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Preparing for the Year 2000, or Y2K, technology problem is a top priority for the electric utility industry. This booklet is designed to provide the reader with an overview of basic facts concerning Y2K and electric utilities' readiness. It is published by the Edison Electric Institute, the association of U.S. shareholder-owned electric utilities, industry affiliates and associates worldwide. EEI's member companies serve about 70 percent of all ultimate electricity customers in the United States. EEI can be contacted at (202) 508-5000, or visit our web site at www.eei.org.

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WHAT IS Y2K?

The Year 2000, or Y2K, refers to a problem in computer software and embedded hardware systems. When the first computer programs were written in the 1960s and 1970s, they were not designed to recognize the year 2000. Instead of representing years as four digits — 1991, for example — years were programmed to appear in computer code as two digits (i.e., 91) to save memory. The “19” is understood.

As a result, on January 1, 2000, millions of computers and chip-based technologies around the world may read “00” as “1900.” Those computer programs that rely on sequential date information may be unable to process the date change from December 31, 1999, to January 1, 2000. And they may not work properly or may shut down entirely.

WILL Y2K AFFECT ME?

The issue could affect all of us.

Virtually every public and private entity around the world that uses computers, computerized systems or devices with electronic chips in them may be vulnerable to the Y2K problem. Without preventive actions now, the Y2K glitch could cause significant incapacities in essential systems, including financial markets, government databases, national security and defense systems, and the electric power grid. However, the actual scope of the problem is still under investigation, and may not be as large or difficult to remedy as some fear.

**WILL Y2K AFFECT
MY ELECTRIC SERVICE
ON JANUARY 1, 2000?**

Electric companies are working aggressively to resolve Y2K issues before the new millennium to ensure that any remaining problems on New Year's Day 2000 will be minor and quickly resolved.

Fortunately, January 1, 2000, falls on a holiday weekend¹ and electricity demand is typically lower on the weekend. The industry, therefore, expects and plans to have excess generating capacity available during the date change to help deal with any problems. While no broad guarantee about service can ever be given, the industry does not expect the Y2K problem to affect the entire electric system infrastructure.

¹ The U.S. federal government will be closed in observance of the New Year's holiday on Friday, December 31, 1999.

HOW WILL Y2K AFFECT ELECTRIC UTILITIES?

Within the electric utility industry, there are hundreds of thousands of computers and software programs that may have Y2K problems. There are also millions of individual computer chips within critical equipment that are not easily seen or accessible, but may be affected by Y2K. These are known as "embedded chips," which are used in digital controls.

Electric systems, however, consist mainly of wires and metal devices. And the majority of equipment is electromechanical, meaning there are no digital controls. In general, electric generation systems are most vulnerable to Y2K, while transmission and, especially, distribution systems are less automated and less subject to failure.

Electric utilities do use computer technology for voice and data communications, as well as for:

- monitoring and controlling power systems;
- managing purchasing operations, accounting functions, and customer billing and service; and
- providing for common services such as telephones, security systems, and building elevators.

However, many of those operations that do rely on computer systems can be manually operated in emergencies — and often are during power outages arising from storms or mechanical problems.

Y2K is a very complex issue, and its likely effects are unknown at this time. The challenge for electric companies lies in identifying which systems are in fact likely to be affected — and then fixing those components which may be Y2K deficient.

WHAT STEPS ARE ELECTRIC UTILITIES TAKING TO PREPARE FOR Y2K?

The electric utility industry is an industry that operates 24 hours a day, 7 days a week. It is accustomed to planning and responding to emergencies and other unexpected events. At any given time, unforeseen factors such as inclement weather, natural disasters, accidents, or equipment failures could affect the generation, transmission and distribution of electricity. That's why electric companies traditionally establish and rely on contingency plans. These existing plans are being revised to take into account potential Y2K problems.

While Y2K is a unique occurrence, electric utilities have been planning for the Y2K transition since the early 1990s. Getting ready for Y2K involves at least three steps:

- **Inventory**—The first process is to identify all systems, software and equipment with computer chips.

- **Assessment**—Companies then must determine which of those chips and programs may be Y2K sensitive and test those systems.
- **Remediation**—Finally, companies must replace and repair chips and software, or develop and implement an alternative process that works around the problem.

The electric utility industry has had years to plan for Y2K. And the industry is well on the way to identifying which computers, systems and equipment have potential Y2K problems, and assessing their vulnerability. Most electric companies will conduct testing and remediation during scheduled maintenance "down times" or outages between now and December 1999.

While electric utilities are cautiously optimistic that the impacts of Y2K on electrical systems are going to be minimal, they are preparing for operating contingencies based on assumed worst-case risks. The goal and expectation of this contingency planning is that electrical systems will be able to sustain safe and reliable operations during the critical Y2K transition periods despite any problems.

**WILL THE ELECTRIC INDUSTRY
BE READY FOR Y2K?**

While no broad guarantee can ever be given, the industry is cautiously optimistic that the Y2K problem will be addressed in time.

The electric power system is very large and diverse. In fact, there are 3,200 entities in the North American electric supply and delivery industry, of which about 200 can be considered operators of electric generation and transmission systems. Due to the high degree of interdependence of electric systems, every electric utility that has a direct reliability impact on North American electrical interconnections, even if it does not own digital equipment, must address the Y2K problem in a coordinated manner.

Today, electric utilities and their respective trade association partners are collaborating with each other and with other industries to ensure that the electric power system remains safe and reliable during the Y2K transition. Despite these coordination efforts, significant additional work remains to be done. Meeting the Y2K challenge will require a team effort from utilities both large and small, as well as from their customers and suppliers.

**WHAT IS THE NORTH AMERICAN ELECTRIC
RELIABILITY COUNCIL (NERC)?
WHAT DOES THE COUNCIL SAY ABOUT
ELECTRIC UTILITIES' Y2K READINESS?**

The North American Electric Reliability Council (NERC) is a voluntary, non-profit organization formed in 1968 to coordinate the reliability and adequacy of bulk electric systems in North America. NERC consists of ten Regional Reliability Councils spanning the United States, Canada, and a portion of Mexico. For thirty years, NERC has played a leadership role in making the North American electric system the most dependable electric supply system in the world.

At the request of the U.S. Department of Energy (DOE), NERC has taken the lead in preparing the electricity sector for Y2K and reporting on the industry's progress. NERC presented its first comprehensive assessment of electric utilities' Y2K readiness to DOE on September 17, 1998.

The NERC report looks at all segments of the electric utility industry — investor-owned utilities, electric cooperatives, municipal utilities, other public power systems such as the federal power marketing administrations, and independent power producers. The report concludes,

"The impacts of Y2K on electrical systems appear to be less than first anticipated. With continued work toward finding and fixing components that may be Y2K deficient and with properly coordinated contingency planning, the operating risks presented by Y2K can be effectively mitigated to achieve reliable and sustained operation of electric systems into the Year 2000."

NERC further asserts:

"Recent reports in the news media and on the Internet regarding anticipated widespread electricity outages are unsubstantiated. In an industry that meets record peak demands during heat waves and quickly restores service to millions of customers who lose power due to a hurricane or earthquake, preparing for and dealing with operating risks is an ingrained part of the business."²

NERC will complete a second written report by January 1999, and a final assessment is due to DOE by July 1999. In addition, the Council has called for an accelerated timetable under which electric utilities will ensure that "mission critical systems and components" are Y2K ready by June 30, 1999.

² For further information on electric utilities' Y2K readiness, see *Preparing the Electric Power Systems of North America for Transition to the Year 2000: A Status Report and Work Plan*, prepared by the North American Electric Reliability Council for the United States Department of Energy, September 17, 1998. The complete report is also available on the NERC website at www.nerc.com/y2k.

HOW MUCH WILL ELECTRIC UTILITIES SPEND ON Y2K READINESS?

While a final cost estimate is not yet available, shareholder-owned electric utilities expect to spend nearly \$2 billion to address the Y2K problem. In addition to financial resources, electric companies are devoting significant personnel and technical resources to prepare for the Y2K transition. For example, one electric utility has assigned 1,400 people across various departments to full- or part-time Y2K activities.

**ARE ELECTRIC COMPANIES
WORKING WITH OTHER INDUSTRIES
TO PREPARE FOR Y2K?**

Yes.

Electric utilities rely heavily on telecommunications services, pipeline transportation of natural gas and oil supplies, and rail transportation of coal supplies. The utility industry is working with these support industries to assess their Y2K readiness and to assist them in developing contingency plans as needed. Like electric utilities, other industries are following the same three-step process: inventory systems and equipment, assess problems, and then solve any problem that is identified.

In addition to working with other industries, and with their customers, electric utilities are working closely with the Electric Power Research Institute (EPRI). EPRI has a special program devoted to identifying problems with embedded microchips and working with vendors to find solutions. The EPRI program is open to all companies, not just electric utilities.

**HOW IMPORTANT IS
INFORMATION SHARING
BETWEEN INDUSTRIES?**

Very important.

Industry cooperation and coordination will be key to meeting the Y2K challenge. And electric utilities support and encourage the full disclosure and exchange of Y2K problems, test results and remediation solutions. However, until recently, the potential for legal liability associated with such disclosure had discouraged businesses from sharing information which may be useful in addressing the problem.

Fortunately, Congress recognized the importance of information sharing, and the need to address the fear of liability for information sharing, and passed the *Year 2000 Information and Readiness Disclosure Act* (S. 2392), which provides limited protection for specific types of Y2K information sharing.

WHAT IS THE ADMINISTRATION DOING ABOUT Y2K?

In February 1998, President Clinton established the President's Council on Year 2000 Conversion. The Council is comprised of representatives from many federal agencies and is responsible for coordinating the federal government's efforts to address the Y2K problem for itself and the country as a whole. The President's Council is divided into more than thirty working groups, including aerospace, energy, finance, health care, telecommunications, and transportation. The electric utility industry is working with the Department of Energy, primarily by means of the NERC reporting process.

WHAT IS CONGRESS DOING?

The U.S. Congress is very concerned about potential Y2K problems and is taking an active role to ensure that U.S. businesses and industries are Y2K-compliant. Policy makers particularly are watching the electric utility industry's Y2K preparations very closely.


Earlier this year, the House of Representatives established a special Y2K Task Force, and the Senate created its Special Committee on the Year 2000 Technology Problem. Both have held hearings to address Y2K problems and industry readiness. Most importantly, Congress passed the bipartisan *Year 2000 Information and Readiness Disclosure Act* (S. 2392) on October 1. This bill provides limited protection for specific types of communication about Y2K information that is essential to remediation efforts. The bill does *not* provide liability protection for failures that may arise from Y2K problems, promoting company-to-company information sharing while protecting the rights of customers.



WHAT CAN I DO?

Understandably, you may be concerned about whether your electric service will be provided without interruption into the Year 2000.

The Edison Electric Institute (EEI) and NERC recommend that you think about the impacts of Y2K on your business or home and then contact your local electricity supplier to seek guidance as to what steps you should take, if any, regarding power supplies. NERC cautions that, "while most customers are not expected to need to take any action, some critical loads may require coordination of contingency plans with the local electricity supplier to provide adequate assurance of continuous supply."



Overall success of Y2K efforts in the electric industry requires cooperation between the industry, government agencies and customers. It is critical that utilities and customers communicate with each other about their Y2K plans and programs. For instance, severe disruptions could result if too many customers suddenly stop using power, without notifying their local utility, and turn off equipment at 11:50 p.m. on December 31, 1999, and then turn it on again at 12:10 a.m. on January 1, 2000.

**WHERE CAN I GET
MORE INFORMATION?**

To learn more about how electric utilities are preparing for the Year 2000, contact the Edison Electric Institute at (202) 508-5000 or visit our web site at www.eei.org/y2k. Or contact your local electric utility. Other useful Y2K web sites include the President's Council on the Year 2000 Conversion at www.y2k.gov; and the North American Electric Reliability Council (NERC) at www.nerc.com/y2k.

GLOSSARY

Assessment: to prepare for Y2K, companies must determine which systems, software and equipment with computer chips may be Y2K sensitive and test those systems.

Embedded chips: millions of individual computer chips used in digital controls that are not easily seen or accessible, but may be affected by Y2K.

Inventory: to prepare for Y2K, companies first must identify all systems, software and equipment with computer chips.

Millennium bug: a term often used to describe Y2K.

Remediation: to prepare for Y2K, companies must replace and repair computer chips and software, or develop and implement an alternative process that works around the problem.

Year 2000 or Y2K: refers to a potential problem in computer software and embedded hardware systems which, without preventive actions now, could cause significant incapacities in essential systems.

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January 11, 1999

Electric Utilities Promise Y2K Preparedness

Filed at 8:10 p.m. EST

By Mary Mosquera for TechWeb, CMPnet

WASHINGTON, D.C. -- The lights will stay on Jan. 1, 2000, because the millennium date change will have little impact on electric-power systems in North America, an industry group said Monday.

Electric utilities throughout the United States, Canada, and parts of northern Mexico have already tested about half of their critical systems. The results show some nuisance errors exist, like incorrect dates, but they will not affect the delivery of power, according to the North American Electric Reliability Council (NERC).

NERC, an industry organization that sets operating and engineering standards for interconnecting electric systems, is coordinating Y2K compliance information for the 3,200 providers of electricity in the region.

"There is no evidence at this time that the Y2K problem will create national failures in electric-power service," said John Koskinen, chair of the President's Council on Year 2000 Conversion.

The year 2000 bug is expected to cause computers to make errors or shut down completely at midnight on Jan. 1, 2000, because they will read two-digit "00" date fields as 1900 instead of 2000.

Just six months ago, Sen. Bob Bennett (R-Utah), chairman of the Special Senate Committee on the Year 2000 Technology Problem, criticized the utility companies' lack of information and preparedness.

But in the final three months of 1998, almost 100 percent of U.S. and Canadian electrical systems were participating in the Y2K readiness program. Testing is scheduled to be completed by May 31, and NERC is

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hoping for system readiness by June 30.

Utilities will test their systems during regularly scheduled shutdowns in the spring when demand for power subsides. "I applaud industry's intention to apply 'peer pressure' to advance the programs of those who may be falling behind," said Energy Secretary Bill Richardson.

Although it plans to be prepared for 2000, the utilities industry is preparing contingency plans for its use of gas, oil, and coal, said Jerry Cauley, NERC's Y2K program manager. "Distribution is the least digital part of electricity -- they are just lines running down the street," he said.

The utilities will conduct two drills in April and September. On April 9, the electric industry will test its systems in conjunction with telecommunications carriers and evaluate if back-up radios and satellite communications can compensate for glitches in voice and data flows.

Sept. 8 to Sept. 9, the utilities will run a drill to determine whether their computer systems can withstand the 9/9/99 date, which can, in some instances, tell a computer to shut down. "The Sept. 8 to Sept. 9 rollover will be a rehearsal for the Dec. 31 to Jan. 1, 2000 rollover," Cauley said.

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Anchorage Water and Wastewater Utility's Year 2000 Remediation Project

Anchorage Water and Wastewater Utility has taken the Y2K threat very seriously and implemented a project to prevent computer collapses and interruptions.

By Larry W. Brys

Anchorage is a mid-size, modern city with approximately 250,000 residents and a climate comparable to upper Michigan, Wisconsin, and Minnesota. Since Anchorage's geographic location precludes the opportunity to participate in regional water and wastewater systems that could provide redundancy for backup, the Anchorage Water and Wastewater Utility (AWWU) is a stand-alone enterprise that must be able to provide consistent and uninterrupted service to its customers without external assistance. The Anchorage Water and Wastewater Utility serves approximately 50,000 accounts consisting of single and multiple family dwellings, businesses, industrial, and military customers.

The Y2K Problem

The Year 2000 (Y2K) computer glitch is a date problem. It can cause a computer to mistake the year 2000 for 1900. This is probably the most pervasive problem but not the only problem and possibly not the most serious. Some computers may incorrectly determine that the year 2000 is not a leap year thereby causing additional problems. Furthermore, certain programming conventions may lead to problems around the turn of the century.

These are all real problems with a dramatic scope. The date rollover presents an impossible situation for many computers. If the computer's operating system does not intercept the problem and terminate the offending program, the whole computer will shut down. The computer could be a microprocessor in a piece of equipment that the owner never suspected was computerized. Indeed, the problem ranges far beyond what are traditionally thought of as "computers."

AWWU's Y2K Project

AWWU's Y2K project formally began in 1996, but programmers had known of the issue for some time. The project began by evaluating systems for Y2K compliance. It was determined that older systems were not compliant, while those developed recently were compliant. Even though AWWU originally planned to hire consultants to develop the Y2K plan, it became clear that internal resources could better and more economically develop this plan. AWWU is currently using a combination of outside consultants and internal resources to implement the plan. In 1997, AWWU inventoried its computer systems and began the final Y2K readiness assessment and remediation project.

There has been an obvious evolution of thinking regarding the Y2K problem. Initially it seemed like a simple, although extremely large problem. As industry understanding of the problem evolved, it turned out to be anything but simple. It now appears that even the industry's pessimists underestimated the *pervasiveness* of the problem.

As remediation of the problems discovered in the 1997 assessment neared completion, problems subsequently identified are still being addressed. These include issues such as problems with microprocessors in equipment that was not known to be computerized and dealing with failure of business partners, some who may have failed to adequately address their problems. As AWWU moves into 1999, its Year 2000 program is on track and ahead of schedule.

The Y2K Compliance Strategy

Strategy Development. Formulating a Y2K strategy for AWWU was not an easy

task. An information systems professional might hope to be able to rely on industry publications and the mass of information available on the Internet for insight. It seems the Y2K problem has brought out the technical tabloid writers en masse. The valuable information is diluted in a sea of doom prophecies, generalizations and redundant information. Everyone has something to say; most of which is very repetitive. Opinions range from "the sky is falling and not only that—it's worse, there are two layers and they will both fall," to "what's the big deal?"

It was incredibly difficult to determine which advice was credible. Moreover, no one knows what will happen on January 1, 2000. What is necessary and prudent, and what is just hype? AWWU determined that these decisions had to be made internally. These did not always align with standard industry thought, but AWWU felt a responsibility to choose internal strategies in which there was great confidence.

AWWU's Y2K program addresses the following objectives:

- finding and fixing potential problems;
- responding to evolving understanding of the Year 2000 problem;
- addressing user-developed systems - spreadsheets and PC databases;
- developing contingency options;
- testing;
- spending the correct amount; and
- developing a Year 2000 Statement.

