpriced)? That is, would it work only if deaths were to occur much earlier than would be expected under reasonable actuarially assumptions? (But in this respect, it would work only for the investors and the charity and not the insurer.)
- Are there impartial tax and legal opinions provided to the charity concerning the proposed arrangement? Do they cover all the tax and nontax issues — such as whether the charity's tax-exempt status will be at risk? Do they address the overall financial feasibility of the arrangement? Are the illustrations both accurate and unambiguous? If the policies are aggregated, are there individual product illustrations to support and substantiate the numbers? Are the names and financial status of the insurers disclosed? Are carriers reputable?
- What happens if the investors do not get their investments back quickly enough?
- If the charity is the owner of the insurance, is the maintenance of the policies both reasonable and prudent? (It must be to meet Prudent Investor rules).
- Does the charity have to put up any collateral? If so, how much?
- What are the upfront fees? What are the annual administration costs? Is the charity aware of and willing to shoulder these costs?
- What does the charity's independent counsel or actuarial study show? (A charity that is not willing to spend the money to have the proposed arrangement independently checked and verified is foolish!)
- Did the promoter mention that the charity will likely have sizable annual legal and accounting costs associated with the program?
- Who is the initial third-party investor? Who will that investor sell the interest to if another more profitable use of the investment comes along, or if that investor believes the investment is no longer profitable? Could that new investment group be T.S.I? (Tony Soprano Inc.)

Think it can't happen? Think again. *The Washington Post* reported that a federal grand jury in Baltimore alleged a sophisticated and unusual operation in which illegal drug trafficking profits were laundered when life insurance policies were purchased on the lives of drug users and others, without their knowledge. At least 17 life insurance policies were acquired over almost a decade and, according to the *Post* article, a law enforcement official familiar with the case said, "Some of those individuals did die sudden and violent deaths. The investigation into the circumstances surrounding those deaths continues. Payments from the policies taken out for those who have since died generated hundreds of thousands of dollars."

The Big Risk to the Life Insurance and Estate Planning Community

The individual and charity-based SOLI arrangements described above transform life insurance into a third-party investment vehicle, a commodity. Once that happens, there is little reason or justification for Congress and the states to continue the multiplicity of unique tax treatment accorded life insurance (for example, income-tax-free buildup of cash value and the generally unlimited income-tax-free nature of death proceeds).

Absent the tax-free nature of life insurance proceeds, many businesses will be unable to afford adequate key employee coverage, sufficient cash to fund a nonqualified deferred compensation agreement or a death-benefit-only plan, or provide a sufficient level of post-retirement health coverage for employees. Likewise, on the personal level, it will become more difficult or impossible (and certainly more expensive) to obtain adequate life insurance for our clients to pay off debts, ensure a standard of living and college education to survivors, or pay state and federal death taxes. Higher insurance costs translate into doing with less or doing without — and would divert funds from investment and retirement savings. Everyone loses if either the death proceeds or the internal buildup in a life insurance policy become taxable.

A more subtle but equally damaging aspect of the development of life insurance as a marketable third-party investment commodity is the havoc it would play on the pricing of life insurance. As the final quote in this commentary notes, "sound underwriting presumes that the owner of the policy and the insurer both are better off if the insured continues to live — a presumption essential to the creation and maintenance of life insurance premium structuring as we know it."

But Don't Take My Word for It

Following are notable quotes from some of the most recognized authorities and commentators in the fields of estate and charitable planning.

In her article, "Dead Pool Donations," *Trusts and Estates*' Senior Editor, Wendy Davis says, "For Donors, the value of their lives is put, literally, in someone else's hands — and it's hard to say whose."¹⁸

Jerry J. McCoy, co-author of the *Family Foundation Handbook* and former chair of the American College of Trust and Estate Counsel's planned giving committee:

¹⁸Wendy Davis, "Death-Pool Donations," *Trusts and Estates*, May 2004.

Charities are placed in a position of hoping people die.

It's probably going to be illegal by the end of the year."

Craig Wruck, chair of the National Committee on Planned Giving's government relations committee:

Charities are being told they can create money out of nothing and you know intuitively that that's impossible.

Vaughn Henry, nationally known charitable consultant:

It's because life insurance protects widows, widowers, and children from becoming paupers when the breadwinner dies that it isn't taxable.

But that may change if Congress or the Treasury Department thinks life insurance has become nothing more than a wager.

Dean E.G. Miller, senior associate dean of the Virginia Commonwealth University School of Business, said, "Congress will take a hard look when life insurance is used to accomplish objectives other than income replacement or business and estate planning. Turning life insurance into a third-party investment vehicle — a commodity — will bring additional scrutiny."

Laura Kalick, chair of the American Bar Association's subcommittee on unrelated business income tax:

If the charity borrows money to buy the life insurance policies, the charity will likely have to pay the IRS tax on unrelated business income — because charities have to pay tax on debt-financed income.

Carolyn M. Osteen, partner in Ropes & Gray, Boston, in "A Review of the Hottest Charitable Gift Issues," *ALI-ABA Estate Planning Course Materials Journal*, Feb. 2005, pg. 37, says:

Non-Charitable businesses are generating income with what's being called a charitable planning tool. From my perspective, it looks like: (1) The charity is selling its exclusive insurable interest to generate profit for commercial lenders in a transaction that has little economic benefit other than to churn money around and generate large premium payments, so raising suspicions of private inurement or personal benefit; (2) If the charity is receiving income from borrowed money, that looks like debt-financed income/UBIT; (3) Life insurance has, as a risk-management tool, its special tax treatment because it serves the public good, but this program amounts to wagering since the lender benefits from selling a larger than average policy that has no relationship to economic risk, and the charity is left with little, or nothing, after all expenses are paid.

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Viewpoints

Mike Nelson of Iowa Savings Bank, author of the special white paper, "Insurable Interest Under Siege,"¹⁹ said:

The objection is not that wholesale murder will ensue. Such an assertion only trivializes the debate. The objection is that the third party owner of the policy benefits only from the death of the insured. The essence of sound underwriting is that the owner of the policy and the insurer both are better off if the insured continues to live.

Yet the proposed insurable interest changes and attempts to turn life insurance into a third party investment vehicle shatter this harmony and sound philosophy.

In the 2005 Blue Book for fiscal year 2006,²⁰ the Treasury proposes an excise tax on these transactions, stating:

The Treasury Department is concerned that, in many cases, such arrangements do more to facilitate investment by private investors in life insurance contracts than to further a charity's exempt purposes. Moreover,

these arrangements may inappropriately afford benefits to private investors that would not otherwise be available without the charity's involvement.

The Bottom Line

What's really happening is this: Charities are being solicited to become very junior members in a business enterprise. That enterprise is the acquisition of life insurance on a person's life — even though the business has no proven interest in the continued life of that person except to profit by his death!

It's almost as if the promoter is paying the charity a commission ("We'll pay you a 5 percent accommodation fee if you let us attach your charity's name to our program"). Why would the promoter want to pay that amount to charity? The answer is, it doesn't want to — it *needs* to, to enable what without the charity's involvement would in most states be an illegal wager, and would in all states be considered unseemly, unsavory, and perhaps even unconscionable!

Stranger-owned life insurance whether or not it is connected to a charity is a dangerous and disturbing trend. Left unchecked, this short-sighted, too-good-to-be-true, something-for-nothing ploy could hurt the charities it is promoted to benefit, trigger a sea change in the way all life insurance is taxed and priced, and in extreme cases encourage criminal activity of the worst kind.

¹⁹Leimberg Information Services Inc. Charitable Planning Newsletter # 50, at <http://www.leimbergservices.com>

²⁰<http://www.treas.gov/offices/tax-policy/library/bluebk05.pdf>.

EXCERPTS FROM NORTH DAKOTA'S INSURABLE INTEREST LAW

Section 26.1-29-09.1 Insurable interest in personal insurance

"No person may procure or cause to be procured an insurance contract upon the life or body of another person unless the benefits under the contract are payable to the individual insured or that individual insured's personal representative, or to a person having, at the time the contract was made, an insurable interest in the individual insured."

"Insurable interest" includes ...

- a. In the case of individuals related closely by blood or by law, a substantial interest engendered by love and affection,
- b. In the case of persons other than those described in subdivision a, a lawful and substantial economic interest in having the life, health or bodily safety of the individual insured continue, as distinguished from an interest that would arise only by, or would be enhanced in value by, the death, dismemberment or injury of the individual insured.

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EXCERPTS FROM A RECENT ADVERTISEMENT PROMOTING STOLI

(The Desert Sun, Sunday February 5, 2006 p. A16)

Dear Friend:

How much life insurance would you have ... if ... you didn't have to pay anything to get it ... and ... you could make a substantial profit from it while you are still alive?

* * *

You don't have to spend a dime of your own money to purchase a life insurance policy on your life because lenders are NOW eager to make safe, secure, non-recourse loans to you, so you can purchase a life insurance policy on your life, using the lenders money, and not yours, that you can eventually sell to the secondary market for a substantial profit.

The secondary market is spending more than 2 billion dollars to buy life insurance policies from people who already have them.

There are ten plans that let you cash in big. I can't describe them all here, but let me give you just one example. You are a 75 year-old male and you decide to purchase a \$10,000,000 policy. A private lending institution pays all premiums and interest on your policy ... you have no out of pocket cost ... and ... after a few years you sell the policy to one of the investment firms in the secondary market that pays off the lender ... and ... gives you maybe \$500,000 or \$600,000 of profit for the privilege of purchasing your policy.

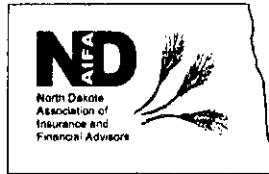
Why is all this true? Well you are at the right place and at the right time to take advantage of a great opportunity. However, it won't be true for very much longer.

You see, life insurance companies didn't sell many life insurance policies to people over age 70 because people didn't want to pay those high premiums for the rest of their life. So life insurance companies weren't much concerned with accurate pricing on those policies since they weren't selling many of them. As a result, the policies they do sell are under priced. Very sharp people in the secondary market for life insurance have discovered this and are paying serious cash for policies owned by senior citizens.

This is all true, 100% legal and completely above board. But, it won't last forever. You see, the insurance companies have discovered their "mistake" and are working hard and fast to correct it.

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TESTIMONY SUPPORTING SB 2268

BY

TERRY WEIS, RHU. LUTCF

January 30, 2007

10:30 a.m.

SENATE INDUSTRY BUSINESS & LABOR COMMITTEE

SENATOR JERRY KLEIN Chairman

Same to House

Good morning Mr. Chairman and members of the Senate Industry Business & Labor Committee.

For the record my name is Terry Weis, I am a volunteer lobbyist for the North Dakota Association of Insurance and Financial Advisors. Our association has nearly 500 member insurance agents from all parts of North Dakota, who sell Life, Health, Property insurance as well as other financial products.

I have been in this business for over 34 years and I can tell you that there is almost nothing the same today as when I started. The insurance products have evolved over the years and the regulations on those products have also changed.

We have all seen our day to day lives change with the times that we live in and that is what SB 2268 is all about. This bill does not preclude someone from selling an unwanted or unaffordable life insurance policy.

Life Insurance currently requires an insurable interest to purchase a policy on someone's life. Because of this fact the beneficiary receives the death benefit tax free. Life insurance is not an investment and if we do not keep up with the changing times by adopting SB 2268 this could change the future for families that depend on the life insurance proceeds to pay for college tuitions and farm mortgages.

This is not a complicated issue. The regulation may have a 5 year waiting period and put restrictions on Stranger Owned Life Insurance, but this is a simple concept that we can all understand is in the best interest of the insured.

I URGE A DO PASS ON SB 2268

I would be happy to answer any questions.

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NATIONAL CONFERENCE OF INSURANCE LEGISLATORS (NCOIL)

**Proposed Resolution Regarding the Enforcement of Existing State Insurable Interest Laws,
Stranger-Originated Life Insurance (STOLI), and Related NAIC Action**

To be considered by the NCOIL Executive Committee on March 3, 2007.

Adopted by the NCOIL Life Insurance & Financial Planning Committee on March 2, 2007.

IT IS HEREBY RESOLVED that the National Conference of Insurance Legislators (NCOIL) believes the first step in combating STOLI schemes lies with the enforcement of existing state insurable interest, life settlement, and/or other consumer protection laws and that state Departments of Insurance should, in a timely fashion, take such appropriate action;

BE IT FURTHER RESOLVED that NCOIL requests that the National Association of Insurance Commissioners (NAIC) delay final action on its model act addressing the assignment of life insurance policies and life settlements until its December 2007 meeting, while NCOIL completes its review and revision of a NCOIL *Life Settlements Model Act*.

Chairman Klein, and members of the Senate Industry Business and Labor Committee, my name is Tom D. Kelsch, with the Kelsch Law Firm. I am presenting your committee with this printout on behalf of Peachtree Settlement Funding. Peachtree Settlement Funding was founded in 1996 and is a leader in the secondary market for life insurance.

Peachtree is opposed to SB 2268 and requests a "Do Not Pass" recommendation from this committee for the following reasons:

1. **SB 2268 violates long standing property rights of North Dakota consumers.** In 1926, the Supreme Court of North Dakota held that, "a life insurance policy, under which the insured has the right to change the beneficiary, is regarded as a chose in action, and may be assigned or transferred by will in this state." Talcott v. Bailey, 208 N.W. 549, 553 (N.D. 1926). Furthermore, the insurance code explicitly allows the transfer of a life insurance policy: "A life insurance policy may pass by transfer, will, or succession to any person, whether that person has an insurable interest or not . . ." NDCC 26.1-33-33.

