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9935 HOUSE LABOR & COMMERCE



Bill History

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Bill: HB 792

Legislative Session: 76(R)

Council Document: 76R 03727

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Relating to the regulation of viatical settlement agreements and life settlement agreements.

Author: Maxey

Coauthor:

Sponsor: Carona

Cosponsor:

Subjects: 10440 Insurance--Life, Health & Accident

Remarks:

Senate Committee: [Economic Development](#)

Status: Out

Vote: AYES= 7 NAYS= 0 PNV= 0 ABSENT= 0

Bill Subcommittee:

House Committee: [Insurance](#)

Status: Out

Vote: AYES= 7 NAYS= 0 PNV= 0 ABSENT= 2

Bill Subcommittee:

Senate Conferees:

House Conferees:

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Bill: HB 792

Legislative Session: 76(R)

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	DESCRIPTION	COMMENT	DATE	JOURNAL PAGE
H	Filed		01/20/1999	0
H	Read first time		02/08/1999	272
H	Referred to Insurance		02/08/1999	272
H	Scheduled for public hearing on		04/27/1999	0
H	Considered in public hearing		04/27/1999	0
H	Committee substitute considered in committee		04/27/1999	0
H	Testimony taken in committee		04/27/1999	0
H	Recommended to be sent to Local & Consent		04/27/1999	0
H	Reported favorably as substituted		04/27/1999	0
H	Committee report filed with Chief Clerk		04/30/1999	1670
H	Committee report printed and distributed	05:17PM	05/02/1999	0
H	Comm. report sent to Local & Consent Calendar		05/03/1999	0
H	Considered in Local & Consent Calendars		05/05/1999	0
H	Placed on Local, Consent, and Res. Calendar		05/08/1999	0
H	Read 2nd time		05/08/1999	1941
H	Passed to engrossment		05/08/1999	1941
H	Read 3rd time		05/08/1999	1958
H	Passed		05/08/1999	1958
H	Reported engrossed	04:20PM	05/08/1999	2063
S	Received from the House		05/10/1999	1568
S	Read first time		05/10/1999	1575
S	Referred to Economic Development		05/10/1999	1575
S	Posting rule suspended		05/13/1999	1771
S	Scheduled for public hearing on		05/13/1999	0
S	Considered in public hearing		05/13/1999	0
S	Testimony taken in committee		05/13/1999	0
S	Reported favorably w/o amendments		05/14/1999	1797
S	Recommended for local & uncontested calendar		05/14/1999	0
S	Committee report printed and distributed	09:46PM	05/15/1999	0
S	Placed on intent calendar		05/18/1999	0

S	Rules suspended		05/19/1999	2066
S	Read 2nd time		05/19/1999	2066
S	Amended	FA1-Carona	05/19/1999	2066
S	Passed to 3rd reading as amended		05/19/1999	2066
S	Rules suspended		05/19/1999	2066
S	Record vote		05/19/1999	2066
S	Read 3rd time		05/19/1999	2066
S	Passed		05/19/1999	2066
S	Statement of Leg. Intent Recorded in Journal		05/19/1999	2067
H	Senate passage as amended reported		05/19/1999	2624
H	Senate Amendments printed and distributed	01:35AM	05/20/1999	0
H	House concurs in Senate amendment(s)		05/21/1999	2797
H	Text of Senate Amendment(s)		05/21/1999	2797
H	Reported enrolled	11:55AM	05/23/1999	3182
H	Signed in the House		05/23/1999	3082
S	House concurs in Senate amendment(s)-reported		05/24/1999	2402
S	Signed in the Senate		05/24/1999	2408
E	Sent to the Governor		05/24/1999	3275
E	Signed by the Governor		06/19/1999	0
E	Effective on 9/1/99		06/19/1999	0

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Created: 17 Sep 1999 -- 3:20pm

AN ACT

relating to the regulation of viatical settlement agreements and life settlement agreements.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF TEXAS:

SECTION 1. The heading of Article 3.50-6A, Insurance Code, is amended to read as follows:

Art. 3.50-6A. VIATICAL SETTLEMENTS AND LIFE SETTLEMENTS

SECTION 2. Section 1, Article 3.50-6A, Insurance Code, is amended by adding Subdivision (3) to read as follows:

(3) "Life settlement" means an agreement that is solicited, negotiated, offered, entered into, delivered, or issued for delivery in this state under which a person pays compensation or anything of value that is less than the expected death benefit of a policy insuring the life of an individual who does not have a catastrophic or life-threatening illness or condition in return for the policy owner's or certificate holder's assignment, transfer, sale, devise, or bequest of the death benefit under or ownership of the policy.

SECTION 3. Section 2, Article 3.50-6A, Insurance Code, is amended by amending Subsections (a), (b), and (c) and adding Subsections (e) and (f) to read as follows:

(a) The purpose of this article is to register persons engaged in the business of viatical settlements or the business of life settlements and to provide consumer protection for a person ~~[with a catastrophic or life-threatening illness or condition]~~ who may sell or otherwise transfer the person's life insurance policy.

(b) The commissioner shall adopt reasonable rules to implement this article as it relates to viatical settlements and as it relates to life settlements.

(c) The rules adopted by the commissioner under this article must include rules governing:

(1) registration of a person engaged in the business of viatical settlements;

(2) registration of a person engaged in the business of life settlements;

(3) approval of contract forms;

(4) ~~[(4)]~~ disclosure requirements;

(5) ~~[(5)]~~ prohibited practices relating to:

(A) unfair discrimination in the provision of viatical settlements or life settlements; and

(B) referral fees paid by persons engaged in the business of viatical settlements or life settlements;

(6) ~~[(5)]~~ the assignment or resale of life insurance policies; ~~[and]~~

(7) ~~[(6)]~~ the maintenance of appropriate confidentiality of personal and medical information; and

(8) the responsibility of a registrant to ensure compliance with this article and rules relating to viatical settlements or life settlements after the registration is revoked, is suspended, or otherwise lapses.

(e) The commissioner may not adopt rules establishing prices or fees for the sale or purchase of life settlements. This subsection does not prohibit the commissioner from adopting rules addressing unjust prices or fees for the sale or purchase of life settlements.

(f) The commissioner may not adopt rules that require the regulation of the actions of an investor providing funds to a viatical or life settlement company.