Finding and Fixing Potential Problems. As its first line of defense, AWWU has adapted a strategy of locating and correcting Y2K problems. When the formal year 2000 effort commenced, the initial task was to inventory and evaluate its systems—itsself an evolving task. This process refined understanding the issue and the overall

strategy. AWWU went through several iterations before arriving at the final inventory and plan. In some areas, the inventory approach eventually took a backseat to a more global strategy. For example, with desktop workstations the concept of inventorying and certifying individual software products was abandoned and replaced with the development of a standard office software set to support. Ultimately, a strategy was implemented for identifying and addressing problems in each class of product.

Response to Evolving Understanding. Nationally, a tremendous amount of money is being spent on Y2K issues and problems. Much of the information obtained from these efforts has become available on the Internet, through industry periodicals, and from vendors. This has prompted a continuous evolution in thinking about the Y2K issue. As problems continue to be found in previously unsuspected places, the understanding of the year 2000 issue advances. A critical part of the AWWU's Y2K strategy is to remain abreast of the evolution of the worldwide understanding of the problem and adjust efforts accordingly. The project manager is taking the lead on monitoring Y2K information on the Internet and in periodicals.

User-Developed Programs

With the evolution of PC-based spreadsheets, databases, and many other office software products, it now seems that there are two ways to develop a system: 1) have a contractor or the IT Division develop it at a substantial cost or 2) develop it yourself for a small fraction of that cost. Even though a system developed in a few hours can have some major limitations, it allows employees to quickly develop a functional, cost justified information system. Prior to the spreadsheet and database packages, that possibility did not exist. As part of the Y2K inventory, all network storage devices were searched for unregistered spreadsheets and PC databases. Approximately 2,000 unregistered spreadsheets and 200 PC databases were found.

AWWU has taken a common-sense approach in addressing user-developed systems. What do end users do when a problem occurs in one of their spreadsheets? They either fix it or retire it. The bottom line is that the Y2K issue is not a

justification for interfering with the users' ability to build and maintain their own economical system.

AWWU's strategy for this problem is to ensure that the underlying software is at least Microsoft Office 97, that all applicable patches have been applied, and to ensure that users are aware of the Y2K problem. The strategy also includes offering the support of the Information Technology Division to those who request it. A few complex spreadsheets within the utility are considered to be critical to the utility's operation. These are considered to be enterprise information systems, not end user spreadsheets, and have been addressed individually.

Developing Contingency Options.

- AWWU does not expect to prevent or correct all Y2K problems but it does expect to find and correct or mitigate most of the problems.
- AWWU expects to prevent undetected problems from causing interruptions in the service to customers.
- AWWU expects to find a high enough percentage of the problems that the few that arise in the year 2000 can be quickly addressed. However, there is no reasonable way to guarantee that a problem will not escape detection. A hardware or software component that was certified to be Y2K compliant could fail. There is no way to fully test bugs out of computer components for which the source code is not available.
- AWWU is vulnerable to the potential mistakes of the computer equipment providers, as well as to internal human limitations.

AWWU is developing contingency plans to ensure effective operation even in the face of some Y2K-related equipment failures. This includes having extra employees on duty on January 1, 2000, inspecting remote sites, and verifying that everything is functioning correctly. *Most importantly, AWWU plans to continue to provide a safe, adequate, and uninterrupted supply of drinking water, and effectively collect and treat wastewater.*

Testing. Much of the available Y2K literature suggests that both public and private entities should be spending massive amounts of money on testing. This is another area where AWWU developed its own strategy based on proven systems analysis and testing concepts. AWWU takes an item of hardware or software, spends some money developing a test plan, and then spends some money testing it.

The product of the testing is an indication, and the indication has some degree of reliability. Simply because the testing revealed no problems, one should not conclude that there are no problems. There are some expenses and some results and AWWU needs to make sure that the results justify the expenses. And, of course, there is the possibility that the test itself will cause more damage than the Y2K problems.

Except for custom software for which AWWU possesses the source code, AWWU is relying primarily on methods other than in-house testing to assess year 2000 readiness and compliance. These are discussed elsewhere in this document.

Spending the Correct Amount

From the beginning AWWU has treated the Y2K remediation project as any other project with respect to cost/benefit justification. How much should be spent to fix a problem? Some problems are cheaper to prevent than to fix, but some are cheaper to fix than to prevent. The Y2K problem must not be a license for irresponsible spending. Cost justification has been a critical factor in the strategy development, but cost has never been allowed to override public health and safety concerns.

Developing Year 2000 Statements

Just as AWWU must be concerned about the failure of business partners, they must be concerned about AWWU's reciprocal ability to operate effectively into the Year 2000. AWWU receives inquiries from customers about year 2000 readiness. Some even demand statements certifying Year 2000 compliance. AWWU customers need to be reassured that Y2K problems are being addressed.

Organizations are growing reluctant to certify their systems to be Year 2000 compliant. A favored term now is Year 2000 Ready. This is usually defined to mean that the entity thinks it is Year 2000 compliant, but it might not be. With the help of the Municipal Attorney's Office, AWWU has developed a standard Year 2000 Statement. AWWU offers the statement in response to inquiries from customers and has posted the statement on its Web site.

Implementation

Custom Business Software. When the Y2K program began, this category was called custom software; however, it was soon discovered that that the custom software was really business software. For software developers, this is the easiest area of the Y2K issue to attack, although not necessarily the cheapest.

For the few client/server systems built in recent years with modern development tools, the task of certifying Y2K capability was delegated to the vendors. Since the software used internal database date storage formats and functions for processing dates, AWWU relied on the strategy of keeping the database software and licenses current so that it would be in a position to receive any patches that might be necessary for Y2K compliance. For the remaining systems, which were mostly COBOL-based (one FORTRAN), the decision about Y2K compliance was based exclusively on source code analysis rather than testing. It became obvious that none of the COBOL or FORTRAN systems were Y2K capable; if this software looked Y2K capable, testing would have been appropriate. However, that was not the case.

The next decision point for each system was whether to replace it or upgrade it. Luckily, almost all of the noncompliant custom software was already scheduled for replacement before the year 2000. Although this was a relief to the Year 2000 team, it added some constraints to the software replacement projects. They were now part of the year 2000 solution and could not be allowed to slip into January of the year 2000. Unfortunately, AWWU's most complex business system, the Customer Information System (CIS), was neither year 2000 compliant nor was it scheduled for replacement.

A separate project was initiated for the CIS upgrade, under the leadership of the Y2K project manager. The upgrade was treated like a new software development project. AWWU spent a month performing high level analysis, gathering metrics, modifying the database definition, and developing a detailed workplan. An interesting twist occurred in the design process. AWWU went into the project with the attitude that this is a legacy system that the utility wants to replace in the near future but could not replace it fast enough to meet the year 2000 deadline. The team agreed that the appropriate action would be to do the minimum required to produce a system that would be stable and depend-

able into the year 2000. There was unanimous agreement within the development team that the database structure would not be modified. Instead, AWWU would use a common programming technique called windowing that assumes dates are in the range 1950 through 2049 instead of assuming they are all in the 1900s. But as the process was analyzed, the thinking changed. The system has almost a thousand modules and the team concluded that it would be far easier to modify the database than to insert windowing code everywhere a date was manipulated.

Five months were spent analyzing each program and developing specifications detailing each change that this would require. Each subsystem was modified individually, each program was tested, and then the subsystem was tested. System testing is scheduled for completion by December of 1998. The project is now about six weeks ahead of schedule and costs are coming in at about 80 percent of the estimates. The upgraded system is scheduled for production after the database upgrade in the first quarter of 1999.

Telemetry and SCADA

Telemetry is the mechanism for communicating between the control or sensing equipment and the monitoring and control panels. This equipment controls and monitors the water distribution and wastewater collection and treatment systems.

The Supervisory Control and Data Acquisition (SCADA) equipment is one of the greatest areas of concern because problems could have immediate and direct effects on the service to customers. Also, the potential for disastrous results is greater than with business systems. A bug in the billing system could destroy a database and cause considerable cost by requiring reconstruction from backup tapes. However, the consequences of a pressure-regulating valve malfunctioning and causing a main water input line to burst or a chemical regulating system failure have far more serious implications.

Certain problems simply cannot be allowed to happen under any circumstances. AWWU needed a comprehensive problem abatement program, but that was not enough. AWWU adopted the position that there is no way to be sure that every Y2K problem will be detected and fixed. Additional measures were needed. The

likelihood of problems as well as the potential severity of (even unlikely) problems was reviewed.

- 1) AWWU needed to look at each class of equipment and determine the worst thing that could happen if it failed.
- 2) AWWU needed to determine how to mitigate the problems.

As AWWU worked through the above issues, it became apparent that two obvious concepts had been missed. First, the equipment can fail, and in some cases already has failed, regardless of the Y2K issue. AWWU has continued to provide consistent and uninterrupted service in spite of these failures. Secondly, wherever there is potential for catastrophic failure, it really does not matter if the failure is caused by the Y2K date problem. It is the failure that is the problem and this could happen anytime. So, to some extent, AWWU broadened its perspective to include a complete review of dependability and contingency issues surrounding the SCADA equipment. At the same time, AWWU has continued to emphasize the timing aspect of the year 2000 and the necessity of having mitigation measures and contingency plans in place by then and preferably sooner.

The SCADA area presented another challenge. The amount of equipment that could not be reliably certified as Y2K compliant exceeded the ability to replace all of it before the year 2000. This called for some creativity. For some of the equipment, reporting an incorrect date could be tolerated though it would cause inconvenience. For this equipment, AWWU will set the clocks back. Preliminary tests have been conducted and a final, comprehensive test will be conducted this winter when the system is at the lowest point on the load cycle.

All of the SCADA systems can be bypassed to allow manual operation. Some equipment is thought to be Y2K compliant, but could produce highly undesirable results if it failed. This equipment will be switched to manual operation before January 1, 2000, and then, item by item, switched back to automatic operation after January 1, 2000, and closely monitored until it has been determined that it is functioning correctly.

Network Hardware and Software

This is another area where testing turned out to take a back seat to other methods.

AWWU is dealing with equipment that can be tested much more meaningfully by the manufacturer. The strategy consists of using trusted vendors, then monitoring their Y2K efforts. AWWU is making sure that all hardware and software is certified Y2K capable by the vendor and is reasonably current (generally not over three years old as of January 1, 2000). AWWU ensures that there is a maintenance contract, reads the vendor's Y2K literature and applies any appropriate Y2K patches. Two older servers that could not be certified to the satisfaction of the AWWU are being phased out. SCADA servers are addressed in the SCADA and Telemetry plan and are not included in this equipment class.

Desktop Hardware and Software. AWWU's year 2000 strategy with office hardware and software is synonymous with the overall strategy for dependability. Although the utility does not endorse any single product it believes that diversity can have detrimental effects in the areas of training, maintenance, and document sharing when it comes to office software. There may be a number of functionally equal products but we selected the Microsoft Office package as the standard. On January 1, 2000, all of the utility's desktop operating systems will be Windows NT Workstation 4.0 or 5.x. No office software older than Office 97 will be in use on January 1, 2000. Patches will be downloaded on July 1 1999, and always kept current. In the last quarter of 1999, IT staff will make the rounds of all workstations and apply all patches.

A PC software inventory has been performed and considerable diversity of software was found. AWWU could easily spend more money evaluating the Y2K compliance of products than the products are worth to AWWU. Reducing diversity and bringing existing software and licenses up to the current levels were major parts of the Y2K strategy. AWWU's Year 2000 Project will not address Y2K compliance of products that are alternatives to the Utility's supported products. If these packages fail to operate properly because of Y2K problems, the users will need to switch to products supported by AWWU.

Commercial Off-the-shelf Software. AWWU performed an inventory of commercial off-the-shelf software, excluding office software, and found relatively few products in this category. None of them could be certified Y2K compliant to the satisfaction of the Year 2000 Project Manager. Each system has been evaluated

and strategies have been adopted for resolving Y2K problems. Resolution strategies include upgrade of license, replacement, and phasing out. For systems to be retained, the solution is to obtain a maintenance agreement that automatically keeps the software current into the Year 2000 so that, for any problems identified and solved by the vendor, the fix will automatically be applied.

Non-IT Equipment

Traditional computer systems were the original source of concern for Y2K issues. However, equipment such as lighting, heating, elevators, and telephone systems sometimes contain computer chips that are date sensitive. Y2K problems in unanticipated places are continually being brought to light. AWWU needed to inventory and assess all equipment and systems that could conceivably contain a micro-processor that works with dates, then assess the potential impacts of failure of the equipment and, where appropriate, upgrade or replace equipment that is not Y2K compliant with equipment that is. The utility's Operations and Maintenance Division has been collecting manufacturers' data to determine where problems may exist so as to get them corrected.

Business Partners

Year 2000 project managers realize that preparing their internal systems for the year 2000 is not enough. Current industry data suggests that a significant number of organizations have waited too long and will not be ready to achieve Y2K compliance in time. Some authors suggest that entities should be evaluating not only their own Y2K readiness, but also the Y2K readiness of the rest of the world. What others do (or do not do) with regards to Y2K preparedness affects everyone.

AWWU is very concerned about its business partners and is trying to pursue a rational approach for self-protection to the extent that is possible. These seem to fall into two categories. The major suppliers are the power and communication suppliers and other important suppliers such as those who supply and deliver chemicals and equipment. The major suppliers are the ones whose problems could have the most immediate and drastic effects on us. But these are the

easiest to monitor because they are local, fixed entities and several are municipally owned.

Other suppliers include a delivery chain which is probably the most impossible to assess and one of the most susceptible to failure because of the large number of small, independent shippers. AWWU's strategy has been to gradually build up the supply inventory to enable bridging some minor worldwide disruptions in the supply chain. Presumably some supply shortages will likely start to develop long before the year 2000 rolls in. This has been factored into the contingency planning as well.

Resource Availability

For the most part, the year 2000 gloom and doom—shortage of programmers and sky-hi prices—never materialized. At the end of 1998, AWWU continues to be able to secure the services of competent analysts and programmers at reasonable prices. The number of computer professionals is adequate to support the demand.

Conclusion

AWWU considers the Y2K problem to be very real and has taken it very seriously. This Y2K project manager feels that many have overstated the problem with gloom-and-doom prophecies and irrational recommendations; however, this may not be all bad. The problem is very pervasive and perhaps more organizations are underestimating than overestimating it. AWWU's Y2K team has complete support of the general manager and management team and has been provided with the resources to do the job. With the continuing effort by all, AWWU expects to be ready for January 1, 2000, and continue to function effectively into the next century. □

LARRY W. BRYE is the Anchorage Water and Wastewater Utility Year 2000 Project Manager. Questions about AWWU's Year 2000 project may be addressed to bryslw@ci.anchorage.ak.us.

BUSINESS

SUNDAY, February 7, 1999

ANCHORAGE DAILY NEWS

SECTION C

Software upgrades confusing

By JOHN J. FRIED
Knight Ridder Newspapers

After testing four programs for PC owners haunted by the Year 2000 question this year, I can only say, "Lots of luck."

By now, just about everyone knows that as a result of coding decisions made decades ago, computers and software manufactured in the 1980s and most of the 1990s handle dates by recognizing only the last two numbers of each year.

Which means that on Jan. 1, 2000, at 12:00:01 a.m., a lot of computers and not just a few programs will grow seriously distressed.

Mainframes and their programs will think it is 1900.

But personal, or desktop, computers will go one dumb step further, if they are Microsoft-dependent.

Once the PC's internal clock has decreed that it is 1900, DOS, which became the equivalent of the Ten Commandments for PCs in the early 1980s, and which rules even under the cover of Windows, will step in.

Because DOS is written with 1980 as its basis year, it will decree not that the year is 2000, not that it is 1900 but that it is 1980.

Got that?

Unfortunately, matters grow only more confusing.

If you bought a Pentium in 1997 or so, your computer's BIOS — a piece of data

The coming of the Millennium 2000 Bug

The Millennium 2000 Bug is a computer glitch that shows years in two digits instead of four. Many software programs lack the first two digits to distinguish 1900 years from 2000 years. The scare is that no one can predict if computers will know what time it is in the 20th century.

Time-sensitive applications

Affects software that runs date and time-aware systems such as elevators, nuclear reactors, thermostats, VCRs, ATMs and traffic lights.

Age-sensitive applications

Applications that work with age projections or multiyear offerings may malfunction in 2000. Many computers will assume that it is 1900 and begin making mistakes or will shut down because of built-in safety features.

Incorrect calculation	Correct calculation
• Birth year: 1954	• Birth year: 1954
• Age in 1999: 99-54=45	• Correct calculation: 2000-1954=0046
• Age in 2000: 00-54=-54	

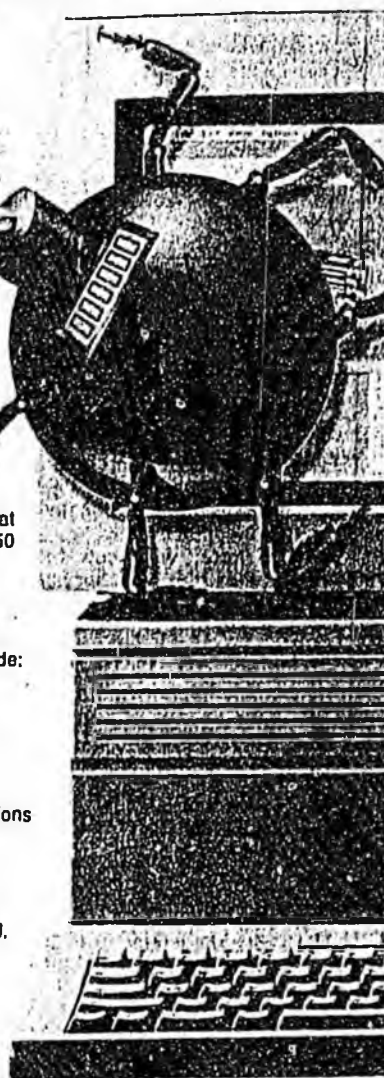
Global cost estimates

- Estimates of the global cost could exceed \$600 billion
- For a medium-size business (one that has 8,000 programs that support business operations), the cost will be approximately \$450 to \$600 per program, or \$3.6 million to \$4.8 million

Embedded-system devices

More than 50 million embedded-system devices worldwide will exhibit year 2000 date anomalies. Some of the problems include:

- | | |
|--|--|
| <p>Aviation</p> <ul style="list-style-type: none"> • In-flight tracking computer might lose where aircraft has been and where it's heading. <p>Military systems</p> <ul style="list-style-type: none"> • Weaponry may malfunction or not operate. <p>Packaging systems</p> <ul style="list-style-type: none"> • Unable to print correct expiration dates on food labels; could shut down product lines. <p>Manufacturing</p> <ul style="list-style-type: none"> • Shipments from suppliers could be delayed or not sent. | <p>Government</p> <ul style="list-style-type: none"> • Government benefits could be delayed or stopped. Tax records could be lost. <p>Power stations</p> <ul style="list-style-type: none"> • Safety systems and malfunctions could cause shutdowns. <p>Banking</p> <ul style="list-style-type: none"> • Electronic transactions could fail. Investment interest may be delayed or incorrectly calculated. <p>Security systems</p> <ul style="list-style-type: none"> • Safes, locks and other security and time-sensitive devices could fail. |
|--|--|



WINDOW OF OPPORTUNITY

Some Y2K fixes offer shortcuts to meet 2000

By LESLIE J. NICHOLSON and JOHN J. FRIED
Knight Ridder Newspapers

There is no single formula for solving a Y2K problem in software, no "silver bullet" sitting in Bill Gates' vault at Microsoft.