An individual has an unlimited interest to procure coverage on his own life and do with it what he pleases. "An individual of competent legal capacity may procure or effect an insurance contract upon that individual's own life or body for the benefit of any person." NDCC 26.1-29-09.1(1). Insurable interest is only required at the time of purchase. "No person may procure or cause to be procured an insurance contract upon the life or body of another person unless the benefits under the contract are payable to the individual insured or that individual's personal representatives, or to a person having, *at the time the contract was made*, an insurable interest in the individual insured." NDCC 26.1-29-09.1(1) (emphasis added). SB 2268 would reverse or infringe upon all these established North Dakota laws and the property rights that they afford consumers.

2. **SB 2268 is based on unapproved amendments to the NAIC Model Act that were passed by the NAIC Life Insurance Committee.** These amendments are subject to review and action by the NAIC Executive Committee and the full membership of the NAIC. The language in SB 2268 cannot be called an NAIC Model any more than the language in a legislative bill can be called law after it has passed a committee in one chamber. It is highly unusual for interest groups or anyone else to bring a not-enacted NAIC proposal to legislatures and claim any sort of blessing of the NAIC.

3. **The NCOIL Life Settlements Subcommittee unanimously rejected the NAIC Life Committee's amendments** because these amendments, which are contained in SB 2268, impaired and interfered with life settlements and, as stated by a subcommittee member, "imposes numerous new strictures on life settlements that have nothing to do with investor-initiated life insurance."

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4. **SB 2268 unjustifiably imposes a broad five-year ban on life settlements.** This is a major change in the well-reasoned NAIC Model and the established laws of all 34 states with a settlement law. The 5 year ban includes if a consumer has ever been evaluated for settlement, on any policy, at any time prior to the first two years of the policy in question. The 5 year ban does not respond concerns about investor-initiated life insurance; expands the settled two-year period by 250% and sweeps in many traditional life settlements – since 40% of policies lapse in the first five years – depriving a substantial number of policyowners of the established benefits of settlements. In fact, the primary supporter of the five year ban, the ACLI, less than a year ago categorically stated that a five year ban was bad for consumers and should be rejected. “The legislation pursued by ACLI will not affect life settlements entered into more than two years after policy issuance.” (ACLI fact sheet, “Key Points on Stranger-Owned Life Insurance.”)

5. **SB 2268 outlaws legitimate lending transactions and, in doing so, violates several provisions of the Gramm-Leach-Bliley Act and/or the National Bank Act,** all of which are in place to ensure that consumers can access capital from lenders to fund needed death benefit coverage. SB 2268 would outlaw legal and appropriate lending transactions where premium finance loans are made supported by the policy as collateral for the loan. This is not only bad public policy, it is illegal under federal law. The Gramm-Leach-Bliley Act prohibits states from significantly interfering with banks’ ability to participate in any way with, directly or indirectly, with cross marketing which allows insurance sales. GLBA also preempts state laws which prevent bank activities while allowing competing insurer activities. The NBA prevents states from passing laws which infringe on banks’ ability to assess good risks for loans or to determine a property’s adequacy to serve as collateral. SB 2268 would outlaw. SB 2268 violates not only the letter but the spirit of GLBA and the NBA – enabling the free flow of capital between financial services sectors so that consumers can access needed financial services products.

6. **It is premature to act on SB2268.** During the December NAIC Life Committee debate, concerns about federal preemption were raised by The American Bankers Association’s insurance affiliate, the American Bankers Insurance Association (ABIA), and representatives from the financial services, premium financing and life settlement markets. The ABIA declared the debated proposal ill-considered and illegal. A representative from the Office of the Controller of the Currency testified that the OCC had concerns about federal preemption and requested additional time to review and comment. No review of this issue by the NAIC has ever been offered. Nor have state banking regulators been consulted, even though SB 2268 would not assert insurance code jurisdiction over its proper subject matter (insurance policies and insurance companies and agents), but rather asserts insurance code and insurance commissioner jurisdiction over lending transactions, banks, other lenders, and borrowers, as well as potential securities transactions. This is an overreach and should not be the subject of rushed legislation.

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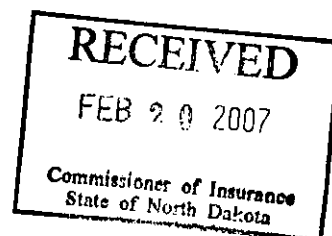
CHUCK JAFFE

Selling yourself short

Life settlements satisfy need for cash, but few really benefit

By Chuck Jaffe, MarketWatch

Last Update: 7:24 PM ET Feb 14, 2007



BOSTON (MarketWatch) -- Everyone could use a little more money, but needing that cash desperately and in a hurry leads consumers to make a lot of mistakes. While the typical mistakes involve payday-advance loans or tax-refund anticipation loans, one big concern for senior citizens in need of cash is the "life settlement."

Life settlements aren't a particularly well-known part of the financial landscape, but they are becoming increasingly popular -- and increasingly dangerous. To that end, NASD last week issued an "investor alert" to warn seniors about the potential dangers involved in selling an existing life insurance policy for cash.



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It's a warning that consumers should heed, particularly if they know seniors who have cash-flow worries.

Life settlements -- sometimes called "senior settlements" -- are a logical extension of a product that became popular in the 1990s, the "viatical settlement."

In a viatical deal, people giving up insurance policies typically are ill and have a short life expectancy; they're taking a lump sum now and giving up their insurance coverage because their life is likely to end within two years and they need the cash to ease the time they've got.

Life settlements are similar in how they operate, but they are targeted at folks who are not terminally ill, just old enough so that their life expectancy generally would fall in the two- to 10-year range.

The life-settlement provider may hold the policy it buys until maturity (the death of the seller of the policy) or it may sell part or all of the policy to other investors, as varied as hedge funds and other insurance companies. The consumer's lump-sum payment depends on a number of factors, including age, health and the terms of the insurance policy being sold. And premiums needed to keep the policy

in effect are paid by the purchaser, who gets the death benefit in the end.

"For some seniors, there are not a lot of places to turn if they need cash," says Ed Long, executive director of Healthcare and Elder Law Programs Corp., which runs the help4srs.org Web site. "But this is an idea that is sold to somebody, not something they tend to come up with on their own, and the real juice here is for the people buying the policy, not the person selling it."

Getting the cash now, instead of leaving it to your estate, is not always a bad idea, particularly if you have a strong need for the money. But NASD officials point out that, even for people who perceive a need, the life settlement works for just a small percentage of the population.

"It might work if you have an immediate need for cash, if you are getting more from the settlement than you'd get in the policy's surrender value, if you can't borrow against the policy you are selling, you haven't got other sources of cash, and you've got a hard-core need for the money right now," says Elissa Walter, senior executive vice president for NASD. "It's being sold to a lot of people who don't really fit that kind of description."

Huge market potential

Most industry data estimates the market for life settlements in the \$5 billion to \$6 billion range, but some studies -- and a number of firms that have gotten into the business -- suggest that the potential market could be 20 times larger.

NASD, which normally regulates securities brokers and dealers, seldom gives insurance advice, since most forms of insurance technically don't qualify as "investments." Life settlements can be made on virtually every form of insurance, although only variable insurance products fall into the realm of securities. The agency steps across the securities boundary and into areas like insurance only when it sees a problem brewing.

Says Walter: "The thorniest issues in the financial world today are the ones on the cusp, the edge between securities products and other products, in part because people aren't sure of where to turn for help."

The issues that the NASD wanted to provide help with are at the core of the life-settlement decision. They include:

- **Costs.** There's nothing wrong with a life-settlement broker making a buck, but commissions on these deals can run as high as 30%. That makes them much less attractive; if the ultimate payoff is less than the surrender value of the policy, the consumer should forget about the deal, avoid the commissions and just give up the policy to the insurer for the surrender money.
- **Figuring out a fair value for the policy.** There is no open market here, so the only way to be sure that an offer is good is to shop around for several deals. A licensed life-settlement broker can present multiple offers, but experts suggest that most consumers take the first deal they are offered rather than looking for another proposal.
- **Tax implications.** For some people, the lump-sum payment is taxable. In addition, that big chunk of change can cut into some people's ability to participate in certain state or federal public assistance programs, most notably Medicaid.
- **Continued insurance needs.** Sometimes the consumer is selling one policy, but using the proceeds to buy another, effectively taking some cash out of the insurance but leaving some protection in place. Because the first policy remains in force, it could affect the consumer's ability to get new coverage. And given that the person trying to buy the policy has a relatively short life expectancy, any coverage is likely to be pricey.

Says Walter: "The biggest problem for most people is that they don't have enough information to know if they are making the best decision. They need to look at their options, both in the form of getting several offers for their policy, and in thinking about everything they might do besides selling the policy. ... They may have a current need for money, but they shouldn't be rushing into this, because it will affect them for the rest of their life."



Chuck Jaffe is a senior MarketWatch columnist. His work appears in dozens of U.S. newspapers.



**TESTIMONY SUPPORTING SB 2268
BY**

NORBERT MAYER, FIC. LUTCF

March 6, 2007

**HOUSE INDUSTRY BUSINESS & LABOR COMMITTEE
REPRESENTATIVE GEORGE KAISER Chairman**

Mr. Chairman and members of the House Industry Business & Labor Committee:

I am Norbert Mayer and I am here to represent the nearly 500 members of the North Dakota Association of Insurance and Financial Advisors.

Our association supports this bill because it protects the integrity of life insurance and preserves the purposes for which it was created. Unlike other financial tools, life insurance creates an immediate estate, when it is needed the most, at the untimely death of the insured. It permits a family to continue living at the same life style they were accustomed to even after the death of the family bread winner. For others it assures that there will be adequate funds to provide a proper and dignified funeral. It also protects businesses from financial ruin at the untimely death of the sole proprietor, a business partner or a key person. In North Dakota it is a valuable tool to help assure that a family farm or family business can be passed on to heirs by providing funds to pay taxes and pay off debts.

Insurance is designed to protect us from the potential losses incurred from pure risks. A pure risk is one in which only losses are incurred, and there is no opportunity for gain. Insurance is carefully regulated by provisions for the coordination of benefits payable by more than one insurance policy and limiting the amount of insurance issued to the actual values of the risk being insured. Life insurance transfers the risk of an untimely death, from the family or business, to the insurance company based upon a realistic value of the life insured. It was never intended to provide coverage for speculative risks and offer an opportunity for strangers to profit by speculating on the time of death of another individual. For these reasons the ND Association of Insurance and Financial Advisors urges you to support this important piece of legislation.

Thank you and I will be happy to answer any questions you may have.

STOLI ALERT

March 2007

Volume 1 Issue 1

Welcome to the first edition of *STOLI Alert*, a newsletter for state regulators and lawmakers, newsmakers and others who are concerned about the practice called stranger-originated life insurance (STOLI). Also known as speculator-initiated life insurance (SPIN-LIFE), these arrangements attempt to circumvent state insurable interest statutes—laws that are intended to assure that people who buy life insurance have a true and meaningful interest in the life of the insured.

State insurance regulators and lawmakers are looking closely at STOLI. The National Association of Insurance Commissioners Life Insurance and Annuities (A) Committee voted in December 2006 to restrict these arrangements by amending its Viatical Settlement Model Act (see page 3). The National Conference of Insurance Legislators is also considering a proposal. The life insurance community endorses efforts to regulate these contrived transactions.

STOLI involves investment firms inducing certain wealthy seniors to obtain life insurance. These come-ons often include promises of “free life insurance” and other incentives—sometimes including payments in the six figures. The investment firms fully finance the transaction and continue paying premiums throughout the life of the contract. Two years into the contract, the investment firms—speculators—purchase the policy and stand to profit from the death benefits from policies on lives of strangers.

Why two years? Because these arrangements are structured to avoid state “wet ink” laws, which bar life insurance policy settlements for two years after a policy takes effect unless certain conditions are met. In addition, under most life insurance policies, the validity of the contract can no longer be contested by the life insurance company two years after the policy takes effect.

STOLI arrangements turn the purpose of life insurance on its head. Instead of taking out policies to protect and benefit those with an insurable interest, it is initiated by strangers who attempt to circumvent the purpose of state insurable interest laws for their own investment purposes.

STOLI is bad for life insurance, and also represents a threat to consumers.

As life expectancies have increased, the life insurance community has taken major strides in making life insurance available to older people who, in years past, would have been

WHERE WE STAND

Life insurance serves many critical social functions. Most importantly, it protects and provides tremendous benefits to individuals, families, businesses and employees. The increasing use of life insurance by speculators—who attempt to circumvent insurable interest laws and profit from the death benefits from policies on lives of strangers—is a clear abuse of life insurance’s social purpose.

Insurable interest is a fundamental concept in a well-functioning life insurance marketplace. The concept preserves the social purpose of life insurance and helps to assure that the product will not be abused. Insurable interest statutes demonstrate the widespread belief among the nation’s lawmakers that society is diminished when life insurance is used as a vehicle for gambling on human life. Stranger-originated life insurance violates the concept of insurable interest. Changes to state viatical settlement laws, laws which deal with settlement issues, are necessary to prevent STOLI promoters from evading state insurable interest laws and violating the social purpose of life insurance.

The life insurance community recognizes that many circumstances may lead the owner of a life insurance policy to explore a life insurance settlement. We have always supported—and will continue to support—legitimate life settlements. The life insurance community also supports the NAIC Life Insurance and Annuities (A) Committee proposal that contains numerous exceptions to a five-year moratorium on policy settlements (see “*Moratorium Exceptions*” on page 3). However, we oppose transactions initiated and solely designed to enable speculators to initiate life insurance, circumvent the intent of insurable interest laws and profit from death benefits from policies on lives of strangers.

considered uninsurable. STOLI threatens to undermine this market, making life insurance more expensive for millions of people who need and want it.