SECTION 4. Sections 3 and 4, Article 3.50-6A, Insurance Code, are amended to read as follows:

Sec. 3. APPLICATION OF OTHER INSURANCE LAWS. Articles 1.10,

3-11 1.10A, 1.10C, 1.10D, 1.10E, 1.19, 1.19-1, 1.24, and 21.21 of this
3-12 code appli to a person engaged in the business of viatical
3-13 settlements or life settlements. [ENFORCEMENT. For a violation of
3-14 a rule adopted under this article, the commissioner may take any
3-15 action against a person engaged in the business of viatical
3-16 settlements that may be taken under.]

3-17 [-(1) Articles 1.10 and 1.10E of this code, or]

3-18 [-(2) Article 1.10D of this code against a person
3-19 engaged in a fraudulent insurance act.]

3-20 Sec. 4. DENIAL, SUSPENSION, OR REVOCATION OF REGISTRATION;

3-21 ENFORCEMENT. (a) The commissioner may suspend or revoke the
3-22 registration of a registrant, or deny an application for
3-23 registration under this article if the commissioner finds that the
3-24 registrant or applicant, individually or through any officer,
3-25 director, or shareholder of the registrant or applicant;

3-26 (1) wilfully violates this article, an applicable
3-27 provision of this code or another insurance law of this state, or a
4-1 rule adopted under this article or under such a provision;

4-2 (2) intentionally makes a material misstatement in the
4-3 application for registration under this article;

4-4 (3) obtains, or attempts to obtain, registration under
4-5 this article by fraud or misrepresentation;

4-6 (4) misappropriates, converts to the registrant's or
4-7 applicant's own use, or illegally withholds money belonging to a
4-8 party to a viatical settlement or life settlement;

4-9 (5) is guilty of fraudulent or dishonest practices;

4-10 (6) materially misrepresents the terms and conditions
4-11 of business conducted under this article or any other provision of
4-12 this code or other insurance laws of this state;

4-13 (7) makes or issues, or causes to be made or issued, a
4-14 statement materially misrepresenting or making incomplete
4-15 comparisons regarding the material terms or material conditions of
4-16 any business conducted under this article; or

4-17 (8) is convicted of a misdemeanor involving moral
4-18 turpitude or criminal fraud or a felony.

4-19 (b) An applicant or registrant whose registration has been
4-20 denied, suspended, or revoked under this section may not file
4-21 another application for registration before the first anniversary
4-22 of the effective date of the denial, suspension, or revocation or,
4-23 if judicial review of the denial, suspension, or revocation is
4-24 sought, the first anniversary of the date of the final court order
4-25 or decree affirming the action. An application filed after that
4-26 period may be denied by the commissioner unless the applicant shows
4-27 good cause why the denial, suspension, or revocation of the
5-1 previous license should not bar the issuance of a new license.

5-2 (c) In addition to an action taken under Subsections (a)
5-3 and (b) of this section, the commissioner may take against a person
5-4 engaged in the business of viatical settlements or life settlements
5-5 who violates this article, an applicable provision of this code or
5-6 another insurance law of this state, or a rule adopted under this
5-7 article or under such a provision any action that the commissioner
5-8 may take against a person engaged in the business of insurance who
5-9 violates a statute or rule. [RELATION TO OTHER INSURANCE LAWS.
5-10 Except as otherwise provided by this article or by rules adopted
5-11 under this article, this code and any other insurance law of this
5-12 state do not apply to the business of viatical settlements.]

5-13 SECTION 5. The change in law made by this Act applies only
5-14 to conduct that occurs on or after the effective date of this Act.
5-15 Conduct that occurs before the effective date of this Act is
5-16 governed by the law in effect when the conduct occurred, and that
5-17 law is continued in effect for that purpose.

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5-23

SECTION 6. This Act takes effect September 1, 1999.

SECTION 7. The importance of this legislation and the crowded condition of the calendars in both houses create an emergency and an imperative public necessity that the constitutional rule requiring bills to be read on three several days in each house be suspended, and this rule is hereby suspended.

President of the Senate

Speaker of the House

I certify that H.B. No. 792 was passed by the House on May 8, 1999, by a non-record vote; and that the House concurred in Senate amendments to H.B. No. 792 on May 21, 1999, by a non-record vote.

Chief Clerk of the House

I certify that H.B. No. 792 was passed by the Senate, with amendments, on May 19, 1999, by a viva-voce vote.

Secretary of the Senate

APPROVED:

Date

Governor

HBA-ATS, TYH H.B. 792 76(R)BILL ANALYSIS

Office of House Bill Analysis H.B. 792

By: Maxey

Insurance

6/3/1999

Enrolled

BACKGROUND AND PURPOSE

The Texas Department of Insurance (TDI) regulates the viatical settlement industry. Since the enactment of the regulating legislation, the industry has shifted from its original focus on serving the terminally ill to offering viatical settlements to healthy seniors. The original legislation defined a viatical settlement to apply only to the sale of a policy of an individual with a terminal illness. Thus, prior to the 76th Legislature, settlements involving healthy seniors were not included in the TDI's regulatory powers.

H.B. 792 defines "life settlement." This bill requires the commissioner of insurance (commissioner) to adopt reasonable rules relating to viatical settlements and life settlements. This bill also authorizes the commissioner to suspend or revoke the registration of a registrant or deny an application for registration if the commissioner finds that the registrant or applicant, individually or through any officer, director, or shareholder of the registrant or applicant performs certain actions. It prohibits an applicant or registrant whose registration has been denied, suspended, or revoked from filing another application for registration before the first anniversary of the effective date of the denial, suspension, or revocation. H.B. 792 authorizes the commissioner to take any appropriate action against a person engaging in the business of viatical settlements who violates certain provisions.

RULEMAKING AUTHORITY

It is the opinion of the Office of House Bill Analysis that rulemaking authority previously delegated to the commissioner of insurance (commissioner) is modified in SECTION 3 (Section 2, Article 3.50-6A, Insurance Code) of this bill.

SECTION BY SECTION ANALYSIS

SECTION 1. Amends the heading of Article 3.50-6A, Insurance Code, as follows:

Art. 3.50-6A. New heading: VIATICAL SETTLEMENTS AND LIFE SETTLEMENTS

SECTION 2. Amends Section 1, Article 3.50-6A, Insurance Code, to define "life settlement."

SECTION 3. Amends Section 2, Article 3.50-6A, Insurance Code, by amending Subsections (a), (b), and (c) and adding Subsections (e) and (f), as follows:

(a) Provides that the purpose of this article is to register persons engaged in the business of viatical settlements or the business of life settlements and to provide consumer protection for a person, rather than a person with a catastrophic or life threatening illness or condition, who

may sell or otherwise transfer the person's life insurance policy.