Personal-computer users generally have less cause to worry than companies and governments using more complex technology.

The PC program that keeps time is called the BIOS, or basic input/output system. It is software permanently encoded on a chip that keeps track of the date, even when the computer is not on, and sends the date to the software applications that are running on the PC.

A PC user might be able to upgrade the BIOS with a special program obtained from the BIOS' manufacturer. Commercial software to override the BIOS also is

Checking your PC

Here's how to verify that your computer running Microsoft Windows 95 or 98 will work properly when 2000 arrives.

From the Windows desktop, choose Start, Settings and Control Panel.

Click Date and Time. The Date/Time Properties screen will appear.

Change the Date to December 31, 1999, and the Time to 11:59:00 p.m.

rules even under the cover of Windows, will step in. Because DOS is written with 1980 as its basis year, it will decree not that the year is 2000, not that it is 1900 but that it is 1980.

Got that?
Unfortunately, matters grow only more confusing. If you bought a Pentium in 1997 or so, your computer's BIOS — a piece of data embedded permanently in one of your computer's main chips — probably knows all about the 2000, especially if its BIOS was written by Phoenix Technologies, its subsidiary Award Software or other leading BIOS vendors.

If your software has been purchased during the past two years or if you have upgraded your software recently, then you are, in all probability, safe.

Some new programs have minor problems with 2000, but patches are on the way.

Data files created by spreadsheets, data bases and other similar programs may also be problematic if you created them before 1997.

Even if your BIOS and programs are now 2000-ready, older files with two-digit years written into them will flop after Jan. 1, 2000.

As a result of all this, if you harbor any doubts about your system, you are thinking that you should find software to test and fix your computer.

Recently, at least two of the programs purporting to address the Year 2000 problem have crossed my desk: Fix2000 by Intelliquis and Norton 2000 by Symantec.

Once installed, Fix2000 opens with a screen with four simple options: to search for software with Y2K problems, to search for them and fix them, to search for problems that are there but cannot be fixed yet, and to undo any fixes that have been made.

If time spent on a task is

Please see Page C-3, REPAIRS

Weapons
• Weaponry may malfunction or not operate.

Packaging systems

• Unable to print correct expiration dates on food labels; could shut down product lines.

Manufacturing

• Shipments from suppliers could be delayed or not sent.

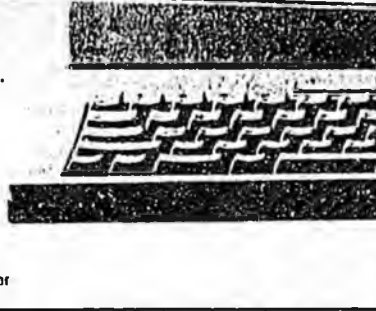
Banking

• Electronic transactions could fail. Investment interest may be delayed or incorrectly calculated.

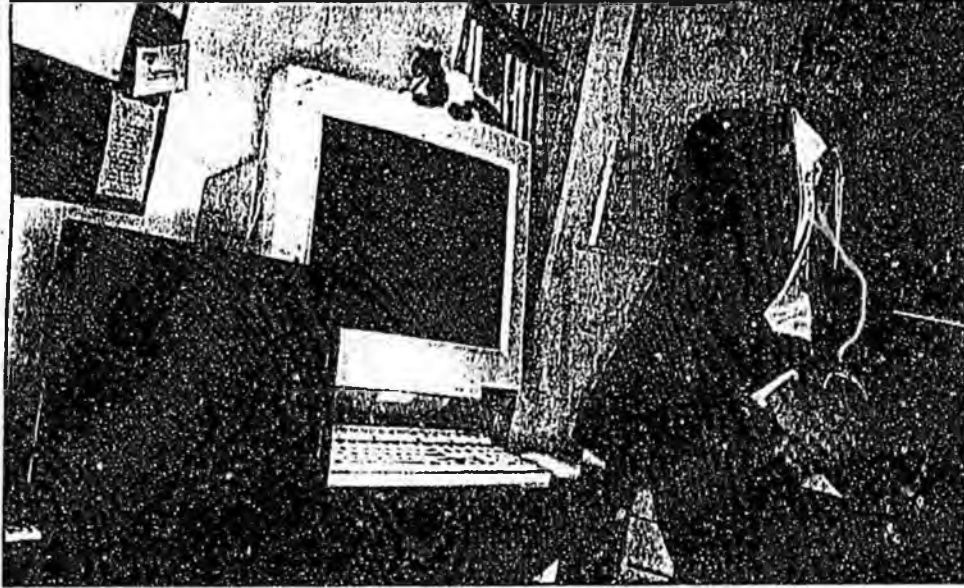
Security systems

• Safes, locks and other security and time-sensitive devices could fail.

SOURCES: Gartner Group, Chicago Tribune file photos, Apple Computer, Reininger



Knight Ridder Tribune



MICHAEL WIRTZ / Philadelphia Inquirer

The trouble with fixing a program that can't handle the year 2000, says Spiros Mancoridis, an assistant professor of computer science at Drex-

el University, is that there often is no documentation of how the original programmer did what he or she did.

Survivalists see new crowd in surplus stores

By FELIX SANCHEZ
The Orange County Register

SANTA ANA, Calif. — Cases of 1 1/2-pound cans of chili mac. Nutrition bars packing 3,600 calories in each lemony rectangle. Giant blue 55-gallon water storage drums. Solar-powered radio-flashlights.

The so-called millennium bug has put a buying bug into a surprising number of people. They want to be prepared in case a computer meltdown hits when 1999 turns into 2000 and scrambles programmed data — the so-called Y2K scenario.

Regular people, and not just alarmists, are

worried that automatic teller machines, gasoline pumps, 401(k) plans, electrical grids and any number of life's staples may be brought down by malfunctioning computers.

As a result, military surplus stores are getting visits from clientele they normally don't see.

"That's the most ironic thing and strange thing about this. It's the type of people that are coming in," said Lindsey Shapiro, 22. The University of California Santa Barbara psychology graduate is helping her mom, Randi, run Tustin

Please see Page C-3, SUPPLIES

tions that are running on the PC.

A PC user might be able to upgrade the BIOS with a special program obtained from the BIOS' manufacturer. Commercial software to override the BIOS also is available, as are special plug-in boards that will bypass the BIOS and provide the correct date.

If the software programs running on the PC have a Y2K problem, compliant versions and patches are likely to be available on the manufacturer's web site.

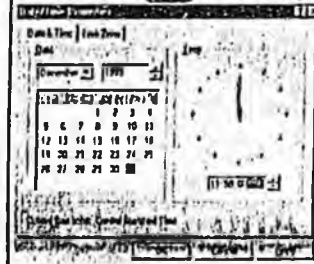
The chief problem for many PC users will be older files that were generated on non-compliant software, especially data bases and spreadsheets. Users can buy numerous "fix-it" programs that attempt to find and resolve Y2K problems in the BIOS, the application software, and specific files.

Big computers are where the major Y2K software problems lie.

For them, the most durable, yet tedious, solution is to use human beings or automated programs to go through each line of code, seek out dates, and expand the years to four digits, theoretically making the coding good for 8,000 more years, until a future generation tackles the Y10K problem.

Date expansion can be tricky because dates don't always make themselves easily known. Blue Moon Consulting, a Y2K consulting firm with offices in

Change the Date to
December 31st 1999, and the
Time to 11:59:00 p.m.



Click Apply and click OK.

Shut down your PC.

Wait approximately 3 minutes.
Turn your PC back on.

After Windows has restarted,
choose Start Settings and
Control Panel.

Click Date and Time.
The year should be
2000 and the time
should be
just after midnight.

Follow steps 1-6
to change the
time back.

SOURCE: Hewlett-Packard

Please see Page C-4, Y2K

Oil layoffs may offer home-buying opportunities

... intention of leaving. Buyers will ... available to these oil industry employees. The ... determine what type of financing is best for

Home appliances should be immune to bug

By MIKE KENNEDY
Knight Ridder Newspapers

KANSAS CITY, Mo. — You're sleeping soundly without a worry about Jan. 1, 2000. After all, you don't even own a personal computer.

Then the alarm clock buzzes. The furnace blows warm air. The coffee maker drips out the morning's first pot. The VCR plays your daily workout video while the microwave heats breakfast from the freezer. The blow dryer and curling iron help you style your hair. The washing machine spins a load of laundry. The CD player provides background music.

And before you're even fully awake, you've used at least 10 computer chips, which are hidden in a surprising number of home appliances.

Don't worry too much. The vast majority of home appliances and consumer electronics should enter 2000 working the same way they did in 1999. Even if they keep track of the time, they don't care about the year.

"We don't think the consumer products are going to be a problem," said Elaine Kolish of the Federal Trade Commission's Bureau of Consumer Protection.

But even optimists say some glitches are likely — and it's almost impossible to predict where they will occur. Computer chips are difficult to reach, and it's hard to know what information is on them.

"You can't just pop (a chip) open like the hood of a car and see if the oil's low," said Jeff Weir, spokesman for the Semiconductor Industry Association in San Jose, Calif.

Even if an appliance — a curling iron, for example — doesn't need to keep track of a date, that doesn't mean the chip inside is not keeping the date.

— Y2K consultant Mark Frautschi

Even if an appliance doesn't appear to be keeping track of the date, the chip inside could be, experts say, and that could cause problems. When the calendar changes from Dec. 31, 1999, to Jan. 1, 2000, chips that use only two digits to keep track of the year could mistake 2000 for 1900.

The appliance industry isn't alarmed.

Only certain products — those that display a date — could be affected, spokesmen say.

The trade commission, in a consumer alert issued in October, noted that VCRs, cameras, camcorders, wristwatches and pocket electronic organizers could begin displaying incorrect information in 2000.

But other products should not be affected, including televisions, microwave ovens, vacuum cleaners, hair dryers, stereos, coffee makers, air conditioners, telephones, refrigerators, washers, dryers, furnaces and cars.

"Products that display or use only the time of day and/or day of the week — programmable microwave ovens and coffee makers, for example — are not likely to have Y2K problems," the commission said. "Other products — like refrigerators and heating and cooling equipment — may have chips that keep track of cycles rather than dates and also are un-

likely to have Y2K problems."

Some companies have placed information on the Internet about whether their products will have any problems related to 2000.

"I expect there will be more and more disclosure in the coming weeks and months as the public begins to become more familiar with the issue," Kolish said.

The Association of Home Appliance Manufacturers, the Gas Appliance Manufacturers Association, the Consumer Electronics Manufacturers Association and individual companies have issued statements that most products will not have 2000 problems.

For example, Michael Cabot, manager of corporate relations for Sony Electronics, said some Sony video cameras made in the late 1980s would display the wrong date after Jan. 1, 2000, but that won't affect their taping capabilities.

"None of our consumer products will stop operating," Cabot said.

John Ahearne, director of communications for the information systems services division of General Motors, said GM cars will start and function normally on Jan. 1, 2000.

"They've been checking these things for years," Ahearne said. "It's all taken care of."

They're very confident there won't be a problem."

Others familiar with Y2K issues aren't so sanguine.

A product that doesn't use a calendar to work properly could still have a calendar function — and potential Y2K troubles — on its computer chip, said Mark Frautschi, a Y2K consultant in Lutherville, Md.

For some manufacturers, it might be cheaper to buy chips "off the shelf" instead of customizing chips for their products. Those chips could have more functions, such as date keeping, than is necessary for the product.

Even if an appliance — a curling iron, for example — doesn't need to keep track of a date, that doesn't mean the chip inside is not keeping the date, Frautschi said.

Tracking down what information is on a chip can be difficult when companies buy chips from third-party sources and the original computer code isn't available.

"If you don't get to the company that produced the software, you're going to have a hard time determining if it's Y2K-compliant," Weir said.

And some chips may have a delayed Y2K problem if they have calendar functions that are not in step with the actual date, Frautschi said. The chip's internal clock may not arrive at Jan. 1, 2000, until months or years later.

Even with those potential troubles, Frautschi says he thinks problems will arise in only a tiny percentage of consumer products.

"I would guess in the vast majority of cases, the device will turn out fine," he said.

REPAIRS: Corrections time-consuming

Continued from Page C-1

an example of thoroughness, Fix2000 is that. A search-only pass through a hard drive with about a dozen programs on it took more than half an hour.

A search-and-fix pass took even longer than that, though I can't tell you exactly how much, because I canceled the process after 45 minutes.

Fix2000 ran smoothly except for two glitches: After I had it run through its search-only routine, it refused to follow my orders to get into the search-and-fix mode until after I had rebooted the machine.

And when it found a DOS-related problem it could not fix while running in Windows, the program sent up one of those scary "system error" boxes, without making

that my version of the program is in fine shape.

Norton 2000 also suggested that I obtain version 8.04 of Outlook for Y2K compliance, even though 8.05 is already on my system.

But why the caustic lots-of-luck re-

And hitches Norton flagged got right by Fix2000.

The inconsistency is not peculiar to Fix2000 and Norton 2000.

When I tested Network Associates Inc.'s 2000 Toolbox and Check 2000 PC from Greenwich Mean Time-UTA, they too told different stories about my computer's ability to cope with Y2K.

So it seems that the only way to make sure that every byte within the PC has been probed is to buy every Y2K program around.

Far more worrisome is that some Y2K programs provide software fixes for non-Y2K-compliant BIOSes.

Laurent Gharde, vice president for marketing at Phoenix Technologies, a leading BIOS vendor, points out that software fixes are the "cheapest, easiest" fixes but are also the least desirable.



SUPPLIES: Fear spurs buying binge

Continued from Page C-1

Military Surplus in Tustin, Calif.

Two weeks ago, a group of families from San Juan Capistrano bought several hundred dollars' worth of water storage tanks, military ready-to-eat meals and survival supplies, Shapiro said.

The buyers are intelligent, from middle-class families, and churchgoers, Shapiro said.

Business has increased about 25 percent because of Y2K, Randi Shapiro said. About 20 people made in-

tain about the effects of the Y2K problem."

It then gives a checklist of things you can do — just in case. According to the Red Cross, about 1,300 pamphlets have been distributed in Orange County — many to neighborhood groups and churches, which requested several hundred.

"We don't want to scare people," said Judy Iannaccone, public affairs director for the Orange County chapter. "It's not like the phone lines are jammed, but it is surprising. The calls are coming from all levels of society."

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And when it found a DOS-related problem it could not fix while running in Windows, the program sent up one of those scary "system error" boxes, without making clear whether to opt for Retry, Cancel or Abort, the choices within the box.

Opting for Cancel turned out to be the right one because what followed was a message that the problem would be dealt with after Windows-based programs had been fixed and I exited to DOS.

In addition to testing your PC's BIOS, Norton 2000 goes after programs, putting special emphasis on data bases and spreadsheets, as well as data files.

Norton sped through a hard drive with some 6 gigabytes of material on it and returned clear explanations of the Y2K problems it encountered.

Though Norton 2000 includes a software fix for noncompliant BIOSes, it conspicuously does not offer to fix data or programs.

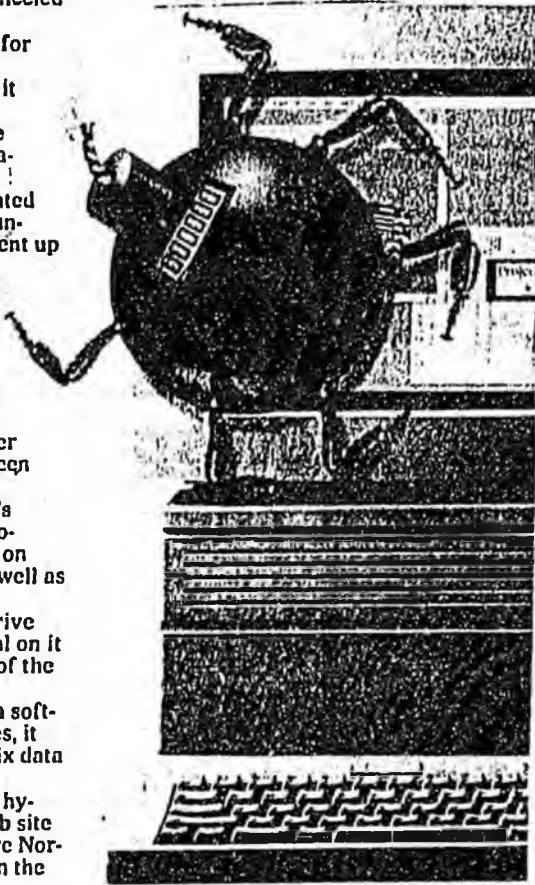
What Norton does is provide a hyperlinked URL address to the web site of the vendor behind any software Norton finds ill-equipped for 2000. On the site you will presumably find an appropriate fix.

Though Norton 2000 seems to do its job well and provides clear explanations for all the problems it finds, some of its work gave me pause.

Among other things, it signaled problems in my WinFax and Microsoft Outlook 98 programs.

What puzzled me is that Symantec's site — WinFax is its product as well — contained information that seemed pretty unequivocal in its declaration

But why the caustic lots-of-luck re-



mark at the top of the column if, except for a few glitches here and there, the programs did their jobs?

Because Fix2000 and Norton 2000 gave me different results.

Fix2000, for example, returned reports that a massive number of my dynamic library links — small files used as helpmates by other programs — had Y2K-disease. Norton breathed not a hint of this.

from Greenwich Mean Time-0-1-1, they too told different stories about my computer's ability to cope with Y2K.