The life insurance community is united in working for changes to state viatical settlement laws to address this abuse of life insurance and to protect legitimate uses of life insurance.

The American Council of Life Insurers (ACLI), the Association for Advanced Life Underwriting (AALU) and the National Association of Insurance and Financial Advisors (NAIFA) are pleased to present this newsletter as a resource on this critical issue. *STOLI Alert* will provide news on STOLI and insights about developments on issues relating to these transactions.



HOW STOLI WORKS

Stranger-originated life insurance—sometimes called speculator-initiated life insurance (SPINLIFE)—has many variations but a common purpose: to allow outside investors to initiate life insurance coverage on strangers and circumvent state insurable interest laws.

Investors will identify older, high-net-worth individuals, generally people 70 or older with a net worth of more than \$1 million. These individuals are targeted because of their relatively short life expectancy and their wealth qualifies them for substantial amounts of life insurance.

The investors offer these individuals the chance to obtain large amounts of life insurance for “free,” or in exchange for some cash compensation. Generally, the investors loan money to their targets to pay the premiums for a defined period, usually two years. This initial period is based on the life insurance policy’s contestability period and state “wet ink” laws. A common feature of the arrangement is that the insured is told that he or she can walk away from the debt without any cost or other liability.

STOLI is structured to allow an investor without an insurable interest to initiate and profit from a life insurance policy on a stranger.

If the insured survives the contestability period, he or she typically is given the option of repaying the loan or transferring ownership of the policy to the investors in complete satisfaction of the debt. As a practical matter, the STOLI arrangement often is designed so that the insured will transfer the policy to satisfy the debt because the cost to repay the loan plus other fees and charges is so high that repayment is economically unfeasible.

If the insured dies during the two-year period, the net death benefit will be paid to the insured’s beneficiaries. However, the beneficiaries will be obliged to repay the premium loan to the investor.

The essence of the arrangement is that the investor is betting that the insured will live longer than the two-year period and transfer ownership to the investor, which then results in nearly all death benefits being paid to the investor.

STOLI DEVELOPMENTS

National Association of Insurance Commissioners

The NAIC’s Life Insurance and Annuities (A) Committee on Dec. 11, 2006, unanimously approved amendments to the NAIC Viatical Settlements Model Act to place restrictions on stranger-originated life insurance arrangements. The entire life insurance community supports the NAIC model.

The model act effectively addresses STOLI while protecting life insurance taken out to benefit individuals, families, businesses and employees, as well as legitimate life settlements.

The NAIC panel voted to deter STOLI by prohibiting settlement of life insurance policies for five years from policy issuance when the policy is purchased for the purpose of selling it in the secondary market. However, the five-year prohibition would not apply if the insured, a family member or employer put up their own money or collateral to buy the policy. A wide array of other legitimate life insurance arrangements are also protected by the NAIC proposal (see *moratorium details on page 3*).

Far from being a blanket five-year ban, as some have charged, the NAIC model represents a carefully-drafted balancing of interests between allowing policy owners to settle for legitimate reasons and preserving the integrity of state insurable interest statutes.

The NAIC Executive Committee and Plenary will consider the model at its upcoming Spring National Meeting scheduled for March 9-12 in New York City.

National Conference of Insurance Legislators

NCIIL says it intends to devote considerable time and energy to reviewing life insurance settlement activities with an eye towards developing a new model act to address STOLI problems. NCIIL is likely to establish a work plan for its review at its Spring Meeting in Savannah, GA, scheduled for March 1-4.

States Where Action is Expected

Illinois: Legislation patterned after the amended NAIC model act has been drafted and is expected to be introduced soon in the Illinois General Assembly. The bill will be supported by the life insurance community and the Illinois Department of Insurance.

Indiana: Legislation designed to crack down on STOLI transactions (H. 1248) has been introduced in the Indiana Legislature. The bill, which would prohibit the sale of a life insurance policy that is financed with the intent to be sold to investors who have no insurable interest in the insured, passed the Insurance Committee unanimously on Feb. 20. ACLI testified in support of the concept of the bill, and suggested that the Committee consider amending the bill to reflect the approach taken by the proposed amendments to the NAIC model. Meanwhile, legislation (S. 144) supported by

the life settlement industry has been introduced in the Senate. This bill does not include the STOLI language and other consumer protection provisions contained in the amended NAIC model. The life insurance community is actively opposing the legislation.

New York: Both the State Assembly and the Senate are likely to consider legislation drafted by the New York State Department of Insurance that incorporates some of the NAIC model's language but takes a different approach to STOLI. Rather than attempting to prescribe which transactions are allowed and which are prohibited, the New York approach seeks broader regulatory oversight of life settlements. This approach includes new consumer protection provisions, disclosure requirements and anti-fraud protections. The legislation was considered last year as A.8785-C in the Assembly and S.8463 in the Senate.

North Dakota: Senate Bill 2268, which tracks the amended NAIC model act, was adopted unanimously by the Senate Industry, Banking and Labor Committee January 30, 2007, on the strength of testimony given by the Insurance Commissioner, the North Dakota Bankers Association, ACLI and NAIFA. The bill later passed the full Senate unanimously and is scheduled to be heard in the House Industry, Banking and Labor committee in early March.

Moratorium Exceptions

The NAIC Life Insurance and Annuity (A) Committee proposal provides numerous exceptions under which policyholders could settle their policies and not be subject to the settlement waiting period. For example, common uses of life insurance in estate planning, business continuation planning, and employee benefit planning would not be affected by the moratorium.

Specific "life circumstances" exempted from the five-year moratorium are:

- A terminal or chronic illness;
- B death of a spouse;
- C divorce;
- D retirement from full-time employment;
- E physical or mental disability preventing full-time employment;
- F bankruptcy or insolvency.

The (A) Committee proposal also would allow settlements after two years when:

- A policy premiums have been funded exclusively by the insured;
- B there is no agreement or understanding that a policy would be settled at the inception of the contract;
- C neither the insured nor the policy has been evaluated for settlement.

While the NAIC model act was just amended in December, 2006, and is awaiting adoption by the full NAIC membership in March, 2007, legislation is expected to be introduced in five or more additional states this year.

Opinion Letters

New York: On Dec. 19, 2005, the New York Insurance Department's Office of General Counsel (OGC) issued an opinion stating a valid insurable interest does not exist in a certain STOLI transaction and thus the transaction is impermissible under New York law.

The OGC responded to an inquiry involving banks proposing to loan money to high net worth individuals to purchase life insurance policies and pay premiums due under an option agreement to sell the policies to third parties on a predetermined date, which would be at least two years from the date of the loan.

OGC said that as described, it appears the intent of the arrangement is to facilitate the procurement of life insurance policies solely for resale. "It is our view that a plan of this nature does not conform to the requirements of the New York Insurance Law," OGC said.

OGC based its opinion on New York's insurable interest law. The transaction presented involves the procurement of life insurance solely as a speculative investment for the ultimate benefit of a disinterested third party, OGC said. This arrangement is "contrary to the long-established public policy against 'gaming' through life insurance purchases," OGC said.

Utah: On July 10, 2006, the Utah Department of Insurance issued Bulletin 2006-3 reminding life insurance companies, agents and viatical settlement providers that transactions involving the purchase of a life insurance policy, premium financing through a non-recourse loan, the sale of the policy in the secondary market and a payment to the policy applicant are not compliant with the insurable interest requirements of Utah law.

The Bulletin says that to determine if an insurable interest exists, the department will look at the entire transaction and will not limit its review to only that part of the transaction that relates to applying for life insurance. The Bulletin describes transactions in which a third-party initiates and arranges the transaction, and ultimately expects to receive the proceeds of the insurance policy.

"The third party has no insurable interest in the person insured because a lawful and substantial interest does not exist in having the life of the insured continue; in fact, there is a substantial interest in *not* having the life of the person continue," the Bulletin says.

Louisiana: On Sept. 5, 2006, Louisiana Insurance Commissioner James J. Donelon issued Bulletin No. 06-05, which deals with whether an insurance company can question policy applicants about their intentions regarding ownership and transfer of the policy. Commissioner Donelon noted that it has come to his attention that some investors, seeking to own policies insuring the lives of those in which the investors lack an insurable interest, have begun to initiate the creation

of life insurance policies for the purpose of settlement in contravention of controlling Louisiana law.

These arrangements, Commissioner Donelon said, may violate some or all of several Louisiana Insurance Code provisions, including insurable interest, the prohibition against wager policies, the prohibition on "wet ink" life settlements, premium finance and usury.

The life insurance community supports Commissioner Donelon's comments on STOLI and its possible violation of Louisiana law. However, we take issue with one aspect of

Bulletin No. 06-05, which prohibits insurance companies from asking questions on policy applications that could help identify whether the policies are for legitimate purposes or for STOLI. We will continue to work with Commissioner Donelon on ways that will help life insurance companies identify illegal transactions.

MYTHS & FACTS

1. Myth: The life insurance industry wants to restrict all life settlements. **Fact:** The life insurance community recognizes and supports the right of our policyholders to sell legitimate life insurance policies in the secondary market. Policyholders often have compelling reasons to sell their life insurance policies. Our concern is not with settlements involving life insurance policies that were purchased consistent with the intent of state insurable interest laws—laws designed to make sure that all policy owners have an insurable interest in the insured at the time the policy is taken out in order to protect their families and their businesses. Rather, we strongly oppose those who want to corrupt the legitimate settlement market with contrived arrangements that circumvent those laws.

2. Myth: The STOLI market would not have developed if life insurance policies had greater cash surrender values. **Fact:** This argument is a red herring. STOLI promoters have no interest in the policy's cash value. Promoters are only interested in receiving the policy's death benefit. A life insurance policy's cash value is important when life insurance is purchased for appropriate reasons. Cash value provides liquidity to a policy owner. Some policy owners turn their cash value into annuities. Cash value also assures that premiums can remain level throughout the life of the contract. These benefits of cash value are inconsequential in the STOLI market.

STOLI Alert is published by the Association for Advanced Life Underwriting, American Council of Life Insurers, the National Association of Insurance and Financial Advisors and the National Association of Independent Life Brokerage Agencies.

Readers are encouraged to copy and share the information contained in **STOLI Alert**.

For further information about **STOLI Alert** and the issue of stranger-originated life insurance, please contact us.

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3. Myth: Insurance company pricing and underwriting practices, such as lapse rates, are the real reason the industry opposes STOLI arrangements. **Fact:** This is also a red herring. The reason the life insurance industry strongly opposes STOLI is that it attempts to circumvent the intent of state insurable interest laws. On the other hand, do those who promote STOLI use underwriting, pricing and other factors to their advantage? Yes they do.

Insurance companies underwrite and price policies based on several factors such as age and health. Because of state solvency requirements, insurers must price their policies to assure they maintain adequate reserves to pay all valid claims promptly. It is true that some policyholders allow their contracts to lapse when they are no longer needed. Insurance companies account for this in their pricing, which helps lower the price of insurance for everyone.

4. Myth: No one is harmed by STOLI. **Fact:** STOLI is life insurance initiated by strangers for their own investment purposes. It attempts to circumvent the intent of state insurable interest laws that assure proper and responsible use of life insurance. A stranger with no insurable interest should not be allowed to initiate coverage and profit from policy-death benefits. STOLI violates the public policy of prohibiting wagering on human life.

From an insurance standpoint, STOLI threatens to undermine the life insurance market for senior citizens. Life insurers have increasingly found ways to make life insurance both available and affordable to senior citizens who want to secure the financial future of a child, a grandchild or other family member. However, if millions of dollars in benefits are paid for contrived arrangements, who can predict what will happen to this market?

Should this growing market be impaired due to skyrocketing and inappropriate claims, the real victims of STOLI could well be those senior citizens who have legitimate needs for life insurance.

TESTIMONY SUPPORTING SB 2268

BY

**J. BRUCE FERGUSON
AMERICAN COUNCIL OF LIFE INSURERS**

March 6, 2007

HOUSE INDUSTRY BUSINESS & LABOR COMMITTEE

REPRESENTATIVE GEORGE KEISER, Chairman

Good morning, Mr. Chairman and members of the committee. My name is Bruce Ferguson, and I am Senior Vice President, State Government Relations with the American Council of Life Insurers. ACLI is a national trade association whose 377 member life insurers account for over 90 percent of the life insurance in force in the United States and in the great state of North Dakota.

I am here today to express our strong support for Senate Bill 2268, which updates North Dakota's viatical and life settlement law. This bill will go a long way toward addressing the growing problem of stranger-originated life insurance transactions by facilitated by settlement companies, as was just explained by Commissioner Poolman.

The work product reflected in this bill is the result of a year-long investigation into the issue by the National Association of Insurance Commissioners, under Commissioner Poolman's leadership. In his remarks, the Commissioner summarized the many issues addressed by this bill quite effectively, so in the interests of your valuable time I won't be repetitive. However, I would like to add additional emphasis to a couple of points he made, because it is important to understand from our perspective what this bill does, and what this bill does not do.

This bill does protect the integrity of the concept of insurable interest – a critically important concept that has been around since the 17th century, and which remains one of the most fundamentally important principles upon which life insurance is based.

North Dakota has one of the most clear and meaningful insurable interest laws in the country. In the material I've provided you is an excerpt from your insurable interest law. It provides, in essence, that at the time the life insurance policy is issued, the person who procures the policy, or causes the policy to be procured, must have an insurable interest in the individual whose life is being insured.