(b) Requires the commissioner of insurance (commissioner) to adopt reasonable rules to implement this article as it relates to viatical settlements and as it relates to life settlements.

(c) Provides that the rules adopted by the commissioner under this article must include rules governing registration of a person engaged in the business of life settlements. Provides that the rules adopted by the commissioner under this article must include rules governing the responsibility of a registrant to ensure compliance with this article and rules relating to viatical settlements or life settlements after the registration is revoked, is suspended, or otherwise lapses. Makes conforming and nonsubstantive changes.

(e) Prohibits the commissioner from adopting rules establishing prices or fees for the sale or purchase of life settlements. Provides that this subsection does not prohibit the commissioner from adopting rules addressing unjust prices or fees for the sale or purchase of life settlements.

(f) Prohibits the commissioner from adopting rules that require regulation of the actions of an investor providing funds to a viatical or life settlement company.

SECTION 4. Amends Sections 3 and 4, Article 3.50-6A, Insurance Code, as follows:

Sec. 3. New title: APPLICATION OF OTHER INSURANCE LAWS. Provides that Articles 1.10 (Duties of the Department), 1.10A (Cease and Desist Orders), 1.10C (Access to Certain Criminal History Record Information), 1.10D (Insurance Fraud Unit), 1.10E (Administrative Penalties), 1.19 (In Case of Examination), 1.19-1 (Subpoena Authority), 1.24 (To Make Inquiries), and 21.21 (Unfair Competition and Unfair Practices) of this code apply to a person engaged in the business of viatical settlements or life settlements. Deletes existing text regarding enforcement of rules adopted under this article.

Sec. 4. New title: DENIAL, SUSPENSION, OR REVOCATION OF REGISTRATION; ENFORCEMENT. (a) Authorizes the commissioner to suspend or revoke the registration of a registrant or deny an application for registration under this article if the commissioner finds that the registrant or applicant, individually or through any officer, director, or shareholder of the registrant or applicant performs the specified actions.

(b) Prohibits an applicant or registrant whose registration has been denied, suspended, or revoked under this section from filing another application for registration before the first anniversary of the effective date of the denial, suspension, or revocation or, if judicial review of the denial, suspension, or revocation is sought, the first anniversary of the date of the final court order or decree affirming the action. Authorizes an application filed after that period to be denied by the commissioner unless the applicant shows good cause why the denial, suspension, or revocation of the previous license should not bar the issuance of a new license.

(c) Authorizes the commissioner to take any appropriate action against a person engaging in the business of viatical settlements or life settlements who violates this article, an applicable provision of this code or another insurance law of this state, or a rule adopted under this article or under such a provision, in addition to an action taken under Subsections (a) and (b) of this section. Deletes existing text relating to the situations under

which this code and any other insurance law does not apply.

SECTION 5. Makes application of this Act prospective.

SECTION 6. Effective date: September 1, 1999.

SECTION 7. Emergency clause.

The Advocate



by Peter Keating

Rolling the Dice on Death

The viatical market may be booming, but it's no place for investors.

Viatikum—it's not where the Pope lives or the latest wonder drug for male pattern baldness. It's a Latin word that can refer to provisions supplied to a departing traveler or to the holy Eucharist placed upon the lips of a dying person. Either way, it means something that helps you move safely to a better place. That's why, when patients facing the crippling costs of AIDS first began selling their life insurance for cash a decade ago, the market that developed was called the viatical industry. Terminally ill people got immediate help to ease their final days, and investors who bought the policies ultimately turned a profit. It looked like a win-win business, if a rather ghastly one.

Well, now it's the end of the '90s. A new class of brokers is using all sorts of aggressive tactics—Internet sites, radio ads, funeral home promos, alliances with financial planners—to pump viaticals to investors eager for big scores. At the same time, new treatments are extending the lives of people with AIDS, making speculation about when they will die more uncertain (and driving down the selling price of their life insurance). So viatical firms are offering settlements to healthy seniors, thereby creating whole new categories of risk for investors. Meanwhile, the industry—in particular, the wildly misleading advertising of many viatical companies—remains haphazardly policed. "Viaticals are falling right through the regulatory cracks," says Joseph Betth, editor of the *Insurance Forum*, an Ellettsville, Ind. trade journal.

The viatical business may be booming—since 1991, the market for viaticals has zoomed from \$50 million a year to more than \$1 billion—but it's no place for individual investors. "The viatical industry started out marketing legitimate policies," says Deborah Bortner, director of securities for the Washington State Department of Financial Institutions. "But now we are seeing a new breed of individuals taking advantage of people who are interested in doubling their money, and we are seeing fraud."

Most viaticals work like this: An insured person, called the viator, sells his or her policy to a viatical settlement company for a percentage of its face value—usually between 30% and 80%, depending on the viator's life expectancy. The viatical company, sometimes working through a broker, then sells the policy to an investor, who stands to gain when the viator dies and the policy is paid. Commissions and fees typically run about 10%, but they're sometimes much higher and aren't always disclosed. In some deals, the viatical company assumes payment of the insurance premiums; in others, they get passed on to the investor.

Now, this sort of investing always has entailed certain risks. What happens, for instance, if your special someone shows a zest for life? If your viator is expected to live for two years but survives for five, your annual rate of return would plummet. You could also be on the hook for extra premium payments. And since the viatical market isn't liquid, you may have to sell your policy at a loss if you need to cash out.

Another danger for investors: policies whose face values decline. "Investors should know that some insurance is written so that if a person's job or salary changes, benefits can decrease," says Anna Grinstead, COO of Accelerated Benefits Corp., an Orlando viatical firm. "We pass on more than 70% of the policies that cross our desk because of underwriting issues." Grinstead says that almost half the policies her firm rejects are sold by other viatical companies.



Buying a terminally ill person's life insurance is a dangerous bet.

The Advocate

Unfortunately, a federal court ruled in 1996—foolishly, in my opinion—that viaticals are not securities. Thus the Securities and Exchange Commission cannot compel the companies that sell them to disclose material risks, or even minimally standardized data such as annualized returns, to investors.

Most viatical ads read as if they were written by alchemists who can turn lead into gold. "Been thinking about the best way to profit with investment funds over the next few years? How about a 70% return on investment?" asks Investments First of Winter Park, Fla. "Looking for a secured rate of high returns at no risk?" blares Services International of Agoura Hills, Calif.