So it seems that the only way to make sure that every byte within the PC has been probed is to buy every Y2K program around.

Far more worrisome is that some Y2K programs provide software fixes for non-Y2K-compliant BIOSes.

Laurent Gharda, vice president for marketing at Phoenix Technologies, a leading BIOS vendor, points out that software fixes are the "cheapest, easiest" fixes but are also the least desirable.

That's because the software overriding the post-2000 and no longer valid clock settings could itself become the victim of a malfunction.

Add-on boards to override BIOS settings are also seen as a solution by some for the Y2K problem.

I have not tested one, but I know this: Just reading the warnings and cautions in the manual that came with one tells me that you fool with this sort of solution at your own risk as well.

There is still another BIOS fix-it alternative.

You can visit the web site of your computer's manufacturer or of the company that wrote its BIOS to determine two things:

- If your computer's BIOS is flashable — if the BIOS currently in its chip bank can be updated with a program designed to do the job.
- If such a file is available.

The problem with the solution, of course, is that you may not have a flashable BIOS. Or, if you do, that the version you download is incompatible with your computer.

As a last resort before you start shopping for a new computer, you could have a technician replace the BIOS chip itself.

The choices are not pretty, are they? Fix2000 for Windows is about \$50. More information: 1-801-553-1127. Norton 2000 for Windows is about \$50. More information: 1-800-441-7234.

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Sherry Heltz, owner of Quake Kare Inc. in Thousand Oaks has seen telephone purchases approaching \$10,000 from her wholesale company. Orders come in every day.

Government and private industry offer reassurance that they are trying to prepare computers for the date change. But predictions about what could happen range from the moderate (ATMs unable to give out cash for a few days) to the catastrophic (financial chaos and delayed airline flights).

In recent days, the American Red Cross has begun issuing some cautionary advice. In the past few weeks, the organization has received a crescendo of calls from worried residents, here and across the United States. So many that it has issued a brochure cautioning that while nothing bad is likely to happen, "no one can be cer-

things you can do — just in case. According to the Red Cross, about 1,300 pamphlets have been distributed in Orange County — many to neighborhood groups and churches, which requested several hundred.

"We don't want to scare people," said Judy Iannaccone, public affairs director for the Orange County chapter. "It's not like the phone lines are jammed, but it is surprising. The calls are coming from all levels of society."

The Red Cross stresses that planning for the remote possibility that Y2K will cause a problem is like planning for an earthquake or any other disaster — most of the materials you should gather will be useful for some kind of disaster even if nothing happens with Y2K.

And that's a good thing, Iannaccone said.

The preparations include stocking up on food and water, getting some extra cash in hand and establishing an alternative power source.

These are mild recommendations compared with those on numerous Internet sites that are peddling a year's supply of freeze-dried or prepared food — things like pepperoni-flavored vegetable or bags of wheat flour — and huge water storage tanks, and predicting dire straits for people hung over from epic new millennium parties.

And everybody else too.

You are invited to an important workshop:

Financial planning for the next millennium

Make plans to attend our workshop and you will hear the following vital topics discussed in detail:

Retirement Investment Strategies

Independent Professionals

Big Office Benefits at an Affordable Price

Pacific Office Center gives small and independent businesses all of the advantages of a prestigious corporate office at an incredibly affordable price. For as little as \$740 per month Pacific Office Center clients enjoy an efficient and professional office environment, plus:

- A spacious, brand-new office (many with excellent views!)
- Your business line answered promptly by the center's receptionist, plus state-of-the-art voice mail and daily mail

In addition to her press hat, Ella Wright wears several other hats in The National Federation of Press Women (NFPW) as well as working full-time for the Bureau of Land Management. Without Ella's efforts Anchorage would not have the opportunity

to host the 275 expected delegates of NFPW and their families when they come to Anchorage in September, 2000.



275 delegates Sept. 2000

Bring your group to town To be a meeting

38

HB



**INVESTMENT
COMPANY
INSTITUTE**

FACSIMILE COVER SHEET

Date: May 7, 1999

**TO: The Honorable Norman Rokeberg
Chairman, House Labor and Commerce Committee
Alaska House of Representatives**

FAX: 907-465-2040

**FROM: Tami Cain Reed
1401 H Street, N.W.
Suite 1200
Washington, D.C. 20005-2148**

**Tel: 202/326-5825
Fax: 202/326-5839**

NUMBER OF PAGES IN THIS TRANSMITTAL (w/COVER): 2

Re: Attached please find a letter the Investment Company Institute faxed today to Senators Robin Taylor, Rick Halford, Jerry Mackie, Drue Pearce, and Johnnie Ellis to encourage them to have the Senate Judiciary Committee hear and consider favorably House Bill 83, which you sponsored. The Institute remains very interested in the enactment of this very important piece of legislation and we appreciate your sponsorship of it. If we can be of any assistance in ensuring the enactment of this bill, please let me know. Tami Reed, Associate Counsel, Investment Company Institute

If you should have problems receiving this fax, please call Deborah Washington at (202) 326-5818.

This transmission is intended for the sole use of the individual and entity to whom it is addressed, and may contain information that is privileged, confidential and exempt from disclosure under applicable law. You are hereby notified that any dissemination, distribution or duplication of this transmission by someone other than the intended addressee or its designated agent is strictly prohibited. If your receipt of this transmission is in error, please notify the Institute immediately by collect call to (202) 326-5818, and send the original transmission to us by return mail at the address above.



INVESTMENT COMPANY INSTITUTE

May 7, 1999

Senator Drue Pearce
President
Alaska Senate
State Capitol Room 111
Juneau, AK 99801-1182

Re: House Bill 83

Dear Senator Pearce:

The Investment Company Institute^{*} is writing to respectfully request that the Senate Judiciary Committee hear and consider favorably House Bill 83, which would conform the Alaska Securities Act to the federal securities laws. Importantly, failure to enact this bill is expected to result in a loss of revenue to the State of Alaska estimated at \$4 to \$5 million. This is because, under the National Securities Markets Improvement Act of 1996 ("NSMIA"), which was enacted by Congress in 1996, as of October 11, 1999 all states lose the ability to impose registration fees on mutual funds and on federally registered investment advisers. While NSMIA does authorize states to replace existing registration fees with "notice filing" fees, the failure of a state to enact a notice filing fee means that, as of October 11, 1999, the state loses its lawful authority to collect fees from mutual funds and federally registered investment advisers. Alaska remains one of less than a dozen states that have yet to amend their securities acts in response to NSMIA and that, as a result, risk the loss of millions of dollars in current revenues.

To avoid the cessation of revenues currently collected under the Alaska Securities Act, the Institute strongly urges the Committee to consider and pass this important piece of legislation. If you have any questions concerning this bill or the Institute's position on it, please contact me at (202) 326-5825. Thank you for your consideration of our views.

Sincerely,

A handwritten signature in cursive script that reads "Tamara K. Reed".

Tamara K. Reed
Associate Counsel

* The Investment Company Institute is the national association of the American investment company industry. Its membership includes 7,546 open-end investment companies ("mutual funds"), 457 closed-end investment companies and 8 sponsors of unit investment trusts. Its mutual fund members have assets of about \$5.730 trillion, accounting for approximately 95% of total industry assets, and have over 73 million individual shareholders. The Institute also represents the interest of investment advisers. Many of the Institute's investment adviser members render investment advice to both investment companies and other clients. In addition, the Institute's membership includes 431 associate members which render investment management services exclusively to non-investment company clients. A substantial portion of the total assets managed by registered investment advisers are managed by these Institute members and associate members.

STATE OF ALASKA

DEPARTMENT OF COMMERCE AND ECONOMIC DEVELOPMENT

DIVISION OF BANKING, SECURITIES, AND CORPORATIONS

TONY KNOWLES, GOVERNOR

333 Willoughby Avenue, 9th Floor
P.O. BOX 110807
JUNEAU, ALASKA 99811-0807
Banking & Securities (907) 485-2521
Corporation Section (907) 465-2530

ANCHORAGE
Corporation Information (907) 269-8140
TDD: (907) 465-5437

March 14, 1999

The Honorable Norman Rokeberg
Alaska House of Representatives
State Capitol Room 24
Juneau, AK 99801-1182

Dear Rep. Rokeberg:


Re: CSHB 83(JUD) Various Amendments to the Alaska Securities Act (AS 45.55)

We are asking for your support in passing CSHB 83(JUD) when it comes before you for a vote on the floor for the following reasons:

1. This bill brings the Alaska Securities Act into compliance with the federal law known as the National Securities Markets Improvement Act (NSMIA), thus preserving Alaska's authority to collect fees from mutual funds and investment advisers that currently amount to about \$4 million in annual general fund revenues. Failure to pass legislation by October 1999 would jeopardize those revenues.
2. The language in the bill was drafted largely by the North American Securities Administrators Association (NASAA), an organization of state and provincial securities regulators which include every state, the District of Columbia, Puerto Rico, the provinces of Canada, and Mexico.
3. More than 40 other states have already passed similar legislation.
4. We have received letters of support from 4 national associations representing the mutual fund industry and investment advisers. We also have received 10 support letters from Alaskans who are securities lawyers, broker-dealer agents, or investment advisers. We have discussed this legislation with the Alaska Bar Association, the Anchorage Bull and Bear Club, and the Alaska Society of CPAs.
5. The bill improves access to capital markets by small businesses by adding new exemptions from registration.
6. Investor protection is improved by the inclusion of language regulating investment advisers that will only be registered with the states due to NSMIA, and the provision of additional time for an investor to sue when a victim of fraud.

We ask for your support of this important legislation. Thank you.

Yours truly,



Franklin T. Elder
Director

ALASKA STATE LEGISLATURE
House of Representatives

COMMITTEE ASSIGNMENTS:

LABOR & COMMERCE COMMITTEE, CHAIRMAN
SPECIAL COMMITTEE ON OIL & GAS, MEMBER
JUDICIARY COMMITTEE, MEMBER
CORRECTIONS BUDGET SUBCOMMITTEE, MEMBER
ADMINISTRATION BUDGET SUBCOMMITTEE, MEMBER
HESS BUDGET SUBCOMMITTEE, MEMBER



INTERIM:
716 WEST 4TH AVENUE, SUITE 640
ANCHORAGE, AK 99501
PHONE: (907) 258-8191
FAX: (907) 258-2916

SESSION:
STATE CAPITOL
JUNEAU, AK 99801-1182
PHONE: (907) 465-4968
FAX: (907) 465-2040

Representative Norman Rokeberg

JUST THE FAX

Date: February 9, 1999

TO: Terry Bannister, Legislative Counsel

FAX: 2029 Telephone:

FROM: Representative Norman Rokeberg

FAX: (907) 465-2040 Telephone: (907) 465-4968

Number of Pages: 4 (including this page) Re: HB 13

Following is a letter from DCED (with a copy of Vincent Uresa's memorandum).

Comments:

This is a followup to the concerns expressed in your memorandum of
Jan. 28th memo on the Alaska Securities Act.

Rep. Rokeberg

Have a Nice Day

STATE OF ALASKA

DEPARTMENT OF COMMERCE AND ECONOMIC DEVELOPMENT

DIVISION OF BANKING, SECURITIES, AND CORPORATIONS

TONY KNOWLES, GOVERNOR

333 Willoughby Avenue, 9th Floor

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Corporation Section (907) 465-2530

Facsimile (907) 465-2549

ANCHORAGE

Corporation Information (907) 269-8140

TDD: (907) 465-5437

February 4, 1999

FEB 05 1999

The Honorable Norman Rokeberg
Chairman, House Labor and Commerce Committee
Alaska House of Representatives
State Capitol Room 24
Juneau, AK 99801-1182

Dear Chairman Rokeberg:

RE: Legislative Counsel Memo of January 28, 1999

You asked us to comment on an issue raised by legislative counsel in the cover memo they sent to you dated January 28, 1999 along with the draft of the Alaska Securities Act bill (Work Order No. 21-LS0253A). Since the issue raised is a legal one, we asked the department of law to provide a comment. In response to that request, Mr. Vincent Usera, Assistant Attorney General, wrote the enclosed memo dated February 3, 1999.

As you can see, Mr. Usera's memo provides an unambiguous answer to the question raised by legislative counsel. In addition, we note that legislative counsel acknowledges that the approach in the draft legislation to reference federal law as it may be amended from time to time is "not uncommon, particularly where federal laws significantly affect the area being regulated, as here." Indeed, legislative counsel is correct in that assertion. Federal covered securities, covered advisers, and investment adviser representatives are all defined by federal law. We have no choice but to follow that and to keep our statute current and consistent, this is the most efficient approach.

We hope this fully responds to the question. If you have further questions, please do not hesitate to ask.

Yours truly,



Franklin T. Elder
Acting Director

cc: Jeff Bush, Deputy Commissioner
Ginny Fay, Special Assistant

Enclosure (1)

MEMORANDUM

State of Alaska
Department of Law

TO: Terry Elder, Acting Director
Division of Banking, Securities
and Corporations
Department of Commerce and
Economic Development

DATE: February 3, 1999

TEL.NO.: 465-4118

FEB 05 1999

FROM: Vincent L. Usera 
Assistant Attorney General

SUBJECT: Alaska Securities Act

You asked whether there is a constitutional problem with providing for federal law to automatically supersede state law including future amendments. There is not; this is done in several places in the Alaska Statutes. For instance, under AS 27.21.960 our statutes are automatically invalidated if they conflict with Surface Mining Control and Reclamation Act of 1977 or regulations adopted under that federal statute.¹ There is a provision in our tax law that adopts the Internal Revenue Code by reference.² Also, at AS 47.07.040 there is a provision for preparation of a state medical assistance plan in accordance with federal statute.³ It is

1. AS 27.21.960. Inconsistencies with federal act. (a) A provision of this chapter that is inconsistent with the provisions of the Surface Mining Control and Reclamation Act of 1977 as determined by the Secretary of the United States Department of the Interior under 30 U.S.C. 1255(b) is invalid from the date of the secretary's determination.

(b) If a provision of the Surface Mining Control and Reclamation Act of 1977 or of the regulations promulgated under that Act by the Secretary of the United States Department of the Interior is deleted, amended, set aside, enjoined, or declared invalid by Congress, the secretary, or in a final, unappealable judgment of a court of competent jurisdiction, then the commissioner shall review the changes made and make an appropriate recommendation as to whether changes in this chapter or the regulations adopted under it should be made.

2. AS 43.20.021(a). Sections 26 U.S.C. 1-1399 and 6001-7872, as amended, are adopted by reference as a part of this chapter. Those portions of the Internal Revenue Code have full force and effect under this chapter unless excepted to or modified by other provisions of this chapter. However, nothing in this chapter or AS 43.19 may be construed as an exception to or modification of 26 U.S.C. 883.

3. AS 47.07.040. State plan for provision of medical assistance. The department shall prepare a state plan in accordance with the provisions of 42 U.S.C. 1396 - 1396p (Title XIX, Social Security Act, Medical Assistance) and submit it for approval to the United States Department of Health and Human Services. The plan shall designate that the Department of Health and Social Services is the single state agency to administer this plan. The department shall act for the state in any negotiations relative to the submission and approval of the plan. The department may make those arrangements or regulatory changes, not inconsistent with law, as may be required under federal law to obtain and retain approval of the United States Department of Health and Human Services to secure for the state the optimum federal payment under the provisions of 42 U.S.C. 1396 - 1396p (Title XIX, Social Security Act, Medical Assistance).

not uncommon for us to adopt federal law by reference.

Additionally, the case cited by Terry Bannister's memo concerns an entity adopting amendments to the building code which was a function of a private, non-governmental body. It bears no relation to our case.

VLU/ps

FISCAL NOTE

STATE OF ALASKA
1999 LEGISLATIVE SESSION

BILL NO. CSHB 83 (JUD) (TITLE AM)

Revision Date/Time (Note if correction) _____ Dept. Affected Commerce & Econ. Dev.
 Title Alaska Securities Act BRU Banking, Securities and Corporations
 Component Banking, Securities and Corporations
 Sponsor Labor & Commerce by Request
 Requester Senate Judiciary Component Serial No. 1233

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2000	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005
Personal Services						
Travel						
Contractual						
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL EXPENDITURES						
-----------------------------	--	--	--	--	--	--

CHANGE IN REVENUES ()						
-------------------------------	--	--	--	--	--	--

FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type)						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY99) cost: _____

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

Because most of the provisions of HB 83 simply bring the Alaska Securities Act (the Act) into compliance with federal law (National Securities Markets Improvement Act of 1996 (NSMIA)), thus preserving the State's revenue and current authority to regulate market participants, there is no cost to implement this bill. Failure to pass this bill would result in a loss of currently anticipated revenue to the State of an estimated \$3.9 million in FY00, rising to \$6.4 million in FY05. Most of the language in HB 83 is uniform language, drafted by the North American Securities Administrators Assn., and has been adopted in a majority of the states at this time.

Franklin T. Elder

Prepared by Franklin T. Elder, Director Phone 465-2521
 Division Banking, Securities and Corporations Date/Time 4/22/99 8:06 AM
 Approved by Commissioner Deborah B. Sedwick Date 4/22/99
 Agency Commerce and Economic Development

PREPARER TO PROVIDE ALL DISTRIBUTION COPIES TO GOVERNOR'S LEGISLATIVE OFFICE

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FISCAL NOTE

**STATE OF ALASKA
1999 LEGISLATIVE SESSION**

BILL NO. HB 83 (L&C)

Revision Date/Time (Note if correction) _____ Dept. Affected Commerce & Econ. Dev.
 Title Alaska Securities Act BRU Banking, Securities and Corporations
 Component Banking, Securities and Corporations
 Sponsor Labor & Commerce by Request
 Requester Senate Labor and Commerce Component Serial No. 1233

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2000	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005
Personal Services						
Travel						
Contractual						
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL EXPENDITURES						
-----------------------------	--	--	--	--	--	--

CHANGE IN REVENUES ()						
-------------------------------	--	--	--	--	--	--

FUND SOURCE (Thousands of Dollars)

FUND SOURCE	FY 2000	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005
1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type)						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY99) cost: _____

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

Because most of the provisions of HB 83 simply bring the Alaska Securities Act (the Act) into compliance with federal law (National Securities Markets Improvement Act of 1996 (NSMIA)), thus preserving the State's revenue and current authority to regulate market participants, there is no cost to implement this bill. Failure to pass this bill would result in a loss of currently anticipated revenue to the State of an estimated \$3.9 million in FY00, rising to \$6.4 million in FY05. Most of the language in HB 83 is uniform language, drafted by the North American Securities Administrators Assn., and has been adopted in a majority of the states at this time.