What does insurable interest mean? Well, the law goes on to provide that insurable interest means the person procuring the policy must have a lawful and substantial economic interest in having the life of the individual insured **continue**, as distinguished from an interest that would arise only by, or would be enhanced in value by, the **death** of the insured.

Now, let me describe what's going on out there in the market place and why this bill is so important to us. I've also included in your material an excerpt from an advertisement that appeared this time last year in an Arizona newspaper, *The Desert Sun*.

It starts out: "How much life insurance would you have if you didn't have to pay anything to get it? It goes on to say "lenders are now eager to make safe, secure, non-recourse loans to you, so you can purchase a life insurance policy on your life, using the lenders money and not yours, that you can eventually sell to the secondary market for a substantial profit." The example cited involves a 75 year old male purchasing a 10 million dollar policy using money provided by a lender, not his own, and then selling the policy after the state's "wet ink" law expires to an investment firm in the secondary market for maybe \$500,000 **for the privilege of purchasing his policy.**

So what's happening here? A structured finance firm, investment bank, maybe even a foreign hedge fund – typically represented by a life settlement company – initiates through premium financing the purchase of a life insurance policy by an individual. The transaction is marketed and structured in a way that results in the later purchase

of the policy by the settlement company, either on its own behalf or on behalf of investors. These third parties now own a policy they were prohibited by the insurable interest law from acquiring when the policy was first taken out. And now, the sooner the insured dies, the more profit the third-party investors make.

Mr. Chairman and members of the committee, a life settlement company should be in the business of buying life insurance policies from people **who already have them** but for some reason no longer need them. Let me say up front that ACLI has no quarrel with that.

But I find it astonishing that some life settlement companies would object to the provisions of this bill governing the financing of life insurance premiums. The fact that they do speaks volumes and is proof positive of what's going on here. They are trying to protect their ability to arrange for the financing of a life insurance policy so they can buy that policy at a later date, for their profit and the profit of investors once the person dies, **the sooner the greater**.

This bill essentially stands for the proposition that if you're using someone else's money and putting up no collateral to finance the purchase of a life insurance policy, you have to wait five years to sell it to someone **without an insurable interest**. There are even exceptions to this rule, such as chronic or terminal illness, death or divorce of a spouse, situations like that. And if you are using your own assets or putting up your own collateral to finance the purchase of the policy, the waiting period is two years, just as it is today under current North Dakota law.

For a person who is financing the purchase of a life insurance policy for legitimate uses, a waiting period with these exceptions should not be a problem. After all, the person is intending to **keep** the policy to provide for family or business protection or for estate planning purposes. And, the person can sell it or transfer it at any time to another person **with** insurable interest or under the specified exceptions. A waiting period does, however, act as a deterrent to stranger-originated life insurance transactions. It makes the investors wait up to five years before they can get their hands on the policy, which makes their investment less predictable.

You may hear from the opponents of the legislation that this bill impairs a person's property rights – that life insurance is property that should be used and disposed of by a person without limitation. Yes, life insurance is property, and like other forms of property it can be assigned, sold, or pledged as collateral.

But it is fundamentally different than any other form of property. Why? Because it's the only financial instrument that instantly creates a large sum of money that is payable at the **death of a human being**. We are not discussing mere property – we are talking about contracts on people's lives!

The only right that is limited by this bill is the right of a life settlement company to directly or indirectly arrange for the financing of a life insurance policy for the purpose of buying and selling it in the secondary market at a later time. Mr. Chairman and members of the committee, I don't think that's a right you should be willing to protect. **The value of human life should not be reduced to a commodity that is auctioned off in the futures market to the highest bidder.**

That's not what life insurance is all about. That's not why Congress has granted tax free treatment to the build up of life insurance policy values and to policy death benefits paid to beneficiaries. Life insurance is designed to be long-term protection for families, and Congress provides incentives for families to keep the product for the long term.

By design, permanent life insurance policy premiums pay for the cost of the death benefit and create a savings component (cash value) to help cover the rising cost of life insurance as one gets older. As an insured ages, if death protection becomes less important, the cash value can pay for various living expenses, such as long-term care.

There is no good public policy reason to take a product designed to provide long term financial security into a way for investors to make a quick buck. There is a lot at stake here, and I hope you'll agree that for the sake of millions of families and business that rely on it, life insurance is a benefit worth preserving and protecting.

Mr. Chairman, there are many potential risks to consumers who "lend their lives" to these transactions. Let me give you a couple of examples.

First, once you've sold your "unused insurance capacity", it's gone. Someone else owns it. So if you later realize that your family or your business really needed the insurance, you may find that insurers are unwilling to give you more insurance because your capacity is already used up.

Second, although the life insurance may be "free" to the person who pays no out-of-pocket costs for the policy, it has significant economic value that may be taxable. In fact, there are many ancillary tax issues that at this point have no clear answers. Just last month, the US Senate Finance Committee called us in for a meeting to discuss the revenue implications of these transactions. Although they seem to be focused on taxing the investors, it is perilously close to a tax on the product, which in our view would end up killing the goose that lays the golden eggs.

Mr. Chairman and members of the Committee, I thank you for the opportunity to speak to you today about this critically important piece of legislation. I urge you to vote this bill out with a Do Pass recommendation, and I am pleased to answer any questions you may have.

Seniors Beware: What You Should Know About Life Settlements

February 8, 2007

Lately, more and more seniors are hearing about opportunities to sell their existing life insurance for cash in transactions known as life settlements. A life settlement, or senior settlement, as they are sometimes called, involves selling an existing life insurance policy to a third party—a person or an entity other than the company that issued the policy—for more than the policy's **cash surrender value**, but less than the **net death benefit**.

Life settlements can be a valuable source of liquidity for people who would otherwise surrender their policies or allow them to **lapse**—or for people whose life insurance needs have changed. But they are not for everyone. Life settlements can have high transaction costs and unintended consequences. And even if you decide a life settlement is generally right for you, it can be hard to tell whether you are getting a fair price.

If you are considering selling your life insurance policy to a third party, you can help protect yourself by familiarizing yourself with your existing policy so that you fully understand your options, becoming fully informed about life settlements, shopping around for the best offer, and dealing only with licensed buyers and brokers. NASD is issuing this Alert to highlight the questions you should ask and the factors to consider before entering into a life settlement.

What Is a Life Settlement?

Until fairly recently, if you owned a life insurance policy that you no longer wanted or needed, you had two choices: surrender the policy for its cash value or allow it to lapse. Now, there is a third option: selling your policy (or the right to receive the death benefit) to an entity other than the insurance company that issued the policy in a transaction known as a life settlement.

The life settlement market emerged as an offshoot of the viatical settlement industry that developed in the 1980s as a source of liquidity for AIDS patients and other terminally ill policyholders with life expectancies of less than two years. Unlike viaticals, however, life settlements involve policyholders who are not terminally ill, but generally have a life expectancy of between two and ten years. Life settlements also tend to involve policies with higher net death benefits than viaticals.

The life settlement market has expanded rapidly in recent years. One recent study estimates that existing policies with a collective face value of \$5.5 billion were sold by policyholders to investors in 2005, while others suggest that the potential market exceeds \$100 billion.

How Do Life Settlements Work?

The purchasers of life settlements, sometimes called life settlement companies or life settlement providers, generally are institutions that either hold the policies to maturity and collect the net death benefits or resell policies—or sell interests in multiple, bundled policies—to hedge funds or other investors. In exchange, you receive a lump sum payment. The amount you will receive in the secondary market depends on a range of factors, including your age, health and the terms and conditions of your policy—but it is generally more than the policy's cash surrender value and less than the net death benefit.

When you sell your life insurance policy, whoever buys it is acquiring a financial interest in your death. In addition to paying you a lump sum for your policy, the buyer agrees to pay any

additional premiums that might be required to support the cost of the policy for as long as you live. In exchange, the buyer will receive the death benefit when you die.

Factors to Consider When Deciding to Sell Your Life Insurance Policy

Life settlements have proven profitable not only for institutional investors that purchase policies, but also for the providers and brokers who handle these transactions. As a result, competition among life settlements providers for individuals seeking to sell or otherwise terminate their life insurance policies has become increasingly intense. Because the life settlement industry is relatively new and may target seniors who may be in poor health, it can be prone to aggressive sales tactics and abuse.

That does not mean that you should never consider a life settlement. A life settlement might make sense for you if you no longer want or need your current policy—or if you can no longer afford the expense of paying insurance premiums and are willing to give up or replace the coverage. Even then, however, you should proceed with caution. Here are some of the key factors you should consider:

- **Ongoing Life Insurance Needs**—If you are considering buying a new policy with the proceeds of the life settlement, you will need to determine whether you will be able to get a new policy with equivalent coverage—and at what cost. Your old policy will still be in force and may affect your ability to get additional coverage. Even if you can get a new policy, you may have to pay higher premiums because of your age or changes in your health status. If your goal is to retain coverage but lower the premiums you pay or otherwise obtain different features, you might want to consider options such as reducing your existing amount of policy coverage or making a "1035 Exchange."

1035 Exchanges

If you're thinking of switching from one life insurance policy to another, you should consider whether a "1035 Exchange" would be more beneficial than a life settlement. Depending on your circumstances, if you opt for a life settlement, you may have to pay taxes if the cash surrender value of your policy—or the amount of a life settlement—exceeds the premiums you've paid.

The Internal Revenue Service allows you to exchange an insurance policy that you own for a new life insurance policy insuring the same person without paying tax on the investment gains earned on your original contract—which could be a substantial benefit. Because this is governed by Section 1035 of the Internal Revenue Code, these are called "1035 Exchanges." But there are other factors you should consider when deciding whether to exchange your policy, including potential loss of death benefits. For more information and a list of questions to ask, see NASD's Investor Alert entitled *Should You Exchange Your Life Insurance Policy?*

- **Less Costly Alternatives**—If one of the factors driving your decision is a need for cash, be aware that surrendering your life insurance policy for its cash value or pursuing a life settlement are not your only options—especially if you would ideally like to retain your coverage. For example, you might want to see whether you can borrow against your policy. You might also be eligible for **accelerated death benefits**, which allow an individual with a long-term, catastrophic, or terminal illness to receive benefits on his or her policy prior to dying. Check with the company that issued your policy before leaping into a life settlement. You may still decide that a life settlement is the best alternative for you, but you should be aware of all of your options before making up your mind.

- **Difficulty Determining Fair Prices**—One of the hardest things to know when you are selling a life insurance policy is whether you are getting a fair price for your policy. There is no transparent secondary market for life insurance policies. The best way to make sure you are getting a fair price is to shop around. This can mean directly contacting multiple life settlement companies, using a licensed life settlement broker who will shop your policy around on your behalf, or contacting your broker or other financial services provider.
- **Impact on Your Finances**—A cash payment from a life settlement can have unintended financial consequences, especially if your financial circumstances have changed from when you first bought the policy. For example, if you currently receive state or federal public assistance, such as Medicaid, a life settlement can negatively impact your ability to participate in that program. Before you proceed with a life settlement, be sure you fully understand the financial implications for you and your family. You may want to consult your attorney, accountant, or other legal or financial professional.

How Can I Protect Myself?

If you decide to go forward with a life settlement, here are some questions you should be sure to ask.

1. **Is the life settlement broker or provider licensed in my state?** A growing number of states regulate life settlement companies and life settlement brokers to some degree, and may require that they be licensed. Be sure to ask your state insurance commissioner whether the life settlement company or broker you are dealing with is properly licensed—and whether either has a record of complaints. If you are working with a securities broker, NASD BrokerCheck should be your first resource to learn about his or her professional background, registration/license status and disciplinary history.
2. **What will happen to my policy?** Ask what the life settlement company that is buying your policy will do with it. Will they hold it themselves? Sell it individually? Or package it with other policies and sell interests in the package to other investors? The ultimate buyer of your policy will become responsible for paying the premiums and will collect the death benefit when you die—and, as noted below, any interim and ultimate buyers of your policy will also have access to a great deal of personal information about you, including your health status.
3. **What information will I have to provide? To whom? For how long?** When you sell your life insurance policy, you will have to sign a release authorizing the release of medical and other personal information so that the buyer can determine how much to offer for your policy. You may also have to agree to provide periodic updates about your health. Once the buyer obtains that information, it may be shared with other parties, including lenders or third party investors.
4. **How can I protect my privacy?** Before accepting any offer from a life settlement company, you should carefully read the application, and make sure that the company has procedures in place to protect the confidentiality of your information. If it will be sold, ask to whom, and whether the end buyers will have access to your personal information. If you use a life settlement broker, find out the names of the life settlement companies from whom the broker solicits bids, and ask about the privacy policies of all parties or potential parties to the transaction. In many cases, state regulations govern the handling of

confidential information. Contact your state insurance commissioner to find out what regulations apply.

5. **What's the best price I can get for my policy?** If you are using a life settlement broker, ask what bids were received, and what steps the broker used to make sure you are being offered the most competitive price available. If you are approached by someone soliciting you to sell your life insurance policy, make sure you understand that person's role in the transaction: is he or she a life settlement broker who represents you, or is the person affiliated with a particular life settlement company? If the answer is the latter, the person may only obtain an offer from that company, making it hard for you to know whether you are being offered a competitive price for your policy.
6. **What are the transaction costs?** Life settlements can have high transaction costs. The commissions paid by life settlement companies to life settlement brokers and other financial professionals involved in the transaction can be as high as 30%. Ask your broker or other financial adviser what they are being compensated for their role in the transaction, and what other parties are receiving commissions. If someone recommends a particular life settlement to you, find out what they are being paid, and by whom.
7. **What are the tax consequences?** The lump sum payment you receive in exchange for your life insurance policy can be taxable, depending on your circumstances. Before entering into a life settlement, check with a tax professional about the tax implications of any transaction you are considering.
8. **What if I change my mind?** Always remember that you do not have to accept an offer to purchase your life insurance policy, even if you shopped around for the best price. If you do accept an offer and later reconsider, be aware that some states have laws that allow you to change your mind within a certain amount of time.
9. **Is the life settlement in my interest or my investment professional's?** At least one marketing brochure targeted at investment professionals not only touts the potential commissions from life settlements, but also emphasizes that additional revenues can be generated from the seller's purchase of other investment products using the proceeds from the life settlement. Citing industry statistics, the brochure notes that almost half of all life settlement transactions result in the purchase of new life insurance. In other words, your investment professional stands to make two commissions off of a life settlement transaction. And you may end up replacing a perfectly good policy with a costly new one.