Conrad Jablonski of Anderson Township, Ohio is a living contradiction of these claims. In 1991, Jablonski was given three to six months to live

because of advanced prostate cancer. The cancer spread, and in 1995 Jablonski sold a term life policy for two-thirds of its face value. Jablonski and his wife Kandi used the proceeds to cover bills, pay for their daughter's wedding and prepay his funeral. "First it sounded good," Jablonski says of his settlement, "then it sounded morbid, then it sounded like we could pay bills and for the wedding. It was as natural as that."

**Investors get
the best rate of
return if the
insured person
dies quickly.**

Four years later, Jablonski, now 63, still hasn't had that funeral. Great news for him; bad news for viatical investors who, to put it bluntly, need their vi-

tors to die quickly in order to achieve high annual rates of return.

Indeed, it's because HIV-positive viators are living longer that the industry is expanding beyond its traditional base. Viatical firms now trade policies owned by older people who are not terminally

ill but are interested in "senior settlements" for estate planning. Estimating life expectancy, however, is an imprecise science even in the presence of terminal illness. Investing when the payoff date involves the death of a healthy person? "It's a wager," says Gloria Greening Wolk, a Laguna Hills, Calif. financial planner who runs a viaticals website (viatical-expert.net).

Viatical companies are also stepping up sales of "contestable" policies—policies that can be challenged by insurers because they are less than two years old. Viatical firms can buy these riskier policies at steeper discounts, then market them as offering higher returns.

Contestable policies carry extra hazards for investors: Buy one and it could get canceled at any time for up to two years, and you'll lose your investment. Of course, your viatical company can roll you into another policy—but that one might be contestable too.

Furthermore, trafficking in contestable policies creates incentives for fraud.

Some features listed are optional.

The Advocate

A Dallas grand jury recently indicted Michael Lee Davis, vice president of Southwest Viatical Corp., for allegedly getting patients at a local AIDS clinic to falsify applications for more than \$10 million in life insurance. Davis bought those policies on the cheap, then turned around and marketed them to investors. (Davis, by the way, used to be named Walter Waldhauser. In 1981, he confessed to being the middleman in a murder-for-hire that involved killing a Houston family, in part for their life insurance benefits. After being convicted and paroled, he moved, changed his identity—and got a job as a viatical executive. Davis evaded arrest last month and remains at large.)

Al Woodard, 78, of Bellingham, Wash. was ambushed by a contestable policy scheme. In July 1998, he invested \$25,000 with Alpha Capital

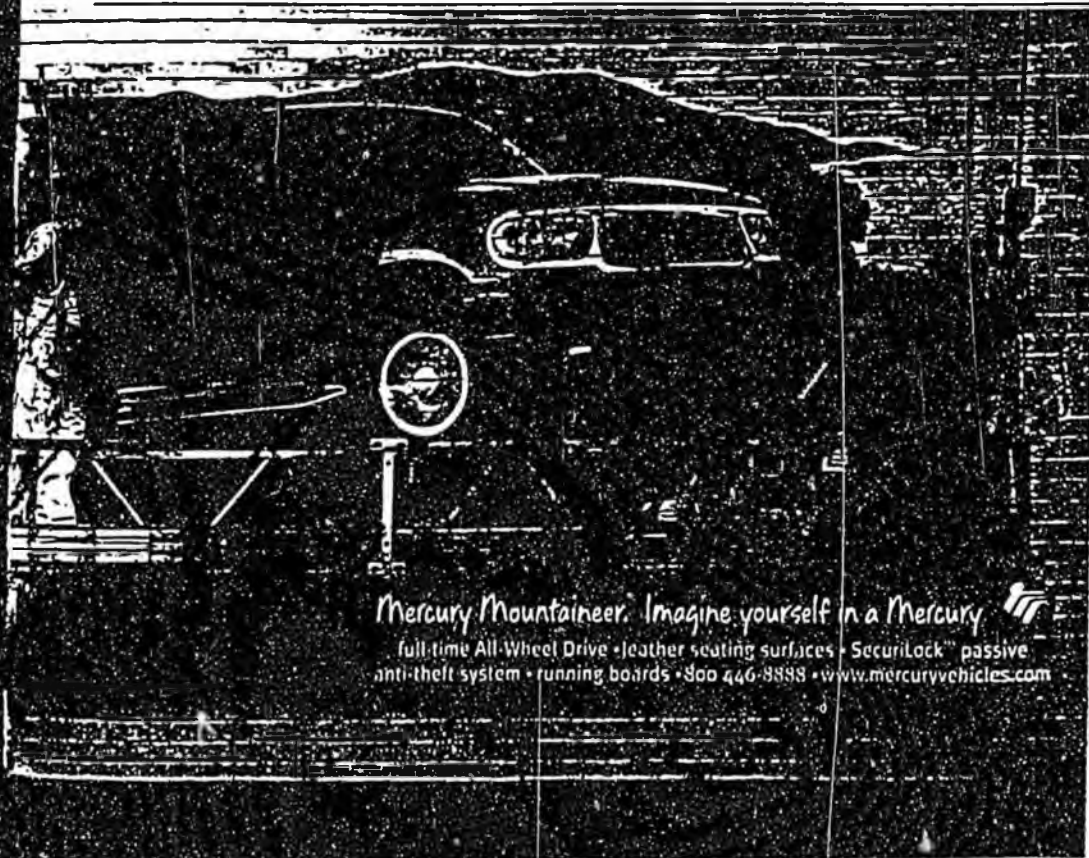
Group, a New York City viatical company, through a financial planner named Linda Scull. Woodard's viator first tested positive for HIV in 1984; by the second half of 1998, his life expectancy was 42 to 48 months. Last November he somehow bought a \$50,000 policy with an annual premium of just \$2,124. That policy was transferred to Woodard in December. According to Washington State investigators, Scull and her cohorts "failed to disclose to investors that the insured was terminally ill prior to being insured" and that "life insurance policies were fraudulently obtained, and thus subject to cancellation by the insurer."

For now, Woodard is still holding his viatical, but he doesn't expect to see his money again. "Linda said it would help the sick person, and it could double, especially if the guy died quickly," he

recalls. "But now it's just a tangled-up mess." (Scull declined to comment. Alpha Capital declined to comment on the state's findings. The state of Washington has ordered Scull to stop selling viaticals. A federal grand jury is investigating Alpha Capital's activities.)