Prepared by Franklin T. Elder, Director Phone 465-2521
 Division Banking, Securities and Corporations Date/Time 4/16/99 11:19 AM
 Approved by Commissioner Deborah B. Sedwick Date 4/16/99
 Agency Commerce and Economic Development

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STATE OF ALASKA

DEPARTMENT OF COMMERCE AND ECONOMIC DEVELOPMENT

DIVISION OF BANKING, SECURITIES, AND CORPORATIONS

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TDD: (907) 465-5437

April 7, 1999

The Honorable Norman Rokeberg
Alaska House of Representatives
State Capitol Room 24
Juneau, AK 99801-1182

Dear Rep. Rokeberg:

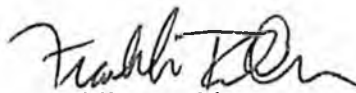
Re: CSHB 83(JUD)(am Title) Various Amendments to the Alaska Securities Act (AS 45.55)

After the title of this bill was amended, we spoke to some members who suggested two additional changes to the new title before passing the bill out of the House. The two changes would return those phrases to their wording in the original title. One phrase would be deleted because it was redundantly added when the title was amended.

We have attached a copy of the amended title that we have discussed. We believe it would be beneficial to accommodate those members that have expressed an interest in this small title change. The title remains considerably shorter than the original, which was the goal of the previous title change. The added language was the language in the previous title, and, if it makes even one more member happy without doing any harm to the bill or the title in any other way, we believe this should be done.

We would support this title amendment and then passage of HB 83 by the House in today's session. It is imperative that we have some time to work with the other body as it considers this legislation. We urge your support of appropriate action to accomplish that. Thank you.

Yours truly,



Franklin T. Elder
Director

Similar letter to: The Honorable Brian Porter
The Honorable Joe Green
The Honorable Ethan Berkowitz

CSHB 83(JUD)(TITLE AM)

“An Act relating to certain securities occupations and investment pools; relating, with regard to the Alaska Securities Act, to federal covered securities, the registration of securities, the general exemptions for securities and transactions, Internet offers of securities and transactions, file confidentiality, [COURT PETITIONS FOR CIVIL PENALTY JUDGMENTS, PENALTIES FOR WILFUL VIOLATIONS] petitions to superior court by the administrator to reduce civil penalties to judgment, time limits for bringing court actions for violations, administrator-established fees and administrator-required reimbursements, consent to service, title, sales, purchases, offers to sell, and offers to purchase; [EXEMPTING CERTAIN VIOLATIONS OF THE ALASKA SECURITIES ACT FROM CERTAIN PENALTIES] exempting certain violations of the Alaska Securities Act from criminal penalties; amending or repealing certain current definitions in the Alaska Securities Act; providing new Alaska Securities Act definitions for certain securities occupations, for certain federal statutes, and for the terms ‘advisory client,’ ‘advisory fee,’ ‘advisory services,’ ‘clients who are natural persons,’ ‘federal covered security,’ ‘investment advisory business,’ ‘investment advisory contract,’ ‘NASDAQ,’ ‘notice filing,’ ‘place of business,’ ‘principal place of business,’ ‘securities business,’ ‘substantial portion of the business,’ and ‘supervised person’; and providing for an effective date.”

THE KITO GROUP

Sam Kito, Jr.
Kate Tesar
William A. Thomas, Jr.

APR 06 1999

Memorandum

Date: April 6, 1999
To: Rep. Norm Rokeberg
From: Sam Kito
RE: HB 83

I am forwarding these attachments to you for your review. Please advise me if the two deletions that we are proposing would be acceptable to you.

I can be reached today and tomorrow on my on my cellular phone, 425-239-6319.

SK/lmn

Attachments

4/6/99

Confidential

1

APR-06-99 TUE 12:01 PM
Mar 31 99 01:38p

Cook Inlet Region, Inc.
L Y LIM

FAX NO. 9072635182
103

P. 03
p.2

New

1-LS0253VH.2
Bannister
3/26/99

AMENDMENT # 1

By Rep. Rokeberg

OFFERED IN THE HOUSE

TO: CSHB 83(JUD)

- 1 Page 1, line 1, through page 3, line 1: *(Title Amendment)*
- 2 Delete all material.
- 3 Insert: ""An Act relating to certain securities occupations and investment pools;
- 4 relating, with regard to the Alaska Securities Act, to federal covered securities,
- 5 the registration of securities, the general exemptions for securities and
- 6 transactions, Internet offers of securities and transactions, file confidentiality,
- 7 court petitions for civil penalty judgments, penalties for wilful violations, time
- 8 limits for bringing court actions for violations, administrator-established fees and
- 9 administrator-required reimbursements, consent to service, title, sales, purchases,
- 10 offers to sell, and offers to purchase; exempting certain violations of the Alaska
- 11 Securities Act from certain penalties; amending or repealing certain current
- 12 definitions in the Alaska Securities Act; providing new Alaska Securities Act
- 13 definitions for certain securities occupations, for certain federal statutes, and for
- 14 the terms 'advisory client,' 'advisory fee,' 'advisory services,' 'clients who are
- 15 natural persons,' 'federal covered security,' 'investment advisory business,'
- 16 'investment advisory contract,' 'NASDAQ,' 'notice filing,' 'place of business,'
- 17 'principal place of business,' 'securities business,' 'substantial portion of the
- 18 business,' and 'supervised person'; and providing for an effective date.'"

APR-06-99 TUE 12:01 PM
Mar 31 99 01:38P

Cook Inlet Region, Inc.
L Y Lin

FAX NO. 9072635182

P. 04

Alaska State House of Representatives
Twenty-First Legislature
First Session

RCS# 125
Item 3

03-31-99
11:26:02

CSHB 83(JUD)
Second Reading
Amendment No. 1

Yeas: 20 Austerman, Barnes, Coghill, Davis, Dyson,
Foster, Green, Harris, James, Kohring,
Kott, Masek, Mulder, Ogan, Porter,
Rokeberg, Sanders, Therriault, Whitaker,
Williams

Nays: 19 Berkowitz, Brice, Bunde, Cissna, Cowdery,
Croft, Davies, Grussendorf, Halcro, Hudson,
Joule, Kapsner, Kemplen, Kerttula, Kookesh,
Morgan, Murkowski, Phillips, Smalley

Excused: 1 Mosas

Absent: 0

FAX 907 263 5182

TO: MARK KROWEA

FAX 2 PAGES

FAX
263-5182

1:LS0253D

Old

HOUSE BILL NO. 83

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-FIRST LEGISLATURE - FIRST SESSION

BY THE HOUSE LABOR AND COMMERCE COMMITTEE BY REQUEST

Introduced: 2/8/99

Referred: Labor and Commerce, Judiciary

A BILL

FOR AN ACT ENTITLED

1 "An Act relating to the licensing of, acts and practices of, notice filings
2 required of, duties of, registration of, capitalization of, financial requirements for,
3 bonding of, coordinated securities examinations of, recordkeeping by, and
4 documents filed by certain securities occupations; relating to public entity
5 investment pools; relating to investment advisory contracts; relating to the
6 examination of records of certain securities occupations; relating to federal
7 covered securities; relating to the registration of securities; relating to the
8 general exemptions for securities and transactions; relating to offers of securities
9 on the Internet; relating to the confidentiality of investigative files under the
10 Alaska Securities Act; relating to the payment by certain securities occupations
11 of expenses and fees of investigations and examinations; relating to petitions to
12 superior court by the administrator to reduce civil penalties to judgment;

HB0083a

-1-

HB 83

New text Underlined (DELETED TEXT BRACKETED)

I-LS02531D

1 [exempting certain violations of the Alaska Securities Act from criminal penalties;
2 relating to time limitations in bringing court actions for violations of the Alaska
3 Securities Act; relating to the affirmative defense of timeliness in court actions
4 relating to securities; prohibiting certain lawsuits involving buyers of securities;
5 relating to time limitations for bringing court actions involving the receipt of a
6 written offer related to securities; relating to offers to repay buyers of securities;
7 relating to notification of certain securities occupations regarding administrative
8 hearings; relating to fees established by the administrator; relating to a sale,
9 a purchase, or an offer to sell or purchase under the Alaska Securities Act;
10 relating to the locations of offers to buy or sell; relating to consent to service;
11 amending the Alaska Securities Act definitions of 'agent,' 'broker-dealer,' 'person,'
12 'Securities Act of 1933,' and 'security;' defining for purposes of the Alaska
13 Securities Act 'advisory client,' 'advisory fee,' 'advisory services,' 'Bank Holding
14 Company Act of 1956,' 'clients who are natural persons,' 'federal covered
15 adviser,' 'federal covered security,' 'Federal Deposit Insurance Act,' 'Home
16 Owners' Loan Act,' 'investment adviser representative,' 'Investment Advisers Act
17 of 1940,' 'investment advisory business,' 'investment advisory contract,' 'Investment
18 Company Act of 1940,' 'NASDAQ,' 'National Securities Markets Improvement Act
19 of 1996,' 'notice filing,' 'place of business,' 'principal place of business,'
20 'Securities Exchange Act of 1934,' 'securities business,' 'state investment adviser,'
21 'substantial portion of the business,' 'supervised person,' and 'viatical settlement';
22 relating to the title of the Alaska Securities Act; relating to the definitions in
23 the Alaska Securities Act of 'assignment' and 'investment adviser'; relating to
24 implementation of the changes to the Alaska Securities Act; and providing for

STATE OF ALASKA

DEPARTMENT OF COMMERCE AND ECONOMIC DEVELOPMENT

DIVISION OF BANKING, SECURITIES, AND CORPORATIONS

TONY KNOWLES, GOVERNOR

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Corporation Section (907) 465-2530

ANCHORAGE
Corporation Information (907) 269-8140
TDD: (907) 465-5437

March 31, 1999

The Honorable Norman Rokeberg
Alaska House of Representatives
State Capitol Room 24
Juneau, AK 99801-1182

APR 01 1999

Dear Rep. Rokeberg:

Re: CSHB 83(JUD) Various Amendments to the Alaska Securities Act (AS 45.55)

We appreciated the bipartisan support expressed on the floor on March 31, 1999, for the contents of HB 83 and what it is trying to accomplish. We regret that discussion of the title change slowed down the progress of the bill. The purpose of this letter is to urge you to vote for passage of HB 83 as amended on the floor, and to send it on to the other body for its consideration.

The title change, drafted by Legislative Legal Counsel and adopted on the floor, has been reviewed by the division and the Attorney General's office. In our opinion, the new title accomplishes the objectives of the old, longer title. We understand, and have made clear all along, that the objective is to limit the bill's vulnerability to amendments unrelated to securities amendments, but we acknowledge that no title can guarantee a bill is "bullet proof." We believe the amended title serves the same purpose of the longer title, and we urge you to vote to pass HB 83, without notice of reconsideration.

We need time to work with the other body as it considers HB 83, and we are concerned that further delay will make it difficult to get the bill through this session. As you know, we must pass legislation bringing our Act into compliance with federal law by October 1999 to preserve our authority to continue to collect annual notice fees totaling between \$4-\$5 million. Please call us if you have any questions.

We ask for your support of this important legislation. Thank you.

Yours truly,



Franklin T. Elder
Director

A M E N D M E N T

OFFERED IN THE HOUSE

BY REPRESENTATIVE ROKEBERG

TO: CSHB 83(JUD)

- 1 Page 1, line 1, through page 3, line 1:
- 2 Delete all material.
- 3 Insert ""An Act relating to the Alaska Securities Act of 1959; and providing for
- 4 an effective date.""

ALASKA STATE LEGISLATURE

HOUSE LABOR AND COMMERCE COMMITTEE

Representative Norman Rokeberg, Chairman
Representative Andrew Halero, Vice-Chairman
Representative John Harris
Representative Lisa Murkowski
Representative Jerry Sanders
Representative Tom Brice
Representative Sharon Cissna



State Capitol
Juneau, AK 99801-1182
Telephone: (907) 465-4954
Fax: (907) 465-2040

MEMORANDUM

TO: Representative Pete Kott, Chairman
House Judiciary Committee

FROM: Representative Norman Rokeberg, Chairman
House Labor & Commerce Committee

DATE: February 23, 1999

RE: HB 83
Alaska Securities Act

Norman Rokeberg

Yesterday evening, the House Labor and Commerce Committee adopted a CS for HB 83 and passed the bill from committee. The bill's next referral is House Judiciary.

I would request that a hearing be scheduled for this legislation. The Division of Banking, Securities & Corporations will be delivering to you a packet containing fiscal note information, letters of support, CSHB 83 (L&C), sectional analysis and other documentation.

Attached are the following:

1. Sponsor Statement
2. Other letters not included in the Division packet
3. Cover letter from me to the Labor & Commerce Committee members indicating the change in the CS.

As this legislation is time sensitive (Alaska must adopt provisions this year in order to prevent loss of \$4-5 million in revenues), I would request that this matter be promptly scheduled before your committee for a hearing.

If you or your staff have any questions about this bill, you may wish to contact Terry Elder, Director, Division of Banking, Securities & Corporations, Department of Commerce & Economic Development, at 465-2521.

cc: Terry Elder (w/out attachments)

ALASKA STATE LEGISLATURE

HOUSE LABOR AND COMMERCE COMMITTEE

Representative Norman Rokeberg, Chairman
Representative Andrew Halcro, Vice-Chairman
Representative John Harris
Representative Lisa Murkowski
Representative Jerry Sanders
Representative Tom Brice
Representative Sharon Cissna



State Capitol
Juneau, AK 99801-1182
Telephone: (907) 465-4954
Fax: (907) 465-2040

SPONSOR STATEMENT

CSHB 83 (L&C)

ALASKA SECURITIES ACT

House Bill 83 would amend the Alaska Securities Act to bring it in line with the October 1996 federally adopted National Securities Markets Improvement Act (NSMIA). Two major impacts from NSMIA on Alaska are preemption from registration of a new class of securities, Federal Covered Securities, and changes to registration requirements of Investment Advisers and their agents.

Federal Covered Securities, for the most part mutual funds, are no longer required to register in Alaska. However, in an attempt to have a revenue neutral impact on the states and to preserve local investor protection, **congress allowed the states to require Notice filings and fees.** NSMIA provides a three-year window for the states to amend their statutes to provide for notice filings and notice fees or lose the authority to require them. **Without this legislation by October 1999, Alaska would lose between \$4-5 million in annual revenue funds for the purpose of investor protection.** Over 40 states already have passed similar legislation.

NSMIA also altered the registration and regulation of investment advisers. Investment advisers were previously registered with the Securities and Exchange Commission (SEC) and each state in which they offered their services. NSMIA created two kinds of advisers: Federal Covered Advisers, those who manage assets in excess of \$25-30 million, must register with the SEC; and State Investment Advisers (SIA) that must register with the states. States may require Federal Covered Advisers to file a notice and pay a notice fee in order to provide services in the state. Although Federal Covered Advisers are exempt from registration, the states retain regulatory authority over them for violations of the anti-fraud provisions of state law. Finally, NSMIA allows the states to require registration of the representatives of Federal Covered Advisers, who actually provide the investment advice, if they have a place of business in the state.

The changes in federal law require significant amendments to the Alaska Securities Act. These amendments must provide for Federal Covered Securities, Federal Covered

Advisers, Investment Adviser Representatives, and Notices and Notice fees. Provisions must also be added to specify fraudulent and unethical behavior that may lead to action not only against a registered person but now, also against a person who filed a Notice in Alaska. Language for the amendments was, for the most part, drafted by the North American Securities Administrators Association (NASAA), an organization of state securities regulators (members also include Mexico and the provinces of Canada). Division staff also worked with industry in developing this legislation. The Investment Company Institute (representing the mutual fund industry), the Investment Counsel Association of America, Inc. (representing the investment adviser industry), and the Institute of Certified Financial Planners (representing about 14,000 CFP licensees in the United States, including 16 in Alaska) have provided written support for the legislation. In addition to NSMIA changes, other proposed amendments would improve access to the capital market without weakening investor protection.

This legislation is essential to continue the State's ability to collect between \$4-\$5 million in fee income and to provide investor protection to Alaska investors who use the services of broker/dealers or investment advisers. Without this legislation, State Investment Advisers essentially would be unregulated, since they are no longer registered with the Securities and Exchange Commission. Not only is time of the essence, but we believe the NSMIA amendments and the other improvements described above will improve investor protection and issuer access to capital.

ED2:2/23/99

Gwaltney & Gwaltney, Inc.

FEB 19 1999

f a c s i m i l e t r a n s m i s s i o n

To: Representative Norman Rokeberg
Company:

From: Jack Gwaltney
Producer:
Fax Number: 907-561-4489
Business Phone: 907-561-7468
Internet: /http://alaska.net/~ggi/
Address: 701 Sesame Street, Suite 200
Anchorage, Alaska 99503-6641

Pages: 7
Date/Time: 02/19/99 05:03 PM
Subject:
Document Number:

Message: Representative Rokeberg here is the outline I followed in the teleconference today. Also I have included additional information just received from Future First. Thanks for taking time out of a very busy schedule to let us discuss the most important issue.

Chairman Rokeberg and Members of this Committee. Thank you for the opportunity to discuss HB 83 and recent requirements and allegations from the Division of Banking and Securities that is adversely affecting commerce and the consumers of Alaska.

My discussion today partially deals with what I feel is a constitutional breach of rights. Further, I am somewhat incensed by the implication that I have broken a statute that hasn't even been put in place and that "formal action...will be held in abeyance pending...response." If it turns out that legislation passes which makes viatical investments a security you can rest assured I will never sell another viatical. To have the specter hanging over my head that I could be charged with criminal action is quite alarming.

When I first spoke to Mr. Salveson, of the Division of Banking and Securities, whom I called after one of our agents received a phone call to cease and desist, I agreed to also cease and desist until as he put it, "We can get this thing straightened out." Now comes a letter indicating I might be charged with a violation of the Alaska Securities act, and that I am required to submit the names of clients and many other documents.

The definition of Viatical has most definitely not been addressed by statute in this and many other states. Of those States which have classified the

product, all have opted for a definition in favor of being guided under insurance laws not securities. The legislature in Alaska can choose to classify the product as it wishes, though it looks likely they will be the only one of the few states that have opted in the direction that HB83 seems to be heading on this issue.