Reminders

Life settlements may make sense for people who no longer need or want their insurance policies, and would otherwise surrender their policies or allow them to lapse. But even then, you should proceed with caution. Consult with your broker or other financial services provider, and make sure that you:

- are dealing with properly licensed entities;
- are aware of the confidentiality policies of the parties involved;
- are getting a fair price; and
- understand the tax and other implications of the transaction.

Where to Turn for Help and Additional Resources

Life settlements can involve almost any kind of insurance policy, including variable policies. However, because only variable insurance products are securities, NASD only has jurisdiction over life settlements involving variable policies.

If you have questions or wish to file a complaint about a life settlement, be sure to call or write your state insurance commissioner. If your complaint concerns a variable life insurance policy, you may also file a complaint with NASD.

For more information, please read the following materials:

- NASD Notice to Members 06-38 (which discusses concerns about, and member firm obligations in the context of, sales of existing variable life insurance policies to third parties)
- Selling Your Life Insurance Policy: Understanding Viatical Settlements (NAIC alert)
- Viatical Settlements: Buying Viaticals as Investments (NAIC alert)
- NASAA Alert Concerning Viatical Settlements
- Should You Exchange Your Life Insurance Policy? (NASD alert)

Glossary of Terms: Life Settlements

Accelerated Death Benefits

Also known as "living benefits," accelerated death benefits provide payments to policy holders who have a long-term, catastrophic, or terminal illness—payments that ordinarily would not be available prior to the policy holder's death. Rules concerning accelerated death benefits vary from company to company and from policy to policy. In some cases, depending on the term of the policy or contract, the beneficiaries of the policy may be entitled to a reduced death benefit.

Cash Surrender Value

The cash surrender value of a life insurance policy is the amount you can collect if you cancel (or "surrender") the policy before it matures or before you die. The amount is typically based on the cash you've built up in the policy over time (your tax-deferred savings) minus any surrender charges or outstanding loan balances.

Lapse

Lapse refers to the termination of an insurance policy when an individual fails to pay his or her premiums on time. If you allow a policy to lapse, you typically cannot collect any cash surrender value that would otherwise be available.

Net Death Benefit

A death benefit is the amount an insurance company pays to a policy holder's beneficiary when the policy holder dies. Not all life insurance policies or annuity contracts provide for this sort of benefit, and not all death benefits are calculated the same way. The net death benefit is the amount specified in the insurance policy or annuity contract, minus any unpaid premiums that are due and outstanding loan balances or other withdrawals. In the case of variable life insurance or variable annuities, investment gains and losses can impact the amount of the death benefit.

Life settlements can involve almost any kind of insurance policy, including variable policies. However, because only variable insurance products are securities, NASD only has jurisdiction over life settlements involving variable policies.

If you have questions or wish to file a complaint about a life settlement, be sure to call or write your state insurance commissioner. If your complaint concerns a variable life insurance policy, you may also file a complaint with NASD.

For more information, please read the following materials:

- NASD Notice to Members 06-38 (which discusses concerns about, and member firm obligations in the context of, sales of existing variable life insurance policies to third parties)
- Selling Your Life Insurance Policy: Understanding Viatical Settlements (NAIC alert)
- Viatical Settlements: Buying Viaticals as Investments (NAIC alert)
- NASAA Alert Concerning Viatical Settlements
- Should You Exchange Your Life Insurance Policy? (NASD alert)

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Chairman Keiser, and members of the House Industry Business and Labor Committee, my name is Tom D. Kelsch, with the Kelsch Law Firm. I am presenting your committee with this printout on behalf of Peachtree Settlement Funding. Peachtree Settlement Funding was founded in 1996 and is a leader in the secondary market for life insurance.

Peachtree is opposed to SB 2268 and requests a "Do Not Pass" recommendation from this committee for the following reasons:

1. **SB 2268 violates long standing property rights of North Dakota consumers.**

In 1926, the Supreme Court of North Dakota held that, "a life insurance policy, under which the insured has the right to change the beneficiary, is regarded as a chose in action, and may be assigned or transferred by will in this state." *Talcott v. Bailey*, 208 N.W. 549, 553 (N.D. 1926). Furthermore, the insurance code explicitly allows the transfer of a life insurance policy: "A life insurance policy may pass by transfer, will, or succession to any person, whether that person has an insurable interest or not . . ." NDCC 26.1-33-33.

An individual has an unlimited interest to procure coverage on his own life and do with it what he pleases. "An individual of competent legal capacity may procure or effect an insurance contract upon that individual's own life or body for the benefit of any person." NDCC 26.1-29-09.1(1). Insurable interest is only required at the time of purchase. "No person may procure or cause to be procured an insurance contract upon the life or body of another person unless the benefits under the contract are payable to the individual insured or that individual's personal representatives, or to a person having, *at the time the contract was made*, an insurable interest in the individual insured." NDCC 26.1-29-09.1(1) (emphasis added). SB 2268 would reverse or infringe upon all these established North Dakota laws and the property rights that they afford consumers.

2. **SB 2268 is based on unapproved amendments to the NAIC Model Act that were passed by the NAIC Life Insurance Committee.** These amendments are subject to review and action by the NAIC Executive Committee and the full membership of the NAIC. The language in SB 2268 cannot be called an NAIC Model any more than the language in a legislative bill can be called law after it has passed a committee in one chamber. It is highly unusual for interest groups or anyone else to bring a not-enacted NAIC proposal to legislatures and claim any sort of blessing of the NAIC.

3. **The NCOIL has adopted a resolution urging the NAIC not to adopt the Model Act at this time.**

4. **SB 2268 unjustifiably imposes a broad five-year ban on life settlements.** This is a major change in the well-reasoned NAIC Model and the established laws of all 34 states with a settlement law. The 5 year ban includes if a consumer has ever been evaluated for settlement, on any policy, at any time prior to the first two years of the policy in question. The 5 year ban does not respond concerns about investor-initiated life

insurance; expands the settled two-year period by 250% and sweeps in many traditional life settlements – since 40% of policies lapse in the first five years – depriving a substantial number of policyowners of the established benefits of settlements. In fact, primary supporter of the five year ban, the ACLI, less than a year ago categorically stated that a five year ban was bad for consumers and should be rejected. “The legislation pursued by ACLI will not affect life settlements entered into more than two years after policy issuance.” (ACLI fact sheet, “Key Points on Stranger-Owned Life Insurance.”)

5. **There are serious concerns and uncertainties on SB 2268 effect on legitimate lending transactions, which may violate provisions of the Gramm-Leach-Bliley Act and/or the National Bank Act**, all of which are in place to ensure that consumers can access capital from lenders to fund needed death benefit coverage. The Gramm-Leach-Bliley Act prohibits states from significantly interfering with banks’ ability to participate in any way with, directly or indirectly; with cross marketing which allows insurance sales. GLBA also preempts state laws which prevent bank activities while allowing competing insurer activities. The NBA prevents states from passing laws, which infringe on banks’ ability to assess good risks for loans or to determine a property’s adequacy to serve as collateral.

6. **It is premature to act on SB2268**. During the December NAIC Life Committee debate, concerns about federal preemption were raised by The American Bankers Association’s insurance affiliate, the American Bankers Insurance Association (ABIA), and representatives from the financial services, premium financing and life settlement markets. The ABIA declared the debated proposal ill-considered and illegal. A representative from the Office of the Controller of the Currency testified that the OCC had concerns about federal preemption and requested additional time to review and comment. No review of this issue by the NAIC has ever been offered. Nor have state banking regulators been consulted, even though SB 2268 would not assert insurance code jurisdiction over its proper subject matter (insurance policies and insurance companies and agents), but rather asserts insurance code and insurance commissioner jurisdiction over lending transactions, banks, other lenders, and borrowers, as well as potential securities transactions. This is an overreach and should not be the subject of rushed legislation.

**North Dakota House of Representatives
Industry, Business and Labor Committee
March 6, 2007**

SB 2268 (Viatical Settlements; Life Settlement industry)

Chairman Keiser and members of the Committee, my name is Robert Harms, I am a lobbyist for Imperial Finance and Trading, LLC a member of the Life Insurance Settlement Association (LISA) and who is engaged in the life settlement industry. Life settlements or viatical contracts are simply the sale of a life insurance policy to a third person.

THE ISSUE: This legislation is not about protecting North Dakota Consumers.....it's about protecting margins (profits) of life insurance companies. (Or stated differently: "What problems exist in North Dakota to warrant a wholesale change of our law"?)

Imperial OPPOSES SB 2268 for several reasons:

1. No problems in North Dakota have been shown to warrant repealing our law that was completely rewritten at the Insurance Department's request in 2001.
2. The bill is untested, and is not supported by legislative experts such as NCOIL.
3. It imposes unduly restrictive regulations (e.g. 5 year limit) on North Dakota consumers, depriving them of a more robust insurance market to better serve them.

Overview: Competition in Life Insurance Sector: Life insurance settlements evolved from 1990s to date, with Life Insurance returns/margins being impacted and companies responded with accelerated death benefits (ADB), and regulatory efforts to impede secondary market entry/efficiency from life settlement companies—in order to maintain life insurance margins resulting from lapsed policies. According to A.M. Best Co., life settlement purchases have grown from \$2.5 billion in 2003 to more than \$10 billion in 2005 based on face amounts. Some expect the industry to grow to \$100 billion. (See attached *Journal of Practical Estate Planning* August, 2005).

"According to a 2005 joint study by the Society of Actuaries and LIMRA International, (Life Insurance Market Research Association) nearly 40% of all life insurance policies lapse in the first five years. And a 2004 report by Millman USA, a leading actuarial consulting firm, found that, using recent industry levels of mortality and lapse experience, nearly 88% of universal life insurance policies, and over 85% of term policies, issued in the United States never result in a death claim."

By extending the 2 year ban to 5 years and incorporating the other provisions of SB 2268, the insurance companies will benefit (i.e., profit) from this continued high rate of lapse.

North Dakota Experience:

In 2001, North Dakota repealed its existing statute, and passed NDCC 26.1-33.2 which was a "strong consumer protection bill" and would address "two major fraudulent acts"—"clean sheeting" and "wet paper" transactions. (See *Legislative Hearings*, 57th *Legislative Assembly*; SB 2150) The bill included a two year limit on the sale of life insurance policies that was "to stop abuse". (SB 2268 now proposes a five year limit on consumers to "stop abuse").

I'd like to take you through the current law that was passed in 2001.

Current Law passed (2001) at request of Insurance Department:

NDCC 26.1-33.2 (13 pages)

- License required (\$250 fee); disclosure of stockholders, officers etc.
- Commissioner may refuse to license
- License provided if: detailed plan of operations; competent and acting in good faith; good reputation; certificate of good standing; anti-fraud plan
- Violation of law is Class C felony
- Commissioner may refuse to renew; revoke; may suspend: if applicant is convicted of dishonesty/fraud or is "untrustworthy"; pattern of unreasonable payments; guilty of felony or misdemeanor fraud;
- Contracts and disclosure forms subject to Commissioner approval
- Must file annual reports including: each policy, face amount and amount paid, date of death; amount of premium paid on policy; total policies and amount financed;
- Commissioner may examine, investigate
- Records must be kept and available to Commissioner
- Disclosure required: alternatives available including early death benefit, policy loans; proceeds may be taxable and subject to claims of creditors;
- Has right to rescind for 30 days; or 15 days from receipt of funds.
- Written disclosure must include: affiliation with insurer, if any; contact information of viatical settlement company; brokers compensation; amount of funds payable to viatical settlement company upon death;
- General rules:
 - Doctor certify of sound mind;
 - Sign written understanding of transaction
 - Consent to release of medical records
 - Must notify insurer of transaction
 - Absolute right to rescind within 30 days
 - Limited contact after signing agreement
 - Control of advertising (1 paragraph)
- **-Cannot transfer for TWO years after purchase (with exceptions)**
- Fraud/Prevention/Control provisions: prohibits fraud, prohibits felons convicted of dishonesty; knowledge of fraud must be reported to Commissioner; immunity from civil liability for reporting; information provided is not subject to discovery;

- Must have anti fraud plan in place; ability to investigate, procedures to detect/investigate fraud, and procedures for reporting same;
- Civil penalty of \$50,000 per violation and restitution
- Commissioner has right to publish administrative rules.

North Dakota law also prohibits inducements (rebates) to acquire insurance and requires an "insurable interest" for one to acquire insurance. See NDCC 26.1-04-03 (8) and 26.1-29-09.1(1)

In Contrast, some high lites of SB 2268:

- 10 pages of definitions
- 49 pages of new text
- Expanded licensing requirements; \$250,000 bond requirement (section 2)
- Great detail on how examinations are to be conducted (section 6)
- Doubles the period to rescind to 60 days
- Extraordinarily detailed disclosure requirements (six pages; section 7 pp.23-29)
- FIVE year limit on selling life insurance contract; (section 10)
- FIVE pages of restrictions on advertisements
- Includes criminal penalties of a **Class A FELONY** (20 years; \$10,000 fine).