Bottom line: Congress should declare that viaticals are securities—then the SEC could require firms to disclose risks more fully and stop making misleading claims. State governments should follow suit—currently, only seven states regulate viaticals as securities, while 21 don't regulate them at all. Insurers should make accelerated death benefits more easily available to terminally ill policyholders, and should stop raising the amounts of life insurance that they issue without medical exams. And viatical companies that help people legitimately—and they do exist—should cooperate. It's cleanup time. **EJ**

Staff writer Peter Keating can be reached at peter_keating@money.com.



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Insurance cheating alleged

The Associated Press

TALLAHASSEE, Fla. — South Florida companies may have defrauded investors who bought life insurance policies from terminally ill people, say investigators, who believe that in some cases the policies did-

n't actually exist.

The odd but legal practice known as "viatical settlements" gives the terminally ill a chance to get much-needed cash while they are still alive. Investors buy the life insurance policies at a fraction of their value, giving the

policyholder money up front, and then profit when the seller dies. Via viatical companies arrange for the purchase of the policies and take a share of the proceeds.

The state, and reportedly the FBI, is investigating American Benefit Services

Inc. and Financial Federated Title and Trust Inc. to determine if they cheated investors out of tens of millions of dollars by selling fake policies.

FBI agents have already seized assets — including 40 cars — belonging to Finan-

cial Federated owner Frederick C. Brandau, according to a recent report in The Wall Street Journal. About 5,000 people have invested between \$115 million and \$125 million, the newspaper reported, citing unnamed sources.



AUGUST 04, 19:06 EDT

Fraud Alleged for 'Death' Investors

By DAVID ROYSE
Associated Press Writer

TALLAHASSEE, Fla. (AP) — Two South Florida companies may have defrauded investors who bought life-insurance policies from terminally ill people, say investigators, who believe that in some cases the policies didn't actually exist.

The odd but legal practice known as "viatical settlements" gives the terminally ill a chance to get much-needed cash while they are still alive. Investors buy the life insurance policies at a fraction of their value, giving the policyholder money up front, and then profit when the seller dies. Viatical companies arrange for the sales of the policies and take a share of the proceeds.

The state, and reportedly the FBI, is investigating American Benefit Services Inc. and Financial Federated Title and Trust Inc. to determine if they cheated investors out of tens of millions of dollars by selling fake policies.

A Florida judge on Wednesday ordered American Benefit Services in Lake Worth, Fla., to turn over records to investigators with the state Department of Insurance. Investigators also are reviewing documents from Sunrise-based Financial Federated Title.

FBI agents have already seized assets — including 40 cars — belonging to Financial Federated owner Frederick C. Brandau, according to a recent report in The Wall Street Journal. About 5,000 people have invested between \$115 million and \$125 million, the newspaper reported, citing unnamed sources.

Brandau told the Journal that he and his companies have done nothing wrong and that he is fighting the accusations. He also said that none of the investments were at risk.

Neither Brandau nor American Benefit owner Raphael Ray Levy could be reached for comment, and FBI officials declined to comment about their investigation.

American Benefit lawyer Houston Park told Circuit Judge Ralph Smith Jr. in Tallahassee Wednesday that American Benefit would cooperate but believed the insurance department did not have the authority to subpoena all the documents it wants from the company.

Park said the company would not comment on the allegations.

Brandau's lawyer, Thomas Sclafani, said he will propose a settlement to federal prosecutors meant to assure the investors that their investments are safe.

Sclafani said Wednesday that an offshore multinational mining company called CSI Ag Ltd., which has bought Financial Federated's assets, will cover the investments.

"This is not a scam," said Sclafani, a former federal prosecutor. "CSI will be more than able to fully guarantee all of the investors on the schedule they are supposed to be repaid on. ... They have as assets a number of gold mines that are very lucrative."

American Benefit and Federated Financial are related, though separate, companies. Essentially, Federated Financial lined up the terminally ill patients and bought the policies, supplying them to American Benefit, which sold the products to investors.

An internal state insurance department memo in February says that American Benefit maintains it solicits investors to buy into viatical settlements offered by Financial Federated. American Benefit said there wasn't any formal agreement between the two companies, according to the memo.

"This statement is not plausible as all funds solicited by ABS are forwarded to FF&T," the department memo said.

The insurance department was looking into American Benefit before the agency received dozens of complaints from investors this spring. A financial specialist recommended the state investigate the company after it refused to document that the policies it was selling existed.

Several investors have sued American Benefit in state court in Palm Beach County, claiming they asked to see the policies but were not provided them.

A short time after the FBI apparently began looking into Brandau's business last fall, he put an ad in the newspaper looking to buy viatical policies.

W. Scott Page, the owner of Wm. Page and Associates, the first licensed viatical company in Florida, and the president of the National Viatical Association, answered the ad.

Brandau gave him \$1 million to keep in escrow to hold onto to show he was interested in buying some of the policies Page already had, Page said.

"They gave it to me with a blanket 'Use it for anything I could get.' All they wanted was a policy," Page said. "That's why my suspicions started to rise."

Asked if he thought Brandau wanted policies because he wanted something to show investigators, Page said his lawyer advised him not to comment.

"Everyone can assume what they like," he said.

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NASAA

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FOR IMMEDIATE RELEASE

State Securities Cops Release New List of "Top 10 Investment Scams"
—'Day-trading' seminars, promissory notes, viatical investments make ranking—

WASHINGTON (May 24, 1999) – State securities regulators today released a list of the Top 10 Scams they are combating, adding pricey day-trading seminars, supposedly high-yielding promissory notes and investments in viatical settlements (interests in the life insurance policies of supposedly terminally ill people) to the second-annual rankings.

"Today we have an ideal climate for fraud," warns Peter C. Hildreth, New Hampshire's Director of Securities Regulation and President of the North American Securities Administrators Association (NASAA), which released the list of scams. "Millions of new investors, many of whom expect unrealistically high returns, are looking for places to put their money. At the same time we're living through an Internet-driven technology revolution that is a boon to investors and con artists alike."

Securities fraud costs Americans billions of dollars each year, state securities regulators estimate.

The list of scams also includes Internet fraud, affinity group fraud, investment seminars, Ponzi and pyramid schemes, illegal franchise offerings and entertainment scams.

State and national securities cops are doing their best to protect investors, but given their limited resources, investors must do their share to prevent fraud," Hildreth said. "By the time the regulators are notified, the investor's money is usually gone and is rarely recovered. As always, investors are the first line of defense against fraud. The best weapons investors have to protect themselves and their money are skepticism and common sense," said Hildreth.