It is my understanding, the state of Florida has enacted legislation that has served as a model to many other states. One of the main questions at issue with the division of Securities and banking is that they consider Viaticals as an investment contract. Thus far Viaticals have been viewed as personal property similar to real estate. In real estate a purchaser is exchanging money for property of value. This represents a fixed value not the definition of a security. Also at issue is the fact that most policies are sold in fractional amounts, which usually constitutes several parts of the face value, [or death value].

I have provided Representative Rokeberg additional information on this subject.

The Future First Viatical settlement program does not meet the definition of a security under SEC v. W. J. Howey Co., 328 U.S. 293 1946. The

Supreme court under section 2[1] of the Securities Act defined an investment contract "as an investment of money undertaken with the expectation of profit, whose profits are derived solely from the efforts of others with existence of a common enterprise." The assertion that Viatical settlements require an investment of money with the expectation of profit cannot be argued. We can easily argue, however, and it seems apparent to reasonable people, that "profit derived solely from the efforts of others," and "existence of a common enterprise" remain definitively excluded. Further, viaticals do not place principal at risk and provide a guaranteed return, subject to carrier solvency, which is a separate issue addressed under Title 21 of Alaska Statutes, and viaticals have not been deemed securities by the SEC, which seems to carry as much weight as any argument I can imagine.

My immediate concern is the arbitrary application of a cease and desist order on a product which is not addressed in any current statute or regulation, and to my understanding and research is only now pending definition. One of my associates has performed a word search on what I believe are the statutes relating to both Titles 45 and 21, and the term

"viatical" is not found. It appears to me that the allegation that these products conform to the investment securities act seems to be a matter of opinion until it is defined by statute.

Issuing a cease and desist order without defined regulatory authority seems to be to be a classical breach of constitutional rights. It is my understanding that "regulators" exist to protect the public interest and welfare. Regulators protect the public at large from unscrupulous providers and inappropriate products. The sale of viaticals, at present, represents no such threat to public welfare. These products have been sold for a long time, and in my experience, we have yet to have a single consumer complaint in Alaska. Consumers are now unable to exercise their right to purchase these products.

During a similar controversy over Surplus Lines with the Division of Insurance, the Division solicited advise, counsel, and testimony from numerous sources and began issuing bulletins on findings. A subsequent law was promulgated and enforced with a defined inception date and penalties for non-compliance. This was a reasonable approach to the situation. During the fact finding period, no producers were held to a

standard or law that "might" be passed. They dealt only with what was, then offered a period of time to gain compliance after the law was passed. Do these products need to be regulated? My opinion is yes, most definitely. But I feel they are reflective of insurance products much more than securities or investment products. Again, Representative Rokeberg is in possession of preliminary information that will support this position. Even so, in the absence of statutory regulation, we the public can not be held accountable for laws that do not exist.

Please note, without question if HB83 passes in its current form, we will comply with all appropriate law and statute just as I have with insurance law for the last thirty-eight years without incident, allegation, or consumer complaint.

To summarize, I am complying with the cease and desist order, despite the fact I feel it is grossly inappropriate. I will follow this testimony with additional correspondence to prove my point for Division of Insurance regulation.

Ladies and gentlemen, thank you for your attention and the opportunity to participate in this hearing.

**FutureFirst**
FINANCIAL GROUP

OFFICE OF THE PRESIDENT

February 19, 1999

Jack,

In reference to our phone conversation this afternoon, I will re-cap some of the key points of issues regarding regulation. It is extremely important to understand the intent or purpose of regulation before modeling any legislation on an industry.

In 1996 the Florida Department of Banking and Finance investigated all activities of Viatical Settlement Funding Companies and found no investment concerns with Future First Financial Group. They reviewed our material and we basically never heard from them again. Soon after, the Department of Insurance notified us of their intent to regulate Viatical Settlements through their department. As such, Future First Financial Group is a licensed Viatical Settlement Company in Florida. The Department has also monitored our business practices in other states in their recent audit of our program. In accordance with this license we must agree to audits at the discretion of the Department. The audit selects a random sample of policies from all states to test our procedures for purchaser placement and Victor payment. We are also required to furnish audited financial information and current financial information to include the mandatory deposit requirements of the Department. Florida has put together a good program and several states may be modeling their programs after the Florida program.

Like Florida, many of the states will initiate some sort of investigative process through the state banking side, only to find that the Department of Insurance is better suited to regulate the industry. Lobbying for regulation has never been from the policy purchase side, but has instead been from the sellers' side. Most of the concern for a need to regulate was because many of the policy sellers were being taken advantage of. The policyholders were changing ownership and beneficiary information only to receive partial payments from brokers. Delays in payments only led to policyholders dying before receiving full payments with all the extra money remaining with the brokers. The intent of regulation was to protect the policy sellers and in turn has included regulation to monitor both sides of the transaction.

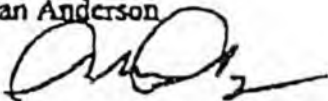
Following the history behind attempts to make Viatical Settlements a security, the Securities and Exchange Commission (SEC) has been unable to sue for this ruling. Additionally, appeals have been unsuccessful. The concept of "fractionalization" came originally from the SEC vs Life Partners cases. Years ago, Life Partners made themselves the owners and beneficiaries of the policies and their investors were given beneficial interest in this pool. Although the SEC made valid arguments that the success or failure of the investment depended on Life Partners being in business in order for investors to receive their payments, they were unable to convince the Federal Government that these investments were securities.

"Fractionalization" was never intended to represent more than one beneficiary on a policy. It was represented as the scenario described above. Not allowing for multiple beneficiaries on an insurance policy violates the rights of individuals to collectively purchase personal property. An insurance policy is nothing more than the personal property of the policyholder, and all policyholders have the right to sell personal property. It is important to not represent securities concerns that don't exist. It's not fair to the individuals selling their policies. It is similar to a homeowner being told they can't sell their home because it's a security.

In no way does any purchase program offered through Future First Financial Group represent a security. Future First does not take purchaser funds and buy policies with unknown expectations. Securities are investments that many times over are dependent on the growth and financial performance of the companies they invest in. The investor never truly knows the final outcome. All purchasers of the death benefits of life insurance policies know from the day they request the settlement what their future value return will be because it is set at life expectancy. I will say it again - all returns are fixed! They will never change! Only the rate of return is not known. This will not be known until the death of the policyholder. Purchasers will not lose their principal. The Trustee of the premium paying escrow fund pays all policy premiums until maturity.

I've run out of time on these comments but if there are any questions please call. Just remember, enforcing securities laws on non-securities is not the answer if the state wants some control over the Viatical Settlement Process. Simply have them model the legislation after Florida. They are tough but fair and have done all the work.

Alan Anderson



Executive Vice President, Future First Financial Group

STATE OF ALASKA

DEPARTMENT OF COMMERCE AND ECONOMIC DEVELOPMENT

DIVISION OF BANKING, SECURITIES, AND CORPORATIONS

TONY KNOWLES, GOVERNOR

333 Willoughby Avenue, 9th Floor
P.O. BOX 110808
JUNEAU, ALASKA 99811-0808
Corporation Section (907) 465-2530
Facsimile (907) 465-3257

Banking & Securities (907) 465-2521
Facsimile (907) 465-2549

ANCHORAGE
Corporation Information (907) 269-8140
TDD: (907) 465-5437

February 18, 1999

VIA FAX AND U.S. MAIL
(907) 297-7363

Jack Gwaltney
Premier Investments and Insurance, Inc.
3510 Spenard Road, Suite 104
Anchorage, AK 99503

Dear Jack Gwaltney:

Re: Future First Financial Group of Ponte Vedra Beach, FL

Reference is made to our conversation of February 17 regarding the program offered through the above sponsor (Future First) for the sale of interests in viatical settlement contracts (the viatical program). This office administers and enforces the Alaska Securities Act (AS 45.55) and it is our opinion that the viatical program, as offered through your agent Escrow Alaska Financial, Inc., is an investment contract security under AS 45.55.990(12) and subject to the registration provisions of AS 45.55.070. Firms and individuals that sell securities must also be registered as broker dealers or agents under AS 45.55.030.

Please immediately confirm to this Division in writing, as the Alaska General manager for the Future First viatical program, that the offer and sale of interests in the viatical program, including all advertising, has been voluntarily stopped. A copy of this letter must be provided to all firms and individuals who were previously authorized to sell the program and a list of those firms and individuals, including address and telephone numbers, must be provided to this office. Also, provide a list of all Alaskan purchasers of the viatical program. If you are offering any other viatical programs, disclosure to this office is required.

If you are aware of any other (non-affiliated) firms or individuals offering the Future First viatical program to Alaska residents, please identify.

As discussed, provide a copy of all written materials provided to or signed by an investor. If not set out in the written materials, disclose to this office supplementally the selling compensation structure of this offering. Provide a copy of any scripts used in telephone sales presentations and if none, so state. Provide a copy of any attorney's opinion, letters or court cases relied upon that supports your position that the viatical program does not constitute a security under AS 45.55. Forward a copy of any financial statements for Future First and if none, so state.

Mr. Jack Gwaltney

-2-

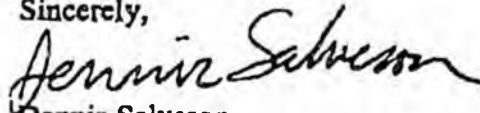
02/18/99

Please be advised that the advertisement of "Returns up to 42% Guaranteed" (emphasis added) in the newspaper constitutes a public offering and that, even in the event a securities registration is subsequently made effective, is strictly prohibited by 3 AAC 08.900(2). Identify the publications used, provide a list of all dates of publication and a copy of any advertising or notice used to promote the viatical program by you, Premier Investments and Insurance, Inc, or any agent or affiliate.

You are required to immediately respond to this letter under AS 45.55.910 and state whether or not you, Premier Investments and Insurance, Inc and its agents and affiliates agree to voluntarily cease and desist from offering or selling the Future First viatical program to Alaska residents. A response to the other information items is required within 10 days. A decision whether to take formal action under the Alaska Securities Act will be held in abeyance pending your full response. If we determine subsequently that there were ongoing activities that violated the Alaska Securities Act after your receipt of this letter, we will treat any such activity as a knowing violation of the Act.

If you have any questions, please feel free to contact me at 907/465-2524. However, only written replies suitable for filing with the Administrator, subject to AS 45.55.160, will be considered as responding to this letter.

Sincerely,



Dennis Salveson
Securities Examiner

Cc: Escrow Alaska Financial, Inc.
J.H. Judy Gopaul, Marg Walker
VIA FAX AND U.S. MAIL

From the desk of
David E. Gwaltney, C.I.C.

6217 Chisigny Street
Anchorage, Alaska 99502
Telephone: (907) 297-7302
Facsimile: (907) 297-7363

Personal Correspondence

e-mail: dave@insuranceok.com

February 19, 1999

Mr. Dennis Salvesson
State of Alaska
Division of Banking
P.O. Box 110808
Juneau, Alaska 99811-0808

Re: February 18, 1999 Premiere Investment Correspondence
Constitutional breach

Dear Mr. Salvesson:

Please accept this correspondence as the first of what I anticipate will be three letters addressing issues raised in your February 18, 1999 correspondence to Jack Gwaltney of Premiere Investments and Insurance, Inc. Mr. Gwaltney has passed your letter on to me as required in your correspondence, and I have ceased solicitation and discussion of the product voluntarily, at least temporarily.

My letter today deals with what I feel is a constitutional breach of rights. Further, I am somewhat incensed by the implication that I have broken statute and that "formal action...will be held in abeyance pending...response." First, the definition of Viatical has most definitely not been addressed by statute in this and most other states. Of those States which have classified the product, virtually all have opted for a definition in favor of insurance offerings, not securities. The legislature in Alaska can choose to classify the product as it wishes, though it looks likely they will be in a vast minority if it opts in the direction that HB83 seems to be heading on this issue. (This will be the subject of my next correspondence.)

My immediate concern is the arbitrary application of a cease and desist order on a product which is not addressed in any current statute or regulation, and to my understanding and research is only now pending definition. I have performed a word search on what I believe are the statutes relating to both Titles 45 and 21, and the term "viatical" is not found. It appears to me that your allegation that these products conform to the investment securities act seems to be a matter of opinion until it is defined by statute. (Without digressing into my next correspondence prematurely, viaticals do not place principal at risk, do provide a guaranteed return (subject to carrier solvency, which is a separate issue addressed under Title 21) and they have not been deemed securities by the SEC, which seems to carry as much weight as any argument I can imagine.)

Issuing a cease and desist order without defined regulatory authority seems to be to be a classical breach of constitutional rights. It is my understanding that "regulators" exist to protect the

Gwalmei & Gwalmei, Inc.
02/19/99

Page 2

public interest and welfare. Regulators protect the public at large from unscrupulous providers and inappropriate products. The sale of viaticals, at present, represents no such threat to public welfare. These products have been sold for more than a decade in the presented format and in my experience we've yet to have a single consumer complaint in Alaska.

Next month will be the twentieth anniversary of my insurance licensure in the State of Alaska. (Incidentally, I've been a Series 7 registered representative since 1984 as well.) Over those twenty years, there have been many concerns over the suitability of numerous products, including a certain class known as "Surplus Lines." Despite the potential public harm or concerns (which are potentially most devastating, by the way, certainly well in excess of viatical sales), the Division of Insurance never issued a cease and desist on the sale of those products. They (the Division) recognized that although additional regulation may be required to fully protect the consumer, the product was still valued and to remove it without cause or notification would place many Alaskan consumers as well as agents and brokers in an untenable position to protect themselves or earn a living.

Your order has done that. Consumers are now unable to exercise their right to purchase these products. Many salespeople are now offering these products for their livelihood, and your order is eliminating their ability to earn a living and provide for their families. Is there a statute that deals with this issue? Will there be State reimbursement? If not, I hope the Attorney General's office agrees with your position, or the State of Alaska will be offering liquidated damages at a time when we (the populace of our State) can least afford it.

In the case of Surplus Lines, the Division of Insurance solicited advise, counsel, and testimony from numerous sources and began issuing bulletins on findings. A subsequent law was promulgated and enforced with a defined inception date and penalties for non-compliance. This was a reasonable approach to the situation. During the fact finding period, no producers were held to a standard or law that "might" be passed. They dealt only with what was, then offered a period of time to gain compliance after the law was passed.

A secondary issue deals with your demand for "...all written materials provided to or signed by an investor." I will not comply with this demand at present for fear of a much larger problem, that being the Federal Privacy Act. As you're aware, by their very nature, the Viatical product deals with individual rights of privacy and terminal medical conditions. Until I can be shown, in writing and at the direction of a federal authority, that releasing this confidential medical information to you is deemed appropriate, my files will remain confidential. I will, however, be happy to provide all non-client specific sales material per your request.

Do these products need to be regulated? My opinion is yes, most definitely. But I feel they are reflective of insurance products much more than securities products. (Future correspondence to substantiate.) Even so, in the absence of statutory regulation, we the public can not be held accountable for laws that do not exist.

You also request information and/or attorney's opinion statements supporting our position on the products themselves. This request for information (supposedly to determine the nature and breadth of our violation), followed immediately by the implication that we have criminally violated Title 45 statutes, seems very close to a request to incriminate ourselves. Last time I checked our legal system, "criminals" were innocent until proven guilty. The burden of proof

Gwaltney & Gwaltney, Inc.
02/19/99

Page 3

does not rest on us – the burden that we have violated a law rests with you. If you feel this statement is an over-reaction, please explain the nature of the cease and desist, and also explain the not-even-veiled threat of further recrimination for non-voluntary compliance with your "request."

Please note that, without question, if HB83 passes in its current form, we will comply with all appropriate law and statute just as I have with insurance law for the last twenty years. I simply see no reason to comply with laws that don't exist nor sit idly while I'm threatened with the removal of my livelihood.

To summarize, I am complying with your cease and desist order, despite the fact I feel it is grossly inappropriate. I will follow this letter with additional correspondence to prove my point for Division of Insurance regulation. I will comply with your request for file information as soon as I'm assured that compliance will not violate or preempt an existing federal statute. And I respectfully request re-consideration of the cease and desist until laws relating to our conduct and product offering have been established.

Regards,



David E. Gwaltney, CIC

P.S. I am writing this letter under personal letterhead given my position for Viatical sales is under a personal agreement. Please note that my current industry positions include President, Principal/Manager and Compliance Officer of Gwaltney & Gwaltney, Inc., President, Alaska Independent Insurance Agents and Brokers, and Property Casualty Representative for the Division of Insurance Continuing Education Advisory Committee. My comments in this correspondence are personal in nature and bare no correlation to those or other positions held.

cc: Rep. Norm Rokeberg (constituent)
Sen. Druc Pearce, (constituent)
Rep. Ramona Barnes (by request)

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Viaticals Not Securities, Court Rules

BY JIM CONNOLLY

Viatical settlements are not securities subject to federal securities laws, a District of Columbia appeals court ruled in a 2-to-1 decision earlier this month.

The ruling in *Securities and Exchange Commission v. Life Partners, Inc. and Brian Pardo* reversed a district court decision handed down in August 1995 which addressed the sale of "fractional interests" in viatical settlements.

Viatical settlements are contracts in which an investor purchases a life insurance policy from a terminally ill person at a discount that can range from 20 percent to 40 percent depending on the life expectancy of the viator, the seller of the policy.

If viatical settlements are not securities, neither are they insurance policies, according to the court opinion which determined that "... a viatical settlement is not an insurance policy, and the business of selling fractional interests in insurance policies is no part of the business of insurance."

The court continued, "LPI's offering does not, therefore, qualify

for the insurance exemption from the federal securities laws, and is not shielded from federal regulation by the McCarran-Perguson Act."

The appeals court reasoned that viatical settlements are not securities because the "profits from their purchase do not derive predominantly from the efforts of a party or parties other than the investors."

Court Also Said That Viatical Settlements Are Not Insurance Policies

The district court had determined that the defendants were selling unregistered securities but that the case rested on a "gray area of securities law."

"We are disappointed with the outcome," said Leo Orenstein, assistant chief litigation counsel with the SEC. At press time, no decision had been made on whether the SEC would take further action.

But, according to Mr. Orenstein, the SEC could request a rehearing en banc by the appeals court. Such

petitions are granted "very infrequently," he said, but in this case, "there is a question of first impression. This is virgin territory."

Other options, he said, include an appeal to the Supreme Court, a rehearing and then an appeal to the Supreme Court, or a decision to let the current decision stand.