SB 2268 is not needed to address transactions described since existing law requires an insurable interest and prohibits inducements or rebates to acquire life insurance policies. If violations are taking place, why not simply say.....you cannot fund in advance, the purchase of life insurance.

SB 2268 is untested

In addition, the National Council of Insurance Legislators (NCOIL) rejected this bill this past week by a significant margin and urged the National Association of Insurance Commissioners (NAIC) to hold the legislation for more study to the end of 2007. (Why should North Dakota rush to pass such a bill?)

Additionally, Governor Keating, of ACLI spoke with NAIC on May 3, 2006 and urged "amendments to NAIC Model Act" not a complete re-write and advocated 10 months ago for a two year limit on selling life insurance policies. (*See Senate testimony*).

No other state restricts the sale of an insurance policy after two-years.

Impact to consumer:

Life settlement: sale of an existing life insurance policy to a third party.

- reduces/eliminates premiums
- generates cash (for life needs/wants)
 - mortgages paid
 - family member financial needs
 - estate planning (estate tax/funeral expense)
 - long term care

-tool for charitable giving

Example: I own a life insurance policy on my mother.....we bought it 2 years ago, to help pay for estate tax, funeral expense etc. Why shouldn't I be able to sell that policy, if she needs to go into a nursing home, or wants to buy a house in Bismarck?

Twenty-six states currently regulate Life Settlements without the burden-some and restrictive provisions of SB 2268. There is not one piece of evidence to suggest that the changes to this NAIC model act are in response to any inadequacy in the original NAIC model language. Changes in SB 2268 reflect efforts to protect insurance company profits at the consumer's expense.

SB 2268 simply makes a participant in an investor owned life insurance transaction wait longer to obtain ownership of a policy, it does not preclude them from doing so. SB 2268 is about protecting insurance company profits not serving the publics interest.

Conclusion:

Not warranted

Not tested

Not fair for North Dakota citizens and consumers.

For these reasons we ask that you recommend a DO NOT PASS on SB 2268.

Life Settlements: A Legitimate Financial Planning Tool

Rick Gardner

Rick Gardner discusses situations in which life settlements of existing insurance policies may be an appropriate planning tool for your client. As oversight of these settlements increases, they may provide value in certain situations where your client's other options may be limited.

As financial planning professionals, it is our responsibility to introduce all applicable tools into the planning process for our clients. A tool that has been often maligned and overlooked is *life settlements*. Quite simply, a life settlement is the sale of an existing life insurance policy to a third party. This serves a client's financial needs by reducing or eliminating premiums, providing cash for needs such as long-term care, or acting as a tool for charitable giving.

Background of Life Settlements

In 1911, Chief Justice Oliver Wendell Holmes stated that a life insurance policy is a capital asset similar to a home, car, stocks or bonds. Traditionally, the value of the policy was fulfilled when the policy owner passed away. However, there were instances where the policy owner could receive value during his lifetime. Originally, it was the insurance agent who was approached by a terminally ill client, seeking cash for his life insurance policies. The agent would either approach an insurance company to secure

an accelerated death benefit or would negotiate a transaction with an individual to purchase the policy from the ill client.

During the earlier days of the AIDS epidemic, when a large number of people needed cash to provide for their care, an industry emerged in which viatical brokers would purchase life insurance policies for as little as possible and then sell them to funders. These funders were primarily private individuals, aligned with finance companies or insurance brokerage firms. But, as a 2001 CONSUMER REPORTS' article stated:

The industry has been dogged by problems—and thorny ethical issues. Insufficient consumer protection has left viators (the people who cash in their policies) with inadequate payments and investors stung after promised returns up to as much as 30 percent or more fail to pan out. Fraud has been so common a problem that the North American Securities Administrators Association, a group of state investment cops, named viaticals one of the top ten investment scams of 1999, along with telemarketing schemes and get-rich-quick seminars. Thirty-three of the 73 viatical companies Consumer Reports found operating in 2000 had been in trouble with regulators in the past two years. Among their problems: failure to register with securities or insurance authorities, misuse of investor funds, misstatements about the medical condition

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of patients, and a fraudulent practice called "cleansheeting." Under that scheme, viatical companies solicit patients with life-threatening chronic or terminal conditions to lie about their health and apply for life insurance policies, which are then resold to investors.

While viatical settlements provided some assistance to thousands of AIDS patients, these settlements may no longer represent a good investment for those purchasing the policies. The development of new treatments for HIV and AIDS has removed this group of policyholders from that category of patients considered to have a terminal medical condition.

As early as 1993, the National Association of Insurance Commissioners (NAIC) developed a model law to provide standards and guidelines. The revised model, introduced in 2001, reflects the emergence of life settlements for use with clients who are of advanced age and in declining health, as a viable tool for financial planning. In 2004, NAIC presented an NAIC framework to the House Financial Services Committee (HFSC) and Chairman Mike Oxley for modernizing the regulatory structure, including additional protections against fraud. The NAIC continues to work with HFSC to "implement national regulatory standards that will achieve the highest levels of marketplace safety and efficiency, while maintaining a competitive marketplace with the strong consumer protections that are the hallmark of state regulation."²

Many states have adopted some version of the statute or have developed regulations of their own.³ In January 2004, A.M. Best Co. issued its first ratings on securities collateralized by life settlements.⁴ Their involvement and scrutiny of this important tool is welcome and helps financial planning professionals as a reliable source for ascertaining which companies not only meet but exceed the state and industry requirements.

Life Settlements As a Legitimate Financial Planning Tool

The U.S. Census Bureau estimates that there will be 50 million people age 65 and older by 2010 (15 percent of the population). A large segment of this group owns life insurance purchased for earlier life-stage milestones and is no longer necessary for

those needs. According to a 2002 Wharton School of Business study, it is now estimated that the potential life settlement market could reach \$100 billion.⁵ Life settlements are becoming recognized by planning professionals as a viable financial planning tool and professionals and consumers alike are seeking more information. There are numerous reasons why a client may want to consider selling an insurance policy, including, but not necessarily limited to the following reasons:

- Insurance needs have changed.
- Premiums have become unaffordable or inconsistent with current needs.
- Estate planning goals have changed.
- Cash is needed to fund a different life insurance policy, annuity or investment.
- A change in business owners or key persons has occurred.
- Funds are needed for long-term health care.
- Funds are needed as a source of cash for charitable giving.

Life Insurance Needs Have Changed

Policies that were purchased to protect a young family in the case of the premature death of the insured or to fund college educations may no longer be appropriate as a client matures. Clients may divorce and remarry then change their estates accordingly. Clients may even outlive the beneficiaries of their life insurance. These policies, with escalating premiums, can become a financial burden on the client or an inappropriate use of his money. It is clear that in many situations, the needs of the client/insured change and the old policies may have outlived their usefulness. By selling the old policy, the client receives cash to purchase a more affordable policy to cover current needs and has additional cash for other insurance, investments or other uses.

A typical scenario might be a 76-year-old widower who owns a whole life policy with a face amount of \$8 million and a \$795,000 cash surrender value. He has outlived his wife, and he has provided for his children and grandchildren through trusts. The Life Settlement professional negotiates a settlement of \$2.3 million, giving him \$1.5 million over the cash value. The insured will have to weigh the benefits of a life settlement against using other assets to cover his current needs and preserving the \$8 million policy for his beneficiaries.

Your clients rely upon you for advice in estate planning, trust administration or financial planning. They may no longer need the life insurance they are carrying. The option of a life settlement presents another opportunity that should be discussed with your clients. It is also important to be cognizant of the fact that the needs for life insurance can change in businesses, as well.

Business Succession

Businesses have changing needs for life insurance—the insured leaves the company or retires, the company has a change in ownership, or the company can no longer afford the premiums. Taking advantage of key person insurance that has been purchased on an executive who is no longer going to stay with the company is a unique opportunity for a life settlement. A case in point: One particular advisor did not see the value of a client's key person insurance policy because it was a term policy with no cash value. However, when the company was sold, the policy was transferred as an asset. The new owners understood the policy's value and sold it in the life settlement market for several hundred thousand dollars.⁶

Another example of using a life settlement creatively is in the sale of a business. Consider the following example: A company owned key person policies with several million dollars in total face value. The cash surrender value was approximately \$800,000. The company's advisor was able to obtain a life settlement of \$3.5 million—\$2.7 million greater than the cash value of \$800,000. The extra amount received from the life settlement made up for the difference between the company's asking price and what it actually netted in the sale.⁷

While it is important to be aware of the opportunities that may arise in the business market, chances are, financial planning professionals will be called upon more often to help clients with life settlements in personal estate planning scenarios. One need becomes obvious if the client has an accident or develops a chronic illness—the need to pay for long-term care.

Need for Long-Term Care Protection

Without some form of coverage, the client could possibly deplete most or all assets on the cost of

long-term care, which averages \$70,080 a year in the United States.⁸ A Life Settlement can provide the money needed to purchase a long-term care insurance policy or one of the specialized life insurance or annuity products with long-term care benefits. The U.S. government's Medicare Web site expressly stipulates that life settlements are an opportunity for funding long-term care and offers a concise overview of requirements and limits for consumers and financial planners alike.⁹

One of the major myths is that wealthy clients have no need for long-term care protection because they could easily self-fund the costs. However, with the costs of care escalating at an average of five percent compounded per year, with no cap in sight, transferring the risk of that possibility to insurance or annuities, provides a sound stop-gap measure against serious erosion or depletion of assets. For clients who want to leave a legacy for family members or help a philanthropic cause, a life settlement is an excellent way to ensure the safety of assets.

Charitable Giving

Among wealthy insureds, a major beneficiary of life insurance policies is the nonprofit sector. Traditionally, policies were donated to the charity with the premiums to be paid by the organization. Many policies that have been donated have been allowed to lapse because the organization cannot afford to continue payment of the premiums and/or maintain the administrative review procedures of such policies. If the donor is in agreement, the policy could be sold to generate immediate revenue for the organization. "If they knew Life Settlements were an option, perhaps development officers would reconsider the practice of letting policies lapse," commented one philanthropic consultant whose clients include numerous foundations, universities and organizations. "Most development staff are not aware of Life Settlements, but I believe having knowledge of this new wealth management tool could help them make better decisions as it relates to managing their donated life insurance policies and donor acceptance programs."¹⁰

An even better way to handle charitable giving is for the policyowner to sell the policy, contribute the proceeds to the charity and, perhaps, take a higher write-off than he would have if he had donated the policy.

This was the case with the donor of a \$750,000 policy. The surrender value of the policy was

approximately \$142,000. However, the sale of the policy brought approximately \$225,000, giving the donor an additional \$83,000 charitable donation, which the charity was able to use immediately.¹¹

Profile of a Life Settlement Client

As stated on the Medicare Web site: To be eligible for a Life Settlement, you can't be ill and must be over age 70 (for females) or over age 74 (for males). In some situations, if your life expectancy is 12 years or less, a life settlement can be done at a younger age.¹² Those with serious health issues and a shorter life expectancy will receive higher settlement offers. The lower the cost to the purchaser to carry the policy and the more imminent the payment, the higher the negotiated settlement amount will likely be.

According to a 2003 study by Conning Research & Consulting and reported in NATIONAL UNDERWRITER:

Males account for most of the settlement business (73 percent to 27 percent female). This split roughly matches the historical experience with policy sales, although recent experience indicates the female share of new life insurance sales is closer to one-third. Less than 1 percent of the life insurance purchases involved insureds with a life expectancy of less than two years. (21 percent had a life expectancy of 2-5 years, 53 percent a life expectancy of 6-10 years, and 25 percent a life expectancy of 11 or more years). This is, in part, due to living benefit provisions, whereby insurers make a portion of the death benefit available to insureds with a terminal condition. Of all the policies purchased, 95 percent and 5 percent are permanent and term policies, respectively.¹³

The funding companies purchasing life insurance policies also review the following criteria to determine the purchasing price of the policy:

- Type of Policy: Whole Life, Variable and Universal Life, Joint and Survivor Life, Adjustable Life, Term and Group policies (if convertible)
- Policy face value
- Percentage of Cash Value to Death Benefit
- Percentage of Loans to Death Benefit
- Percentage of Premium to Death Benefit

Values-Based Case Studies

According to *Elderlifeplanning.com*, there are other benefits to candidates inquiring about Life Settlements. "Clients who qualify for life settlements can see what the highest purchase offer is. If they choose to accept the payment, they have added pure bottom-line dollars to their asset base."¹⁴

Case Study #1

A 79-year-old female approached her financial planner, worried about her ability to continue to pay her annual premiums of \$250,000 on her \$7 million face value Universal Life policy. She purchased the policy to pay all estate taxes and leave a substantial legacy to her children. She thought her only option was to lapse the policy and take the cash value of \$17,000. The financial planner realized that by negotiating a life settlement on the existing policy she would be able to receive enough cash from the old policy to invest in a new policy at a substantially lower premium. In fact, the settlement offer was for \$1.2 million and the new term life policy, for the same \$7 million face amount, has an annual premium of \$119,000. Using the life settlement allowed the client to continue to fulfill the desire to leave a substantial legacy to her children at a far more affordable cost.

Case Study #2

A male client, aged 82, had a Universal Life policy with a face amount of \$1 million, which he purchased to cover estate taxes. The client experienced a substantial reduction in estate value and no longer needed the policy to pay the taxes. The cash value on the policy was \$112,000. By utilizing the life settlement option, the client received \$257,000, twice the cash surrender value for his policy. The value-add of the life settlement in this case was the higher return on the investment he had made into the policy than he would have received by merely taking the cash surrender value.