Here is a list of the Top Ten Scams, ranked roughly in order of seriousness or prevalence:

1. **Internet fraud.** Con artists are using the Internet to "pump and dump" small stocks, peddle bogus offshore "prime bank" notes and perpetrate fraudulent pyramid schemes. About half of the states have programs to monitor the Internet for fraud and they regularly team up with other regulators for Internet "Surf Days." The Internet is like a big city, with good neighborhoods and bad neighborhoods and investors need to be careful about taking advice from strangers. Never invest based on a "tip" on the Internet without doing independent research. You never know who's offering you the "help."

2. **Investment seminars.** Investors should be very wary about expensive seminars where self-anointed gurus imply you can get rich quick. Some people do get rich but usually they're the ones running the seminar, making money from admission fees, and selling their books and

audiotapes. Seminars are marketed through newspaper, radio and TV ads and "infomercials" on cable television. Recently promoters have begun offering seminars and courses promising to turn investors into successful stock "day traders." Day trading, more akin to gambling than investing, is inappropriate for the vast majority of investors.

3. Affinity group fraud. Members of closely knit religious, political or ethnic groups are targeted by con artists of the same religion, ethnicity or political orientation. The crooks seek to take advantage of our natural trust of people who are like us. Targeted media advertising is used to identify potential victims, often with offers of employment or financial advice. California's Asian communities, for example, have been victimized by scammers promoting bogus foreign exchange investments. Typically promoters steal the money and no investments are made.

4. Abusive sales practices. State and other securities regulators report progress in the fight against "microcap" stock fraud by suspending, barring and criminally prosecuting brokers who specialize in the manipulation of low-priced securities. Nevertheless investors need to be on guard and should hang up on aggressive cold callers.

5. Telemarketing fraud. New "boiler rooms" (high-pressure telephone sales operations), open all the time, selling illegal or fraudulent investments. Promoters try to capitalize on the headlines—from fears over the Year 2000 problem to the Asian currency crisis or breakthroughs in computers or biotechnology. One way vulnerable investors can protect themselves is to use their telephone answering machine to screen their calls and not even answer solicitations by cold-calling salespeople.

6. Promissory notes. A growing area of fraud, these notes are supposedly "insured" and backed by real assets. In fact, they are backed only by an often worthless promise to repay. They offer high interest rates to investors who may be struggling to get by on income from money market funds or certificates of deposits. These "investments" are often sold by life insurance agents, lured by high commissions, who may know nothing about the promoters of the investments beyond what they're told. The agents also may not realize they have to be licensed as securities brokers with state securities regulators to sell these notes. In most cases, the notes also must be registered with regulators. Multi-state investigations have revealed that a number of the promoters of these notes have had problems with regulators in the past. Some notes are issued on behalf of companies that don't even exist. Even if the companies are legitimate, investors should realize that the reason these notes are being offered directly to small investors is because banks and venture capitalists have declined to invest in the companies.

7. Viatical investment scams. One of the hottest new investment products and one of the riskiest, viatical contracts are interests in the death benefits of terminally ill patients such as AIDS and cancer victims. The insured gets a percentage of the death benefit in cash, supposedly to improve the quality of their lives in the last days. Investors get a share of the death benefit when the insured later dies, after a fee is paid to the viatical investment broker. Because of uncertainties in predicting when even a terminally ill person is going to die, these investments must be considered extremely speculative.

8. Entertainment fraud. Con artists zero in on investors hoping to hit it big by buying a piece of the next "Titanic." Besides movies, investment vehicles include cable television shows, video games and other entertainment products.

9. Ponzi/pyramid schemes. Always in style, these swindles promise high rates of return to investors, but the only people who really make a killing are the promoters who set them in motion, at the expense and out of funds from later investors, who end up losing their money when the house of

cards inevitably collapses.

10. Illegal franchise offerings. States have taken actions relating to inadequate disclosure and fraud involving franchise investments, often marketed at business opportunity and franchise trade shows where promoters target people attracted by the prospect of owning their own business.

Before making an investment or doing business with a stock broker or investment or franchise promoter, call your state securities regulator to find out if they are properly registered or have a disciplinary history. When checking out a stock broker, ask for their CRD record, which gives their employment and disciplinary history. To find your state regulator, visit the NASAA website at www.nasaa.org/regulator or call 202/ 737-0900.

ADN 25 MAY 1999 PF-1

Life-insurance payoff not always sure thing

COMMON INVESTMENT SCAMS

- **ON-LINE:** Investment fraud over the Internet.
- **SEMINARS:** Includes the seminars promising to teach people how to become day traders of stocks.
- **AFFINITY GROUP:** Fraud that targets religious, ethnic and professional groups.
- **ABUSIVE SALES:** Practices include aggressive, unsolicited telephone calls to consumers by people selling small-company stocks.
- **TELEMARKETING:** Fraud by telephone promoting bogus investments.
- **PROMISSORY NOTES:** Notes sold as insured investments with high interest rates.
- **VIATICAL INVESTMENTS:** Scams that take advantage of investors who thought they could earn money by helping the terminally ill get an early payoff on their life insurance.
- **ENTERTAINMENT FRAUD:** Scams offering bogus investments in movies, cable TV shows, video games and other products.
- **FRANCHISE:** Bogus business franchise offerings.

By **MARCY GORDON**
The Associated Press

WASHINGTON — One of the hottest new investment scams involves people who think they can earn money by helping terminally ill people get an early payoff on their life-insurance policies.

Investors buy the policies through a broker and a portion of the money is paid to the policyholder, who often has AIDS or cancer, to help with medical bills. The investor is supposed to get paid when the person dies, but in some cases, the policyholders aren't really dying. In other cases, the policyholder doesn't exist.

State securities regulators added the scams Monday to their annual list of the "top 10" investment frauds. Also added were high-priced seminars in "day trading," in which inexperienced investors are convinced they can get rich quick by rapid-fire

YOUR MONEY

buying and selling of stocks.

"Today we have an ideal climate for fraud," said Peter Hildreth, president of the North American Securities Administrators Association and director of securities regulation in New Hampshire. "Millions of new investors, many of whom expect unrealistically high returns, are looking for places to put their money. At the same time, we're living through an Internet-driven technology revolution that is a boon to investors and con artists alike."