"Fractionalized interests are a very smart way to buy viatical settlements and spread risk and return," according to Brian Pardo, current chairman and former president of Life Partners, Waco, Texas.

Within 60 to 90 days, Life Partners "will begin to act as an agent selling fractionalized interests again," Mr. Pardo said. "Now a billion dollars and three years later, we can go back to the original way that we do business."

Speaking for the Viatical Association of America, Melv Eliav, president, said, "we as an industry, are very much concerned that investors, one or many, have a very good understanding of the risks they are taking upon themselves by buying policies." This is particularly true of the small investor, he said.



FutureFirst ★
FINANCIAL GROUP

OFFICE OF THE PRESIDENT

November 5, 1998

The following analysis is provided to educate all concerned parties on the Future First Viatical Program, and how the Securities and Exchange Commission (SEC) may view this program. This analysis is strictly the opinion of Future First Financial Group, Inc. Future First strongly recommends the consultation with private legal counsel on the following position.

From all available information and in our opinion, it is not the intent of the SEC to exercise jurisdiction over Viatical Settlement Companies. Leo Ornstein, assistant chief litigation counsel at the SEC's division of enforcement says the SEC is not opposed to the simple brokering of insurance policies, yet Viatical Companies that do much more are having to 'bare all' to the SEC. To date, only one Viatical Company has been charged by the SEC.

Specifically, the SEC contended that the Viatical Company charged sold fractional interests in insurance contracts, thus constituting a sale of investment contracts subject to federal securities laws. The Future First Viatical Program coordinates the purchase of the death benefits of life insurance policies by direction of a Purchase Request Agreement (PRA). The Purchaser named in the PRA authorizes Future First to act on their behalf to purchase the death-related benefit of an insurance policy. The purchaser becomes a beneficiary of the death benefit of an insurance policy. Future First as well as most Viatical Companies coordinate this exchange of real property in a manner resembling the Real Estate Business. Viatical Brokers (requiring a license in many states) serve as agents for the Viators (sellers), and Viatical Companies (requiring a license in many states) serve as agents for the purchasers. The Future First Program requires an attorney for closing and through this closing the transaction is finalized through the exchange of money (value).

As in real estate all purchasers are exchanging money for property of value. This value is fixed - never to increase or decrease in value. Similarities to real estate are focused mostly on the transaction process not the future value. Investors in real estate base most of their future value estimates on the economy. Viatical Settlements coordinated through the Future First program have a fixed future value, not dependent on the economy.

The Future First Viatical Settlement Program does not meet the definition of a security under *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946) [hereinafter *Howey*]. The Supreme Court under section 2(1) of the Securities Act defined an investment contract as an investment of money undertaken with the expectation of profit, whose profits are derived solely from the efforts of others with the existence of a common enterprise.

Under *Howey*, all Viatical Settlements require an investment of money with expectations of profit. These two points Future First cannot argue. Future First will argue that profits derived solely from the efforts of others and the existence of a common enterprise are not satisfied under *Howey*.

For Howey to be satisfied, Viatical Settlement profits must be derived solely from the efforts of others. In application, the courts have not adhered to a literal interpretation of the word "solely." In *SEC v. International Loan Network, Inc.*, 968 F.2d 1304, 1308 (D.C.Cir.1992), "solely" was relaxed to "predominately." In any case, to satisfy this test, both the "others" whose effort produces profits and the effort itself must be identified. Under the Future First Viatical Program there are many possible "others:" the policy seller, a financial advisor of the seller, the policy broker, a financial advisor to the purchaser, and the purchaser's broker to name a few. The complexity of the settlement and the inability to know just when a person will die, makes it literally impossible to identify "others" and "whose effort" to satisfy Howey.

Common enterprise under Howey is defined in terms of horizontal and vertical commonality. Under horizontal commonality a common enterprise is defined in terms of the relationship between individual investors. A common enterprise exists if investor funds are pooled together, usually with pro-rata distribution of profits or losses. Both forms of vertical commonality define a common enterprise in terms of the relationship between the individual investor and the promoter. Narrow vertical commonality demands that the success or failure of the investor mirror the success or failure of the promoter. The broader form of vertical commonality requires that only the success or failure of the investor be dependent upon the efforts of the promoter. In our opinion, for Howey to be satisfied under common enterprise, both horizontal and vertical commonality must exist. It is difficult to argue against horizontal commonality, but neither forms of vertical commonality are present under the Future First Viatical Program. The success or failure of Future First Financial Group, Inc. has no correlation with the success or failure of a Viatical Settlement under the Future First Program. As described earlier, the value of the purchase is fixed at closing, never to increase - never to decrease. It is simply an exchange of real property finalized through a closing.

Beyond Howey and the SEC, Future First Financial Group, Inc. has developed the finest Viatical Program in the industry. Years of research and experience has uncovered the good and the bad in the industry, and Future First has capitalized on them all. Since day one, the Future First Viatical Program has become the model for the industry.

Probably the number one concern for all purchasers is: *who has access to purchaser funds?* Simply answered, *no one at Future First!* Future First is only authorized to make deposits. An independent CPA serves as trustee on the account, and only they have the authority to transact funds out of this account. This trustee is bound by a Trust and Escrow agreement limiting them to specific transactions at the direction of a law firm, and is personally covered by a Fidelity/Surety bond, providing third party protection of all purchaser funds.

The Future First Viatical Program has been designed to allow for as much choice as possible in the purchase process. As an agent for the purchaser, Future First is bound by the PRA to arrange the purchase of the death benefits of insurance policies under fixed program returns of their choice. The purchaser knows and agrees upon all settlement programs prior to closing.

After closing, the greatest concern for the purchaser is insurance policy premium payments. Some companies will not pay premium payments beyond their determination of life expectancy.

This should be a warning sign that these companies may not be placing appropriate life estimates with purchaser funds. The Future First Viatical Program, guarantees in writing under the PRA, to pay all insurance policy premiums to maturity, no matter how many years beyond the program the seller lives! This is accomplished through the Fidelity Viatical Special Trust. Advance premium payments required of the settlement at closing are deposited into this account. This is the sole purpose of this account, and bound by a Trust and Escrow agreement, this money can only be used for premium payments. All excess funds must remain in this account, earning interest over time, existing independent of Future First, to pay all policy premiums until maturity. Although this account may be over-funded, over-funding will allow for perpetual growth in the account even as individuals live beyond life estimates.

Future First Financial Group is a proponent for purchaser / investor protection. Protection may be in some form of regulation, but not at the expense of the entire industry. Regulation has almost ruined some industries, where de-regulation has been the savior. Any attempt to regulate a person's right to sell their personal property should not be approached. Most of the states developing legislation to regulate Viatical Settlements are following the lead of other states with legislation already in place. They are pushing the regulation through the insurance departments, with most of the emphasis on protection of the seller. Although this is an extremely important area to place emphasis, the protection of the purchaser / investor has received less attention.

This is not a reason for regulation by means of making this purchase of real property a security! It means that the insurance departments need to model the Viatical purchase process in some form similar to the Future First process. Regulation must not complicate this process and transform this process into something it's not. It is nothing more than the exchange of real property!

The future of this industry is not tied to more regulation. It is tied to legitimate claims of fixed future returns. The best 'statistical guessers' in the world will be wrong more times than right given a shorter time to be right. This is not magic, it's just common sense. Time is the key element to future events. This is why time is such a critical factor of the unknown. With more time, the unknown may be more predictable. Therefore, we must not be so naive and force naivete on purchasers / investors by claiming to be of a higher power when it comes to estimating life expectancy. It is then reasonable to assume that Viatical Companies should have a much better track record on longer-term programs than shorter-term programs. No one really knows when a person will pass away. What we do know is that one day they will and the purchaser / investor will receive their promised fixed return as long as the Viatical Company or Third Party Trust has not let the policy lapse. Based on what the industry is offering in the competitive market for fixed returns, even a Viator doubling their life estimate presents an extremely competitive and risk averse return.

All of the employees, managers, and officers of Future First Financial Group, Inc. welcome you to the finest Viatical Program in the industry.

STATE OF ALASKA

DEPARTMENT OF COMMERCE AND ECONOMIC DEVELOPMENT

DIVISION OF BANKING, SECURITIES, AND CORPORATIONS

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February 19, 1999

The Honorable Norman Rokeberg
Chairman, Labor & Commerce Committee
Alaska House of Representatives
State Capitol Room 24
Juneau, AK 99801-1182

FEB 19 1999

Dear Chairman Rokeberg:

RE: Information on viaticals

At the hearing of the House Labor and Commerce Committee on Wednesday, February 17, 1999, you asked that we provide you with some further information about the issue of viaticals as securities and various state responses.

In the May 11, 1998 issue of *BestWeek* (pp. 13-14), it was reported that the founders of Mutual Benefits Corp., a viatical settlement firm in Miami, Florida agreed to pay \$950,000 to settle charges brought against the firm by the U.S. Securities and Exchange Commission (SEC) for allegedly misleading investors. The article states that this was the first case concerning viaticals in which the SEC achieved full injunctive and monetary relief. In the previous December, the SEC lost a battle in the District of Columbia Appellate Court against Life Partners Inc., a Waco, Texas viatical settlement company (I believe the cite is 318 U.S. App. D.C. 305, 87 F.3d).

In the SEC v. Life Partners Inc. case, the appeals court found the viatical interests were not investment contracts based on its analysis of the activities of the company both before and after the investors' money was received. Although the decision is not binding outside of the D.C. area, it caused the SEC and state regulators considerable concern as the growth of the industry has been accompanied by a growth in complaints about the marketing of these interests to investors. The Mutual Benefits action shows that the SEC continues to look at this issue on a case by case basis.

In the November 2, 1998 issue of *Investment News* (pp. 1 and 33), a number of investor complaints are described, and the article states that at that point "...only Maine has formally put life insurance agents on notice that viaticals are subject to state securities laws and that all sales agents be licensed." Sales agents may not be insurance agents, of course. The North American Securities Administrators Association (NASAA) has created a task force to follow developments

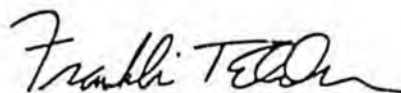
February 19, 1999

in this field, and individual states are beginning to take actions to overcome the chilling effect SEC v. Life Partners, Inc. had on regulatory efforts. In addition to Maine, Missouri has introduced HB 492 and Oregon has introduced SB 285 to add interests in viatical settlements to the definition of securities in their securities statutes. Recently, we have had communication with a number of other states that are considering adding these interests to the definition of a security. Those state include North Dakota, South Dakota, Ohio, California, and Arizona. Arizona attempted legislation a year ago, but industry opposition killed the bill. We do not know what specific proposals were introduced there, or what specific objections were raised.

We would not be surprised if the viatical industry prefers not to have these interests added to the Alaska Securities Act. We have no objection to the proper marketing of these securities, but experience both here in Alaska and elsewhere shows a need to protect investors from improper marketing of these securities by unlicensed agents.

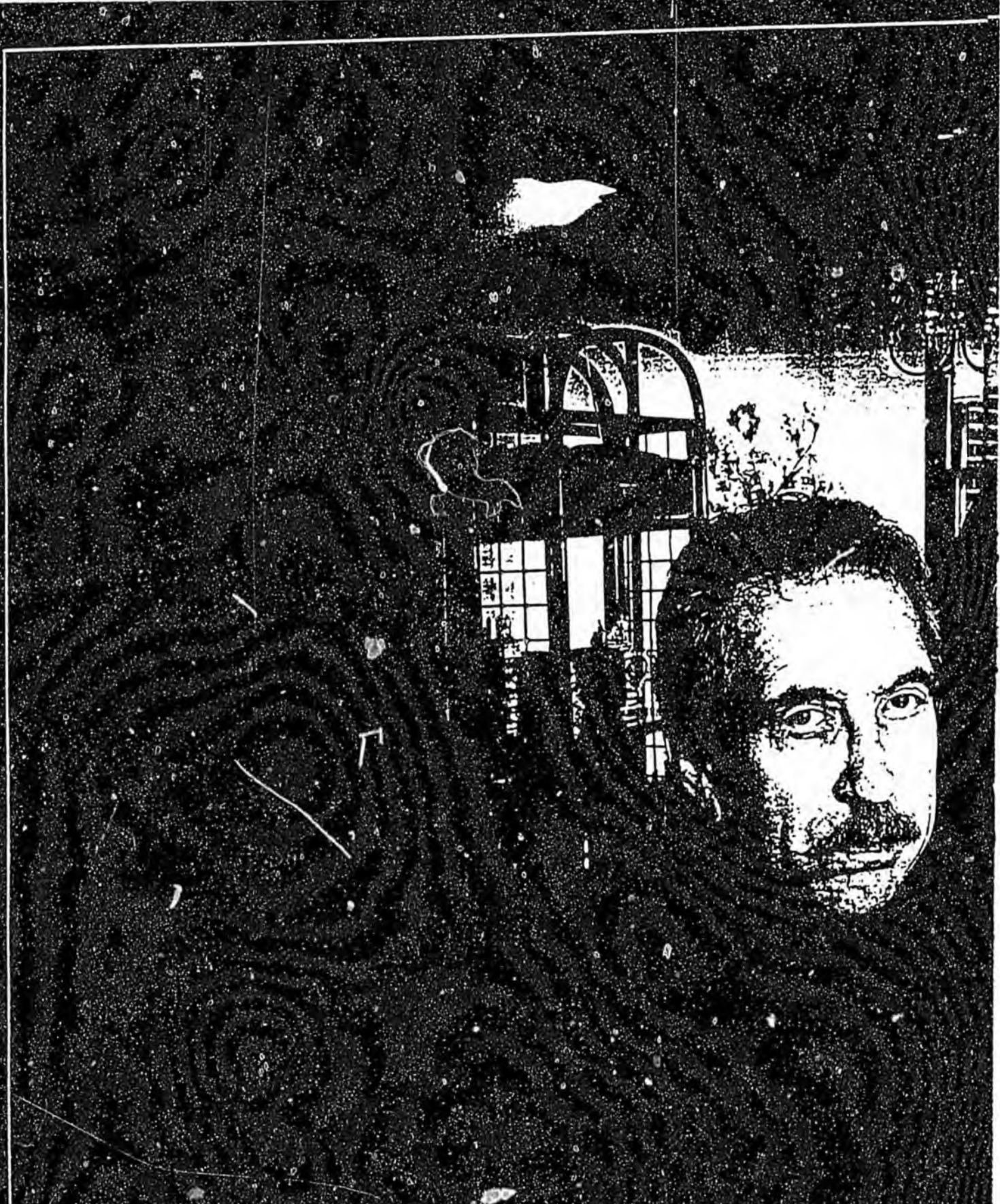
We hope this letter is responsive to the chairman's question. For your added information, we have attached a copy of an article on viatical investments appearing in the March issue of *Kiplinger's Personal Finance Magazine*.

Yours truly,



Franklin T. Elder
Director

**THE FOLLOWING PAGES MAY
NOT FILM LEGIBLY BECAUSE OF
THE POOR QUALITY OF THE ORIGINAL**



Jerry Warner and his mother, Vera, invested more than \$45,000 in viatical settlements, then received an early payoff when the viatical company sold its policies. They lost more than \$15,000.

DE WAT

By buying life insurance on
of the terminally ill, investors
thought they were getting a
payoff from a humanitarian
investment. Now they're waiting
for the policyholders to die.

By Robert R. ...
1992 ...



For more than a decade after her husband died, Betty Paxton barely touched her savings, other than to reinvest CDs and savings bonds when they matured. But two and a half years ago, Paxton, then 78 and worried about her health, filled out a card she'd received in the mail requesting more information about probate and estate planning.

A few weeks later, an insurance agent arrived at the door of her Ohio apartment. Initially he sold Paxton an annuity. Then, a little over a year later, the agent was back. He urged her to cash in her savings bonds and buy a viatical settlement—a life insurance policy that a terminally ill person sells to receive part of the death benefit early. The agent told Paxton she would earn a guaranteed 24% by investing in policies of people expected to live 24 months or less. When the insured person died, she would receive the death benefit.

Paxton felt uncomfortable about profiting from someone's death, but the agent reassured her that her investment would give terminally ill people money to help them live during their final days. He said *60 Minutes* had called viaticals "a perfect no-risk investment." The agent would not leave, Paxton says, until she promised to sell her savings bonds and buy a viatical investment—even though she'd lose four months of interest by cashing in early.

As Paxton's CDs and savings bonds matured over the next five months, she bought a total of \$33,000 worth of viatical-settlement investments on three people who, she was told, had life expectancies of 24 months or less.

For several years, viatical-settlement companies have been pushing these investments as a risk-free way to get a guaranteed return. With viatical settlements, terminally ill patients sell their life insurance policies before they die and get a fraction of the death benefit in cash. The policy remains in force and investors can buy portions of the policy at a discount to the death benefit. The investors become the beneficiaries and get their share of the full death benefit when the insured dies or, in the industry's terms, when the policy "matures."

Longer life expectancies aren't the only problem. Quick-buck artists have poured their efforts into selling viatical settlements (which are unregulated as investments), concentrating on elderly investors looking for a higher return on their fixed-income investments. Several viatical companies and their owners have been charged with fraud or misrepresentation; two such cases involved nearly \$100 million each. More than 35 state securities regulators are now investigating viatical-settlement companies, estimates John Ellis, securities counsel with the Missouri Securities Division.

"There's a lot of fraud almost inherent in these," says Bill McDonald, assistant commissioner of the California Department of Corporations' enforcement division. "Viaticals are unique because legally you're not entitled to know much about the insureds," he says. "You're completely at the mercy of the broker."

Now that several years have passed since a lot of policies were sold and the payoffs aren't forthcoming, the industry is "right on the edge of collapsing," says Roger Walter, general counsel for the Kansas Securities Commissioner and chairman of a national task force of securities regulators who are investigating viatical investments. The national organization of insurance commissioners is also searching for ways to regulate viaticals.