Case Study #3

At age 75, a male client purchased a 10-year \$200,000 convertible term policy with his newly divorced daughter as the beneficiary, so that she would have financial support for herself and her children, if he were to die. In the seventh year of the policy, the daughter remarried and there was no longer any need for the insurance. The financial planner suggested a life settlement as a way of recouping the money the

client had invested into the policy. At the end of the conversion period, the policy was sold for \$27,000. Without the life settlement, the policy would have had no cash value at all.

Case #4

A 78-year-old male client asked his financial planner for a way to replace his existing nonguaranteed Universal Life policy with a guaranteed policy. The original policy had a \$12 million face value and a cash surrender value of \$177,000. By using a life settlement, the client received \$2 million and was able to purchase a new guaranteed \$12 policy with reduced annual premiums from \$500,000 to \$410,000. The life settlement not only helped him achieve his goal, it saved him one year of premiums because of the premium reduction.

While the value proposition for using life settlements is evident, it is important for the client considering a life settlement to know that there are tax consequences to this transaction.

Life Settlements and Taxation

Life Settlements have three areas of taxation consideration. First, total premiums paid by the policy owner are nontaxable and are the owner's cost basis. If the cash surrender value is greater than the total premium paid, the difference would be treated as ordinary income. Settlement proceeds that are in excess of cash surrender value may be treated as long-term capital gains.

Choosing a Life Settlement Professional

It is critical to seek out a reputable life settlement broker. The broker is the liaison between financial planning professionals and their clients, and life settlement funding companies. The exponential growth of this industry has spawned a plethora of individuals and companies proposing to negotiate life settlements on a client's behalf. The following is a condensed list of qualifications to be considered when choosing a life settlement broker¹⁵:

- Regulations on life settlement companies vary from state to state. Check your state's regulations.
- Some states require licensing; others do not. Check to be sure the life settlement broker is licensed through the state Department of Insurance, if required.
- Though the life settlement industry is relatively new, it is still important to find out how long the broker has been in business.
- Equally as important is to check the reputation of the company. One simple way to do this is to ask for a list of referrals from the broker. In addition, obtain this information if possible:
 - Are life settlements a core competency?
 - Is detailed information about the company available?
 - Are the senior executives of the company recognized as leaders in the industry?
 - Does the company have an anti-fraud policy?

Reputable brokers conduct business with providers who are doing business with A.M. Best-Rated Issuers. Receiving an Issuer Credit Rating (ICR) from A.M. Best is a rigorous process and has applied high standards to the life settlement industry.¹⁶

In Conclusion

Last but not least, it is important to choose a life settlement broker who shows a steadfast commitment to doing what is best for your client. A good broker will diligently seek out and negotiate the highest offer. A broker who has direct contracts with many funding companies has a much better opportunity to obtain the best offer. Due diligence on your part includes asking how many funding companies the broker has a direct contract with and how many of those will be used in the process of obtaining an offer.

The U.S. Census Bureau estimates there will be 50 million people age 65 or older by 2010. That is 15 percent of the population. A significant number will be able to benefit from life settlements. As financial planning professionals, it is our responsibility to make sure that this solution is considered and explored to determine if it is in the best interest of our clients.

ENDNOTES

¹ *Betting on Death*, www.ConsumerReports.org, Feb. 2001.

² *Modernizing the Insurance Regulatory Struc-*

ture: The NAIC Framework for a National System of State-Based Regulation, www.naic.org.

³ *State By State*, Viatical and Life Settlement Association of America, <http://viatical.org/States>.

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⁶ David Port, *Settling for More*, SENIOR MARKET ADVISOR, Feb. 2005, 89-102.

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¹⁶ *Supra* note 4.

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House of Representatives
COMMONWEALTH OF PENNSYLVANIA
HARRISBURG

E-mail: rgodshal@pahousegop.com

Indiana State Representative Michael Ripley
Chairman
Life Insurance and Financial Planning Committee
National Conference of Insurance Legislators
385 Jordan Road
Troy, New York 12180

Dear Representative Ripley:

We are members of the NCOIL Life Settlement Subcommittee, appointed in November 2006 to fulfill a 2007 charge of the full Life Insurance and Financial Planning Committee: "to work on developing an appropriate policy position regarding life settlements, and continue to monitor, investigate, and report on issues related to the life settlement market, insurable interest laws, and investor-initiated life insurance."

Since that time we have participated in several conference calls to discuss and work on this task. We felt it critical to report on our activities and to respectfully submit recommendations regarding investor-initiated life insurance, or stranger-originated life insurance (STOLI) in response to our charge.

We reviewed the proposal under consideration at the NAIC and believe it is not the appropriate model to follow because it is contrary to NCOIL's stated policy goals and does not correct the primary problems associated with STOLI. The NAIC Proposal's five year ban on life settlements from policy inception and ban on so-called non-recourse premium financing, while well-intentioned, ultimately fall short of our two core goals, which are preventing investors from manufacturing life insurance policies and ensuring that we do not "impair, or interfere with Life Settlements or Viatical Settlements." Since the NAIC Proposal only focuses on the potential subsequent transfer of ownership in a life insurance policy, it does not correct the problem of investors taking an interest in a life insurance policy from policy inception – while inadvertently attacking policyowners' right of lawful and proper assignment in an attempt to discourage investors from investing in problem STOLI schemes.

In addition to our substantive concerns about the NAIC Proposal, the members of both this Committee and the Subcommittee have voiced our belief that NCOIL should provide independent leadership on this issue. As legislators, we apply a different perspective than regulators, allowing us to serve an oversight function that the NAIC cannot. We were the first to identify and address this problem, in NCOIL's resolution on this topic dated March, 2005, and we traditionally in the states exercise oversight over the regulatory function both by passing laws and evaluating whether they are being enforced.

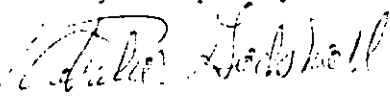
The problem of strangers attempting to initiate life insurance on strangers is not new. The case books are full of discussion which makes clear that the insurable interest laws have been used for centuries to combat inventive stranger origination of life insurance schemes. The laws established over the years – such as insurable interest laws, anti-inducement laws and life settlement laws – are essential tools to combat STOLI. The strength of these laws are a primary reason that state legislatures refused many attempts last year to impair the established property rights and value of life insurance in combating STOLI. In line with this history, we should seek enforcement of the existing laws passed by state legislatures to combat STOLI schemes before considering broad bans on commerce which eviscerate life insurance consumers' existing rights in their property.

We, therefore, advocate that the Life Insurance and Financial Planning Committee take the following actions:

- **Pass a resolution urging state departments of insurance to promote enforcement of exiting insurance laws that combat STOLI.** A few State Insurance Departments have already issued opinions and bulletins that use existing state laws to give guidance to insurers on how to detect and prevent various STOLI schemes, but most have failed to act despite their jurisdiction. Regulators have the primary responsibility for addressing this problem through executive action before asking legislators for a panacea solution.
- **Update the insurable interest and life settlement laws with model language tailored to the existing laws which adds specific reference to premium finance schemes whereby an investor takes most of the death benefit at policy inception, makes an arrangement to purchase the policy, or pays an inducement to the consumer to take out the policy.** This would reinforce to regulators their obligation to use the tools in the code to attack STOLI.
- **Adopt consumer disclosures for premium financing.** Since many of today's STOLI schemes are disguised as premium financing, all premium financing programs which use the policy as collateral should be required to disclose risks associated with premium financing, which will serve to empower consumers to avoid the STOLI schemes by exposing the insidious marketing techniques under which such loans are marketed as "free insurance."
- **Authorize life insurers to require an applicant for new life insurance to certify that she or he is not participating in a STOLI scheme.** This will not only help consumers avoid such schemes, it will be a powerful tool for insurers to detect STOLI schemes and, therefore, allow them to not issue the policy.

NCOIL has been the leader to date and must continue to provide needed guidance and direction on the STOLI matter. As members of the subcommittee we respectfully submit our report and these recommendations. We believe that, if the action of the full Life Insurance and Financial Planning Committee follows our suggestions, NCOIL will have stayed true to our stated goals and struck the proper balance on behalf of consumers.

Sincerely and respectfully submitted,



Robert W. Godshall
State Representative
53rd District

RWG



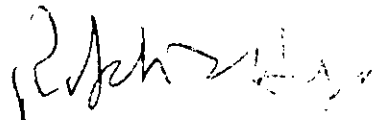
GEORGE KEISER
STATE REPRESENTATIVE
NORTH DAKOTA



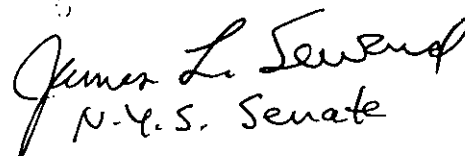
TEXAS House of Representatives



RONALD CRIMM
KY HOUSE OF REPRESENTATIVES



Ralph T. Rodgers
State Senator
Oregon 47A



N.Y.S. Senate

A

SB 2268: RESPONSES AND CLARIFICATIONS TO ARGUMENTS

"The beauty of the regulators' initiative is that it targets only the contrived arrangements where life insurance is taken out to benefit investors and the strangers with no insurable interest. However, if the insured or someone with insurable interest rather than stranger investors – take out the policy by putting up their own money or collateral, the regulators' proposal would impose no new restrictions on the ability to resell the policy in the secondary market." – ACLI (companies), AALU (insurance underwriters), NAIFA (insurance and annuity agents) and NAILBA (brokers)

The ACLI, NDAIFA, AALU and the NDBA are aligned with Insurance Commissioner, Jim Poolman, in regulating the practice of Stranger Originated Life Insurance (STOLI) to protect North Dakota consumers.

Argument: "The NAIC failed to adopt the model at the recent meeting in New York City."

Response: The NAIC did not fail to adopt the model. Commissioner Poolman is allowing due process related to the OCC suggested amendments. The bill will be sent back to the Life and Annuities Committee for the sole purpose of considering the amendments, not to reconsider the entire model. These amendments were discussed and adopted by the North Dakota Senate before the full Senate passed the bill unanimously.

Argument: "The NAIC did not allow sufficient time for the model to be discussed."

Response: The model, which is based on significant existing viatical statutes, has been discussed for almost a year in the NAIC Life and Annuities Committee. Numerous meetings, teleconferences and hearings were held involving industry, regulators, consumers and federal officials where written and oral comments were received and considered. In the end, the draft model was fully vetted and received unanimous approval from the committee.

Argument: "Since you don't hear talk about this issue at the gas station pump or at church, it's not a serious problem in North Dakota."

Response: It is the purpose and intention of the ND Insurance Department to preempt consumer injury in our state that is occurring elsewhere in the country. There are many cases of fraud, criminal intent and lost economic gain in this fast growing, relatively unregulated industry.

Argument: "We don't deal with STOLI transactions."

Response: The life settlement companies claim that they do not perform STOLI transactions. Nevertheless, we know they exist and to protect the integrity of the social benefits of life insurance it is imperative that these STOLI transactions be stopped. If life settlement companies don't deal in STOLI transactions, then they should support this bill.

Argument: "This five year moratorium will also restrict traditional life settlements."

Response: This could not be further from the truth! Life insurance initiated with the intent of protecting the policyowner's assets and family members is typically purchased for planning needs to span from 5 and 50 years. The proposal to extend the moratorium on settlement from 2 to 5 years would have no effect on policies that are purchased with policyholders assets.

Extending the moratorium is carefully and narrowly designed to target only those policies procured solely for settlement to a third party investor and financed with non-recourse premium finance loans. Moreover;

consumers that have specific needs due to terminal illness, disability, death of a spouse, etc. are still allowed to viaticate their policies.

Argument: "The five year moratorium violates the property rights of the consumer."

Response: Property rights are a little different with life insurance than with other types of property because it creates a large amount of money on the death of a person. In these transactions the insured-seller has no investment interest in the contract (except for a likely capital gains tax liability upon settlement) and therefore no property rights. Furthermore, STOLI policies obtained through fraud or with no legitimate insurable interest have no property rights.

The property rights associated with an insurance policy must be balanced with the fundamental principle of insurable interest which protects the insured, the policy owner, and the policy's beneficiaries. This longstanding public policy insists that the person who initiates the policy has an economic interest in the longevity of the insured and not in the insured's early demise. The intent of the purchase of insurance must be based on what the policyholder stands to lose by the insured's death, NOT on what the policyholder will gain through settlement of the policy.

With a STOLI transaction, the intent is not to provide a death benefit for a beneficiary with insurable interest, but rather a financial gain for investors. This makes the transaction an illegal purchase and therefore, the policyholder has no property rights.

Argument: "Regulation should be focused on the initiation of the purchase of the policy."

Response: The life settlement industry is pushing for focusing reform at the initiation of the policy. Regulation at the purchase is impossible because the carrier cannot discern intent to re-sell via the application process.

Argument: "Spitzer's law suit proves that current law is enough to deal with the bad apples in the industry."

Response: The North American Securities Administrators Association has a top ten list of the most prevalent types of investment fraud and illegal viatical settlements rank as number six. Current law is not adequate to effectively curb this growing abuse of life insurance. More specific law will provide more specific enforcement. The disclosure requirements, advertising requirements, and prohibited practices that are in the bill provide for necessary consumer protection and give the policyholder selling power in working with life settlement companies.

Argument: "Wait for NCOIL's model before taking action."