Investing in insurance policies of the terminally ill is legal and has been around for a decade. Advocates call it viatical investing, which takes its name from the Latin "viaticum" — a purse

Please see Page F-4, SCAM

SCAM: Economy is 'ideal climate for fraud'

Continued from Page F-1

given to a traveler in preparation for a journey.

Viatical companies arrange for the sales of the policies and take a share of the proceeds.

As an example, a group of investors may pay a terminally ill person \$80,000 for the person's \$100,000 life insurance policy. When the person dies, the group will make a \$20,000 profit, minus premiums and fees to the viatical broker.

While many brokers operate legally, the practice isn't regulated, which "creates a situation that could be ripe for fraud," said Scott Lane, assistant enforcement director of Pennsylvania's Securities

Commission.

Gloria Wolk, an expert cited by Lane, estimates that investors have lost more than \$400 million in viatical investments since the industry sprouted in the late 1980s.

One problem occurs when people who aren't really sick take out policies.

In some cases, Lane said, people can get life insurance policies worth as much as \$100,000 without medical exams or blood tests.

In other cases, the viatical company promises big returns of 25 percent or more to investors, but never has any insurance policies to back them up.

Even when someone is terminally ill, the state securities

regulators caution, viatical investing is risky because of the uncertainty in predicting when the person will die. New AIDS drugs have compounded the risk for investors because they keep people with AIDS alive longer.

Deborah Rhoades, a vice president of the National Viatical Association, said fraud is not widespread in the \$1 billion-a-year industry. She said it has occurred in a few instances, as happens "in any other industry that is unregulated."

"We believe it should be regulated," Rhoades said, noting that the trade group has been working to that end with the National Association of Insurance Commissioners.

J.M. Walsh & Company

A Professional Lobbying Firm

P.O. Box 240952 Douglas, Alaska 99824 Phone/Fax 907-364-3410 Pager 907-789-8394

September 23, 1999

Representative Norm Rokeberg
State Capitol
Juneau, Alaska 99801

RE: Viaticals.

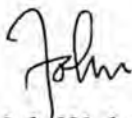
Dear Representative Rokeberg:

On behalf of my client, Future First Financial Group and the Viatical Association of America (VAA), please find enclosed a copy of the Viatical Settlements Model Act, as recommended by the VAA to the National Association of Insurance Commissioners.

House Bill 190, currently before the House Labor & Commerce committee, relates to the issue of viaticals. It is the position of my client that the enclosed model act, as amended, is a preferred approach to HB190.

Please review the enclosed copy and feel welcome to contact me if you have questions or wish to discuss the matter in greater detail. Company officials or representatives of the VAA have indicated that they are more than willing to develop their position or answer any questions you or your staff may have.

Thank you.


J. M. Walsh

Enclosure: 1

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

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ANCHORAGE

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

June 16, 1999

Norman Rokeberg
The Honorable Norman Rokeberg
Alaska House of Representatives
716 W. 4th Avenue, Suite 640
Anchorage, AK 99501-2133

JUN 21 1999

Dear Representative Rokeberg:

RE: viaticals article

During the session, we made reference to an article named "Death Watch" that appeared in the March 1999 edition of *Kiplinger's Personal Finance Magazine*. We noticed that the magazine made some corrections to that article, and we thought you would be interested in that. We have enclosed a copy of the correction as printed from the magazine's web page.

While these specific corrections clarify one part of the article, we believe the general information contained in the March 1999 article provides an appropriate discussion of some of the risks involved with investments in viaticals. If you have any questions or comments, please feel free to call.

Yours truly,



Franklin T. Elder
Director

Enclosure (1)

CORRECTION AND CLARIFICATION:

Death Watch

In the March 1999 story "Death Watch," we reported that Accelerated Benefits Corp. sold a viatical contract in 1998 on a man whose life expectancy had been estimated to be 48 months in 1989. That is not correct. In fact, his life expectancy was estimated in 1998 on a form that referred to a medical examination in 1989. *Kiplinger's* regrets the error, which was based on a misinterpretation of the form.

The same article stated that Dick Hausten, whose in-laws had purchased viatical contracts, got "two wrong numbers" when he attempted to call the two doctors listed on the medical evaluation forms and "couldn't find any evidence that they really were doctors." In fact, Mr. Hausten said that the first number he called was apparently answered by a fax machine. The phone number listed for the second doctor was answered by someone who told Mr. Hausten that the person he was trying to reach no longer resided or worked at that address. *Kiplinger's* regrets any inference readers may have drawn that the doctors did not exist.

Finally, the article stated that Mr. Hausten's in-laws "lost \$11,000" on an investment of \$92,000 in viatical contracts when they asked for their money back nine months later. Accelerated Benefits Corp. notes that the investors chose to cash in their contracts before maturity. According to ABC, the \$11,000 shortfall (about 12%) represented the company's administrative costs and commissions involved in reselling the contracts, which, it says, were allowed under the terms of the contracts.

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**THE VIATICAL ASSOCIATION OF AMERICA
THE NATIONAL VIATICAL ASSOCIATION**

April 16, 1999

Rep. Norman Rokeberg
State Capitol, Rm. 24
Juneau, AK 99801-1182

Dear Representative Rokeberg:

On behalf of the Viatical Association of America and the National Viatical Association, we write to advise you that we are not able to support HB 190 as it has been introduced on April 13. We want, however, to affirm our support for comprehensive viatical legislation in Alaska. In 1998, the National Association of Insurance Commissioners, working with our industry developed a model act and rule to regulate the industry which has our full support. We have urged that it be considered in all states. In addition, we are now working with the NAIC to develop a full proposal governing all aspects of this industry. A copy of the most recent proposal is attached.

We have always believed that the Viatical Industry is closely affiliated with the Insurance industry and that issues arising in the viatical area are best regulated by and within the Insurance Department of any state. In this regard, we have continued to work closely with the NAIC to develop legislative models to deal with emerging issues. In recent months we presented to the NAIC the attached model for an enhanced Viatical Settlement Act dealing with all aspects of this complex emerging industry. This suggestion is being reviewed in 1999 by the NAIC working group and the Life Committee.

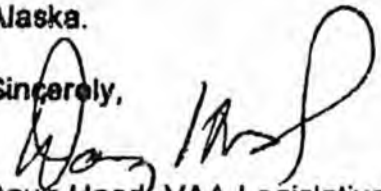
We were pleased when language was removed from HB 83 which did not deal with the complexities of consumer concerns in Alaska. Today, we learned of the new bill, HB 190, to be introduced and heard in your Committee on Monday. By telephone, we will participate in that hearing. We understand that the bill was first presented only Wednesday of this week, so it has been difficult for us to prepare comment. But, we are writing today to strongly urge more deliberate consideration of the issues in this bill.