We had little trouble finding people who invested in

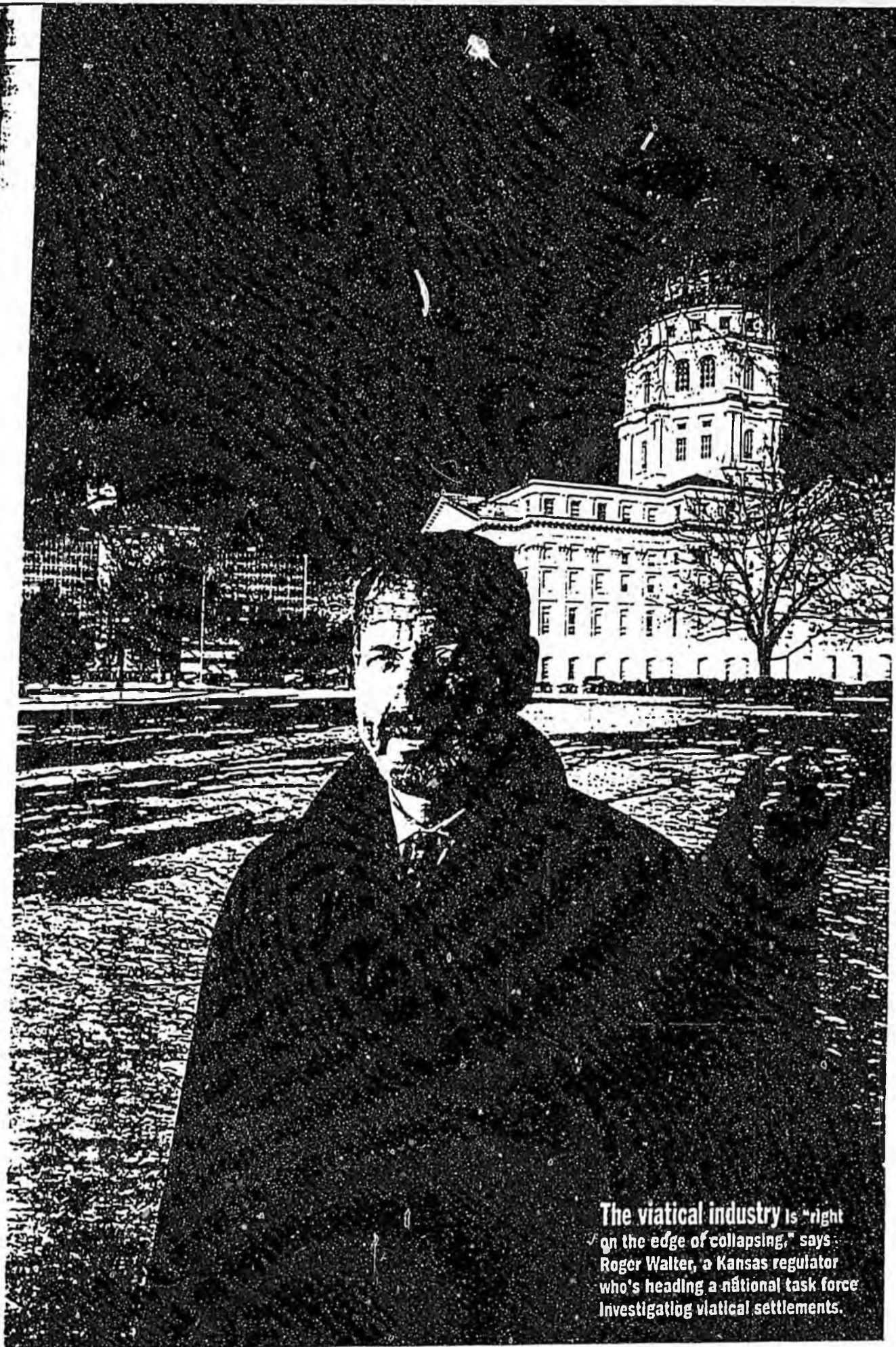
Quick-buck artists have poured their efforts into selling viatical settlements, concentrating on elderly investors looking for a higher return.

Viatical-settlement investments really took off when terminal AIDS patients began selling their policies to viatical firms in the early 1990s. But when protease inhibitors and other medical advancements started extending patients' lives, viatical investors found themselves waiting longer than expected for a payout. Many are still waiting. Others, such as Jerry Warner of Independence, Mo., and his mother, Vera—who together invested more than \$45,000 in viatical settlements—found themselves with an unexpected payout, but for much less than they'd put in. They lost more than \$15,000 between them.

viatical settlements and now wish they hadn't. Some have lost thousands of dollars; others haven't seen a cent yet because the policyholders have lived years longer than expected. Many investors are risk-averse seniors—a prime target of viatical sellers—who, like Paxton, have cashed in their savings and are still waiting for their money.

Some were told lies or half-truths and strong-armed. When they expressed reluctance to participate in this admittedly morbid investment, they were assured that viatical settlements are humane instruments that give the terminally ill much-needed cash. What they weren't told is

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The viatical industry is "right on the edge of collapsing," says Roger Walter, a Kansas regulator who's heading a national task force investigating viatical settlements.

Some investors feel intimidated by the salespeople and fear they'll never get their money back if their names appear in print.

that there are actually more investors than there are policies. In some cases, investors have had to wait for several weeks before the viatical company could find policies for them to buy. At least one viatical company has urged terminally ill people to hide their medical conditions from life insurance companies so they could buy policies that the company could immediately resell to investors. And several insurers are willing to buy back policies themselves or offer to pay death benefits while policyholders are still alive, so terminally ill people aren't dependent on individual investors for cash.

Almost everyone we talked with is embarrassed and angry. Some are intimidated by the salespeople and afraid they'll never get their money back if their names appear in print. Among the investors we interviewed, only Jerry and Vera Warner agreed to let us use their real names.

When Betty Paxton's son learned about her viatical investments, he was suspicious. After he and his financial adviser did some digging, the suspicion turned to anger.

Paxton's son discovered many risks that his mother hadn't been warned about—such as that the policyholders could outlive their life expectancies and leave Paxton without access to her money for years to come. (The insureds could live even longer than the 80-year-old Paxton.) If she tried to resell the policies before the policyholders died, she'd probably get 25% to 50% less than her original investment—if she could find a buyer.

The salesman didn't explain that the 24% total return would become a smaller annualized return each year the insured people lived beyond their life expectancy—or

that Paxton could even be forced to pay additional premiums to keep the policies in force. And if anyone who invested in the same policies didn't pay the premiums, the policies could lapse and she'd lose her investment.

Paxton wasn't given any medical information about the policyholders until after she had invested her money. Because the policyholders wanted privacy, there was no way she could get a second opinion and verify that their life expectancies were reasonable.

Paxton's son and his financial adviser even looked up the full *60 Minutes* quote and discovered it was taken out of context from a 1995 program about AIDS—before medical advancements extended patients' life expectancies—but none of the people Paxton invested in had AIDS.

After the Ohio Department of Insurance told Paxton's son that the agent had been the subject of several complaints for misrepresentation, he sent certified letters to Beneficial Assistance, the Baltimore, Md., company that sold the policies, asking to have his mother's money refunded because this was clearly an unsuitable investment for her. So far, he has received no response.

Perhaps the biggest drawback of viatical investments is that the return depends on when the policyholder dies. Miscalculations are inevitable, but some companies have deliberately filed false medical reports. Life Options International, a Tuscaloosa, Ala., company that drew close to \$5 million in investments from 250 Missouri residents, was issued a cease and desist order by the Missouri Commissioner of Securities, which charged the company with misrepresenting insureds' medical conditions and falsely underestimating

Big commissions, big compromise

MARK CORTAZZO, a financial planner in Denville, N.J., receives at least one letter a month trying to recruit him to sell viatical investments. The companies usually offer him 7% to 12% of the investment amount. "It would take me ten years with a client to earn the same money these people make from selling one viatical," says Cortazzo.

But Cortazzo won't sell viaticals. And he wonders whether many of the salespeople, who

don't need to be licensed in most states, really understand how the investments work. One solicitation for prospective salespeople, for example, includes a "Pyramid of Safety," which shows viatical settlements, insurance and annuities on the bottom layer as the safest investments. CDs and money-market accounts are listed on the next layer up, as riskier investments.

Chris Gemignani, the lawyer for a life insurance agent who

was offered 15% commissions to sell viaticals, researched the business for his client and discovered that so many people were taking a cut of the sale that there was little money left to help the terminally ill person. Additional money is used to pay premiums and to track the insured (if you can't find the insured and don't get a death certificate, there's no payout). His client decided not to bite.

Some viatical salespeople

have been trying to be responsive to their clients. Karl Hanke, who sold half a million dollars in viaticals to about 50 of his clients from 1995 to 1997, probably earned about \$40,000 in commissions, but now he calls the investments a "service nightmare." He's tried in vain to get information for clients who expected payouts several years ago. "The companies won't even take my phone calls," he says. He doesn't sell viaticals anymore.

life expectancies. In one case, an independent doctor estimated the insured's life expectancy to be four to ten years, but the company told an investor it was 36 to 48 months.

Patty Norton was one Life Options investor. As the 55-year-old Missouri woman's certificates of deposit matured in late 1994 and early 1995, she was disappointed with her investment options. "When the CDs came due, the new rate was just zilch," she says. A broker recommended that she buy viaticals instead. He told her that even if the person didn't die after the second or third year, the company would still offer to give back her money with a small return; but she'd get the big bucks if she waited until the person died. He also told her the policies were paid up—no matter how long the policyholders lived, she wouldn't owe any money to pay premiums. Both statements were untrue.

Within a year, Norton owned portions of seven policies from Life Options. Some promised a 10.5% return when the insured died, which she was told should be in about six to 12 months. Others promised 56% returns on life expectancies of two to three years and 95% for life expectancies of three to four years. "You think that didn't look good?" she says.

One of the insureds did die a year after Norton bought the policy, and she made \$525 on her \$5,000 investment. But she had to give back her \$500 gain on another \$5,000

because medical advancements had extended the life expectancies of the insureds, the company needed to sell the policies as soon as possible and had accepted an offer from the highest bidder. "They didn't give us any choice," says Warner, who hadn't been warned that Aide the Living could sell the policies for less than the invested amount.

About 70 Missouri residents had invested more than \$4 million with Aide the Living, the Missouri Securities Division discovered. It charged the company with misrepresentation and issued a cease and desist order prohibiting it from doing business in the state. Other states have also issued orders against the company.

Anne Jones's nephew—a viatical salesman—convinced her that she'd get better returns from viatical investments than she would from an annuity. At his urging, she cashed out a recently purchased annuity, paid \$24,000 in surrender charges and bought portions of insurance policies on seven terminally ill people. By the end of 1995, she had invested more than \$214,000 in viatical settlements. She expected to receive \$309,000 when the people died—which she was told should be no more than 24 to 36 months later.

Jones received one payout, for \$24,000. Jones, who is 70, still has nearly \$193,000 tied up in the other six policies. One person, who had a 12- to 18-month life

After five years, Janice Cannady hasn't received a payout. Meanwhile she's been diagnosed with Alzheimer's disease and her husband has died.

policy. According to Norton, Life Options said that the insured's family claimed he didn't have the right to sell the policy and wanted the insured's son to receive the death benefit. The company told her she could get back her original investment, but she'd have to return her gains to avoid a lawsuit.

Four years later, the five remaining insureds are still alive. Norton has about \$50,000 in the viaticals but has not received any updates from the company.

Sometimes the life-expectancy problem can turn returns into big losses. In 1996, Jerry Warner, 53, of Independence, Mo., purchased part of two life insurance policies belonging to terminally ill people for nearly \$19,000. His 76-year-old mother, Vera, from Lake of the Ozarks, Mo., invested \$27,000. Vera, who had had a friend who died of AIDS, says, "I just wanted to invest my money and thought, why not help someone at the same time?"

The Warners were told the patients were expected to live about three to five years. They both thought the lump sum they'd receive after the patients died would equal a 12% to 20% return for each year.

More than two years later, their investments unexpectedly paid off—but at far less than they had invested. Jerry received a check for \$12,000—nearly \$7,000 less than the amount he had invested. His mother lost nearly \$8,700. The company, Aide the Living, told investors that

expectancy in 1995, is still alive 43 months later. The 15% return Jones was to receive on that policy has dwindled to less than 4.2% per year—and is still falling.

The viatical company recently sent her a letter claiming that, because the insureds had outlived their life expectancies, she'd either have to pay premiums to prevent the policies from lapsing or sell them back to the company for half of her original investment. If she did that, she'd lose more than \$96,000.

Despite the company's threat to start charging her for premiums, the insurance companies told the Kansas Securities Commissioner's office, which is investigating her case, that premiums had been waived on some of the policies because the policyholders were considered disabled.

There's another complication. The viaticals are in an IRA, and since Jones turned 70½ recently, she needs to begin taking withdrawals. Other than the \$24,000 payout she received, the rest of her IRA money is trapped in the viaticals. Any required distributions she can't take will be considered excess accumulations and subject to a 50% penalty for every year they're not distributed.

The uncertain wait for the payoff could have more dire repercussions for Janice Cannady, 75. Five years ago, a salesman from her hometown in Nebraska recommended that she cash in her CDs and buy a viatical for \$12,000. The investment was to pay out \$20,000 when the insured

In one large court case, a viatical company owner pleaded guilty to fraud after he and his colleagues pocketed \$95 million in investments.

died which, she was told, should be in 18 to 36 months.

Five years later, she still hasn't received a payout. Janice's daughter, Sally, requested an updated medical report, but the company hasn't responded. Since she bought the policy, Janice has been diagnosed with Alzheimer's disease and her husband has died. Sally wonders what will happen if her mother needs to enter a nursing home. She'll need the money to cover the bills. But if she doesn't have it, she'll have to apply for Medicaid—which might be difficult because of the viatical. "It complicates eligibility if you have an asset you can sell only at a tremendous discount," says Cynthia Barrett, an elder-law attorney in Portland, Ore.

Dick Hausten's in-laws were 78 years old when they saw a newspaper ad offering "guaranteed returns." A salesman came to their home, told them they were "burning their money by leaving it in CDs" and sold them \$92,000 in viatical settlements. (Hausten let us use his real name but not the names of his in-laws.)

When Hausten found out, he called the two doctors' phone numbers printed on the insureds' medical evaluations and got two wrong numbers. He couldn't find any evidence that they really were doctors. Plus, the medical report for one of the policyholders was from 1989, when he was said to have a life expectancy of 48 months. Yet the investment was made in 1998.

Nine months later, Hausten's father-in-law asked the company to return their money and received 88% of their original investment. They lost \$11,000.

The company that sold the policies, Accelerated Bene-

fits Corp., continues to run advertisements that say, "With the stock market plummeting and interest rates falling, isn't it nice to know there is still an investment that offers your clients fixed high profits with safety?" (Regulators cannot discuss current investigations, but at least one state is looking into Accelerated Benefits Corp.)

Several lawsuits have been won against viatical-settlement companies, and more have been filed. In the largest viatical case so far, David Laing, owner of Personal Choice Opportunities, of Palm Springs, Cal., pleaded guilty to fraud. More than 1,100 investors had given Laing's firm a total of \$95 million to purchase viatical investments, which were advertised as a "risk-free" way to earn 25% per year. Laing and his colleagues pocketed the money and never bought the viaticals.

After an investigation that included the FBI, several states' securities regulators and the U.S. attorney for the Southern District of New York, a receiver was appointed to track down the money and return it to investors.

The Securities and Exchange Commission brought a separate suit against Laing and has gone after other viatical firms for misrepresentation. Civil suits are also starting to appear. Mitchell Perlstein of Investors' Law Center and Scott Link of Ackerman, Link & Sartory have filed class-action lawsuits in Florida against three viatical-settlement companies, alleging that they misrepresented insureds' life expectancies because they knew protease inhibitors had extended the lives of AIDS patients. Yet they continued to tell potential investors that "death is certain and measured only in a matter of months." The plaintiffs are still waiting for payouts they expected several years ago. •

REPORTER: MARGARET RINGER

What to do if you've invested in a viatical

WHAT IF YOU already own a viatical settlement and suspect the company of misrepresentation or wonder whether you should accept an offer to sell back the policy? First contact the securities administrator, insurance department and attorney general in your state and the state where the company is located. (Find your state's Web site and contact numbers at www.piperinfo.com/state/states.html.) They may be investigating the firm and usually have

leverage to get more information from the insurance company and the viatical company. Also contact the Securities and Exchange Commission's Office of Investor Education and Assistance at 202-942-7040.

You'll need to contact that many people because viatical settlements aren't regulated by one central agency. The securities commission takes the lead in some states; in others, it's the insurance department. And some states haven't figured out

yet what to do with viaticals—which makes it easy for unscrupulous sellers.

"One of the things consumers do is rely on jurisdictional gaps—they have the advantage of confusion," says Bill McDonald of the California Department of Corporations, which is currently participating in about ten viatical investigations.

But few consumer organizations know how to help viatical investors. The best one-stop resource is Gloria Grening

Wolk's Viatical Settlements: An Investor's Guide (Bialkin Books) and her Web site (www.viatical-expert.net). She learned about viatical investments while writing a financial guide for people with terminal illnesses.

The Florida Department of Insurance also offers a free booklet that discusses the risks related to viatical-settlement investments. Call the department's consumer help line at 850-922-3132.

From the desk of
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February 22, 1999

Representative Norman Rokeberg
Chairman, House Labor and Commerce
State of Alaska, House of Representatives

Re: February 19, 1999 committee testimony

Dear Chairman:

Thank you very much for allowing Jack and my testimony at your recent L&C Committee Hearing on HB-83. I know the procedure was somewhat unconventional, and your willingness to allow us the public forum to air our concerns was gratifying. I will even go onto say that my prior experiences with the legislative process have been less than desirable, and your efforts both on the part of our Association and now personally have renewed my hope for the system. I know we have a long way to go, but at least having an advocate like you looking at both sides gives me hope.

Per your request, please accept the following as my written testimony for the committee hearing of February 19, 1999:

Chairman Rokeberg, Members of the Committee:

I wish to add my concurrence with Jack's testimony. In addition, I wish to argue on a point of logic as to the actual nature of a viatical settlement. As you know, numerous State and Federal Courts have upheld that the proceeds of life insurance policies are personal property. They are sold as an estate asset or planning tool and have always been regulated by the Division of Insurance. Further, proceeds are taxed as personal property, not securities. The best comparison to a mature life insurance policy may be the equity in your personal residence. Both the insurance proceeds and home are considered personal property, not securities. To sell viaticals as securities would be the same as selling your house as a security. Selling any personal property as a security provides an undo complication (and will restrict free market trade to no appreciable benefit). Thank you for your consideration.

I am still distressed at the constitutional nature of the "cease and desist" request (the Director noted there was no "order") issued by the Division of Banking. First, if there is no order (or implied order), what's the big deal? Why couldn't we continue our sales efforts until the end result was ascertained?