Response: Rather than being premature to act, at this juncture it is risky to procrastinate. The life settlement industry is growing at the extraordinary rate of 70% annually since 1998 to \$13 billion in 2005. By the next legislative session in 2009 the life settlement market is expected to escalate to more than \$160 billion. Without immediate regulatory action the rate of fraud associated with the industry is sure to grow at least as fast. The insurance industry is regulated on a state basis and the life settlement industry must deal with 51 different sets of regulations and commissioners. Protecting North Dakota consumers and discouraging fraudulent practices is our mission. (Source, Bernstein Research Company)

Argument: "We agree that regulation is good, but we prefer a narrowly tailored solution rather than this overly broad application approach of a five year moratorium."

Response: The long standing two year contestability period was established to protect insurable interest laws. The reason brokers target seniors over 65 years old with a life expectancy between 2 and 12 years is because

odds are most insureds will live beyond the two year period. If the insured dies during the first two years STOLI investors lose their bet and the death benefit goes to the beneficiary. Once the two-year period has passed, it is in the best interest of the settlement company if the insured dies sooner rather than later. This is contrary to the original intent of life insurance and insurable interest laws.

Argument: "The OCC is against the bill."

Response: The OCC is not opposed to the bill. The amendments proposed nationally are virtually the same as those of the North Dakota Bankers Associations that have been adopted by the North Dakota Senate. The banking insurance professionals organizations are also satisfied with the OCC amendments.

Argument: The bonding requirements are too onerous."

Response: The intent of this section is to require only one \$ 250,000 surety bond that could be acted upon for recovery by any state in which the viatical settlement broker or provider is licensed. If an amendment is needed to clarify this section, the Department would be pleased to draft it.

Argument: "The IRS will never change the manner in which it treats the taxability of the buildup of value or death benefits."

Response The North Dakota Insurance Department does not presume to know what the Internal Revenue Service will do with regards to taxing life insurance value buildup or death benefits. What we do know, is that if these transactions persist and are treated more like investments than their original purpose – insurance – the IRS is likely to look at them more closely. This would negatively impact consumers and businesses that rely on life insurance for their financial and retirement security.

"Life insurance is not – and never was – intended to be used as just another investment vehicle by investors and speculators with no relationship to the insured. The more life insurance resembles other invest-type products, the greater the chance that regulators and legislators will argue that it should be treated just like other investment products." – Advisor Today

Argument: "We give them a better deal than lapsing a policy or receiving a cash surrender."

Response: Unfortunately, most companies initiating STOLI transactions do not provide all offers to viators. They are not necessarily getting the highest value for their policy. The bill would force settlement companies to reveal ALL offers.

While it is true that a policy owner can receive more by settling the policy than surrendering it, there is currently no way for the policyholder to determine if that amount is fair and represents the true value of the policy.

The purpose of life insurance is to provide long-term financial protection for families. As NCOIL recently stated in a resolution adopted by their Executive Committee "Life Insurance policies should not be turned into commodities to be used as investment vehicles by entities that have no relationship to the insured. If we allow companies to alter this intent it has detrimental consequences on those of us that still desire to purchase affordable life insurance."

Allowing these types of transactions will increase the cost of traditional life insurance and cause the nation to have even more under-insured households.

Terminology

NAIC Drafting Note: In implementing this model act, states may elect to use terminology referring to life settlements rather than viatical settlements.

Advertising

Refer to Insurance Advertising

26.1-33-02. Solicitation of life insurance regulated by rule of the commissioner. Insurers shall deliver to purchasers of life insurance information which will improve the purchaser's ability to select the most appropriate plan of life insurance for the purchaser's needs, which will improve the purchaser's understanding of the basic features of the policy which has been purchased or which is under consideration, and which will improve the ability of the purchaser to evaluate the relative costs of similar plans of life insurance. The commissioner may adopt reasonable rules to implement this section.

Examination

Pursuant to 26.1-03-19.1, the Commissioner shall have authority to conduct examinations of the Market Conduct of any person engaged in the business of Viatical Settlements, as if that person were engaged in the business of insurance, in accord with 26.1-03-19.1, of the North Dakota Century Code.

To: State Directors
Date: 19 February 2007
From: Michael Lovendusky
Subject: VSMA Amendment Five Year Settlement Prohibition Simplified

The following is a short explanation of the NAIC VSMA Amendment five-year settlement prohibition.

Perpetrators of Stranger Originated Life Insurance (STOLI) target affluent senior citizens. The nature of STOLI is that its perpetrators react to circumvent all attempts at regulation. Hence any effort to simply regulate STOLI by directly defining and then banning it will fail. Hence the NAIC VSMA Amendment is structured to:

- Define every relevant transaction as a "viatical settlement contract".
- Exclude from the definition all traditional insurance transactions.
- Exclude from the definition all traditional premium financing transactions based on cash value plus loan costs.
- The result is that only settlement transactions including financings based on death benefit values remain covered by the definition of "viatical settlement contract".

The Amendment then prohibits settlements of such contracts for five years but provides consumer property protection reflecting public policy determinations by permitting certain *any time* settlements. These include exceptions for:

- Chronic or terminal illness (genuine viaticals);
- Death of the spouse;
- Divorce;
- Retirement;
- Physical or mental disability; or
- Personal insolvency.

Then the Amendment goes further to protect consumer interests -- including even non-recourse financing of premium -- by barring settlement of a policy for only two years if:

1. The policy owner posts some cash or collateral for a loan against the policy or limits the loan to the net cash surrender value of the policy; and
2. There is no agreement evidencing intent to settle the policy prior to two years from policy issuance; and
3. There has been no evaluation of the insured or the policy for settlement prior to two years from policy issuance.

What is left to be prohibited for five years? The answer is: only stranger-originated transactions. All "natural" settlements are protected by one or more of the exceptions, some permitting "any time" settlement and the others permitting settlement after two years. But even the five-year settlement prohibition might not stop all abusive transactions. ACLI believes the economic implications that follow from the Amendment's operation become the effective deterrent to investment speculation. That is, the targets of STOLI perpetrators are affluent seniors. STOLI perpetrators demonstrate a willingness to wait two years to capture the death benefit; that is, investors are willing to risk capital for two years before realizing a return. In other words, investors are willing to bet on a 75-year-old for two years. The odds that the 75 year old will live to 80 is too long for investors. Investors need a quicker return, especially when their "asset" may transform into a genuine insurance policy as a result of mortality, thus denying them any return beyond their investment plus reasonable interest.

1 assistance should be sought from a professional tax advisor.

2 d. Proceeds of the viatical settlement could be subject to the claims of
3 creditors.

4 e. Receipt of the proceeds of a viatical settlement may adversely affect the
5 viator's eligibility for medicaid or other government benefits or
6 entitlements, and advice should be obtained from the appropriate
7 government agencies.

8 f. The viator has the right to rescind a viatical settlement contract before the
9 earlier of sixty calendar days after the date upon which the viatical
10 settlement contract is executed by all parties or thirty calendar days after
11 the viatical settlement proceeds have been paid delivered to the escrow
12 agent by or on behalf of the settlement provider, viator, as provided in
13 subsection 6 of section 26.1-33.3-09. Rescission, if exercised by the
14 viator, is effective only if both notice of the rescission is given, and the
15 viator repays all proceeds and any premiums, loans and loan interest paid
16 on account of the viatical settlement provider within the rescission period.
17 If the insured dies during the rescission period, the viatical settlement
18 contract shall be deemed to have been rescinded, subject to repayment
19 by the viator or the viator's estate of all viatical settlement proceeds and
20 any premiums, loans, and loan interest the viatical settlement within sixty
21 days of the insured's death.

22 g. Funds will be sent to the viator by the later of the expiration of the
23 recission period, or within three business days after the viatical
24 settlement provider has received the insurer or group administrator's
25 written acknowledgment that ownership of the policy or interest in the
26 certificate has been transferred and the beneficiary has been designated.

27 h. Entering into a viatical settlement contract may cause other rights or
28 benefits, including conversion rights and waiver of premium benefits that

1 section 26.1-33.3-10 and section 26.2-33.3-15.

2 e. Prior to or at the time of execution of the viatical settlement contract, the
3 viatical settlement provider shall obtain a witnessed document in which
4 the viator consents to the viatical settlement contract, represents that the
5 viator has a full and complete understanding of the viatical settlement
6 contract, that the viator has a full and complete understanding of the
7 benefits of the life insurance policy, acknowledges that the viator is
8 entering into the viatical settlement contract freely and voluntarily and, for
9 persons with a terminal or chronic illness or condition, acknowledges that
10 the insured has a terminal or chronic illness and that the terminal or
11 chronic illness or condition was diagnosed after the life insurance policy
12 was issued.

13 f. If a viatical settlement broker performs any of these activities required of
14 the viatical settlement provider, the provider is deemed to have fulfilled
15 the requirements of this section.

16 2. All medical information solicited or obtained by any licensee shall be subject to
17 the applicable provisions of state law relating to confidentiality of medical
18 information.

19 3. All viatical settlement contracts entered into in this state shall provide the viator
20 with an absolute right to rescind the contract before the earlier of sixty-calendar
21 days after the date upon which the viatical settlement contract is executed by all
22 parties or thirty calendar days after the viatical settlement proceeds have been
23 sent to the escrow agent by or on behalf of the viatical settlement provider viator,
24 as provided in subdivision 6 of section 26.1-33.3-09. Rescission by the viator
25 may be conditioned upon the viator both giving notice and repaying to the viatical
26 settlement provider within the rescission period all proceeds of the settlement
27 and any premiums, loans, and loan interest paid by or on behalf of the viatical
28 settlement provider in connection with or as a consequence of the viatical

1 settlement. If the insured dies during the rescission period, the viatical settlement
2 contract shall be deemed to have been rescinded, subject to repayment to the
3 viatical settlement provider or purchaser of all viatical settlement proceeds, and
4 any premiums, loans, and loan interest that have been paid by the viatical
5 settlement provider or purchaser, which shall be paid within sixty calendar days
6 of the death of the insured. In the event of any rescission if the viatical settlement
7 provider has paid commissions or other compensation to a viatical settlement
8 broker in connection with the rescinded transaction, the viatical settlement broker
9 shall refund all such commissions and compensation to the viatical settlement
10 provider within five business days following receipt of written demand from the
11 viatical settlement provider, which demand shall be accompanied by either the
12 viator's notice of rescission if rescinded at the election of the viator, or notice of
13 the death of the insured if rescinded by reason of the death of the insured within
14 the applicable rescission period.

- 15 4. The viatical settlement provider shall instruct the viator to send the executed
16 documents required to effect the change in ownership, assignment, or change in
17 beneficiary directly to the independent escrow agent. Within three business days
18 after the date the escrow agent receives the document, or from the date the
19 viatical settlement provider receives the documents, if the viator erroneously
20 provides the documents directly to the provider, the provider shall pay or transfer
21 the proceeds of the viatical settlement into an escrow or trust account maintained
22 in a state or federally chartered financial institution whose deposits are insured
23 by the federal deposit insurance corporation. Upon payment of the settlement
24 proceeds into the escrow account, the escrow agent shall deliver the original
25 change in ownership, assignment, or change in beneficiary forms to the viatical
26 settlement provider or related provider trust or other designated representative of
27 the viatical settlement provider. Upon the later to occur of the expiration of the
28 any then remaining rescission period or the escrow agent's receipt of the

1 acknowledgment of the properly completed transfer of ownership, assignment, or
2 designation of beneficiary from the insurance company, the escrow agent shall
3 pay the settlement proceeds to the viator. The viator may waive any then
4 remaining rescission period rights in a separate written waiver provided to the
5 escrow agent.

6 5. Failure to tender consideration to the viator for the viatical settlement contract
7 within the time set forth in the disclosure pursuant to subdivision g of subsection
8 1 of section 26.1-33.3-07 renders the viatical settlement contract voidable by the
9 viator for lack of consideration until the time consideration is tendered to and
10 accepted by the viator. Funds shall be deemed sent by a viatical settlement
11 provider to a viator as of the date that the escrow agent either releases funds for
12 wire transfer to the viator or places a check for delivery to the viator via United
13 States postal service or other nationally recognized delivery service.

14 6. Contacts with the insured for the purpose of determining the health status of the
15 insured by the viatical settlement provider or viatical settlement broker after the
16 viatical settlement has occurred shall only be made by the viatical settlement
17 provider or broker licensed in this state or its authorized representatives and shall
18 be limited to once every three months for insureds with a life expectancy of more
19 than one year, and to no more than once per month for insureds with a life
20 expectancy of one year or less. The provider or broker shall explain the
21 procedure for these contacts at the time the viatical settlement contract is
22 entered into. The limitations set forth in this subsection shall not apply to any
23 contacts with an insured for reasons other than determining the insured's health
24 status. Viatical settlement providers and viatical settlement brokers shall be
25 responsible for the actions of their authorized representatives.

26 **26.1-33.3-10. Prohibited practices.**

27 1. It is in violation of this chapter for any person to enter into a viatical settlement
28 contract at any time prior to the application for or issuance of a policy which is the

RE: SB 2268

3-19-07

Dear Chairman Keiser, Vice Chair Johnson
and members of the committee:

I received a call last week from a phone bank in NYC
and was being enticed to search for and sell life
settlements and STOLI, although they called it an
institutional settlement.

I was told the following:

I would need no license or contract
Agents are easily making 500,000/yr on
settlement business only.

New sales commissions were also possible by
settling a policy and reselling another.

I could negotiate my compensation (which
would be to the detriment of the consumer)

I should look for clients in older ages
(they will die sooner.)

My involvement is to protect my clients and
future consumers of insurance in ND from
the above tactics, all of which I believe are
unethical uses for the core value of life insurance
I support SB 2268 as amended by the Ins. Dept.

Glenn Trembling (29 yr agnt in Fargo)
C 701-238-6660