We feel that the intent of the bill as described in your internet explanation is well taken; that the "legislation would make the status of [viatical settlements] explicit." But, we feel that the legislation, as drafted, may only result in making such settlements impossible under any circumstances. Large institutional members of our industry agree with our smaller participants that, as drafted, the bill has many technical flaws and should be significantly rewritten.

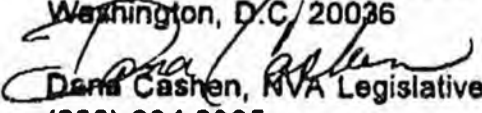
We hope to hope to work with the Department of Commerce and other interested parties to develop a comprehensive Act for Alaska. But, we are concerned that an effort to develop such a solution over the remaining few weeks of the session would do more harm than good.

In substance, we believe that the bill as offered does not correspond to the nature of the business or recognize the real threats to Alaska consumers. Nor does it meet with your stated objectives. We would look forward to the opportunity to work with you to develop a comprehensive approach to this issue for the citizens and consumers of Alaska.

Sincerely,



Doug Head, VAA Legislative Chair
(407) 898-4203
1200 19th St. N.W., Ste. 300
Washington, D.C. 20036



Dana Cashen, NVA Legislative Chair
(800) 894-3985
1501 Broadway, Ste. 312
New York, New York 10036

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 Fak! BOE

DRAFT: APRIL 15, 1999
Includes: The NAIC Model Act
With Wraparound

VIATICAL SETTLEMENTS MODEL ACT

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Section 1. Short Title

This Act may be cited as the Viatical Settlements Act.

Section 2. Definitions

- A. "Financing entity" means an underwriter, placement agent, lender, purchaser of securities, purchaser of a policy or certificate from a viatical settlement provider, credit enhancer, or any person that may be a party to a viatical settlement contract and that has a direct ownership in a policy or certificate that is the subject of a viatical settlement contract but whose sole activity related to the transaction is providing funds to effect the viatical settlement and who has an agreement in writing with a licensed viatical settlement provider to act as a participant in a financing transaction.
- B. "Financing transaction" means a transaction in which a licensed viatical settlement provider or a financing entity obtains financing for viatical settlement contracts, viaticated policies or interests therein including, without limitation, any secured or unsecured financing, any securitization transaction or any securities offering either registered or exempt from registration under federal and state securities law, or any direct purchase of interests in a policy or certificate, if the financing transaction complies with federal and state securities law.

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- C. "Person" means a legal entity, including but not limited to, an individual, partnership, limited liability company, association, trust, corporation or other legal entity.
- D. (1) "Viatical settlement representative" means a person who is an authorized agent of a licensed viatical settlement provider or viatical settlement broker, as applicable, who acts or aids in any manner in the solicitation of a viatical settlement. Viatical settlement representative shall not include:
- (a) An attorney, an accountant, a financial planner or any person exercising a power of attorney granted by a viator; or
 - (b) Any person who is retained to represent a viator and whose compensation is paid by or at the direction of the viator regardless of whether the viatical settlement is consummated.
- (2) A viatical settlement representative is deemed to represent only the viatical settlement provider or viatical settlement broker.
- E. "Viatical settlement broker" means a person that on behalf of a viator and for a fee, commission or other valuable consideration offers or attempts to negotiate viatical settlements between a viator and one or more viatical settlement providers. **NOTWITHSTANDING** ~~irrespective of~~ the manner in which the viatical settlement broker is compensated, a viatical settlement broker is deemed to represent only the viator and owes a fiduciary duty to the viator to act according to the viator's instructions and in the best interest of the viator. The term does not include an attorney, accountant or financial planner retained to represent the viator whose compensation is paid directly by or at the direction of the viator.
- F. "Viatical settlement contract" means a written agreement entered into between a viatical settlement provider and a viator. The agreement shall establish the terms under which the viatical settlement provider will pay compensation or anything of value, which compensation or value is less than the expected death benefit of the insurance policy or certificate, in return for the viator's assignment, transfer, sale, devise or bequest of the death benefit or ownership of all or a portion of the insurance policy or certificate of insurance to the viatical settlement provider. A viatical settlement contract also includes a contract for a loan or other financial transaction secured primarily by an individual or group life insurance policy, other than a loan by a life insurance company pursuant to the terms of the life insurance contract, or a loan secured by the cash value of a policy.

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- G. "Viatical settlement provider" means a person, other than a viator, that enters into a viatical settlement contract. Viatical settlement provider also means a person that obtains financing from a financing entity for the purchase, acquisition, transfer or other assignment of one or more viatical settlement contracts, viaticated policies or interests therein, or otherwise sells, assigns, transfers, pledges, hypothecates or otherwise disposes of one or more viatical settlement contracts, viaticated policies or interests therein. Viatical settlement provider does not include:
- (1) A bank, savings bank, savings and loan association, credit union or other licensed lending institution that takes an assignment of a life insurance policy as collateral for a loan;
 - (2) The issuer of a life insurance policy providing accelerated benefits under Section [refer to law or regulation implementing the Accelerated Benefits Model Regulation or similar provision] and pursuant to the contract; or
 - (3) A natural person who enters into no more than one agreement in a calendar year for the transfer of life insurance policies for any value less than the expected death benefit.
- H. "Viator" means the owner of a life insurance policy or a certificate holder under a group policy insuring the life of an individual with a catastrophic, life-threatening or chronic illness or condition who enters or seeks to enter into a viatical settlement contract.
- I. "Viaticated policy" means a life insurance policy or certificate that has been acquired by a viatical settlement provider pursuant to a viatical settlement contract.
- J. "Viatical Settlement Purchaser" - means a person who gives a sum of money as consideration for a life insurance policy or an interest IN THE DEATH BENEFITS OF in a life insurance policy, which is entered into for the purpose of deriving an economic benefit.
- K. "Viatical Settlement Purchase Agreement" - means a contract or agreement entered into by a viatical settlement purchaser and a viatical settlement provider, to which the viator is not a party, to purchase a life insurance policy or an interest in a life insurance policy, which is entered into for the purpose of deriving an economic benefit.
- L. "Viatical Settlement Sales Agent" - means a person or entity that arranges the purchase through a viatical settlement purchase agreement of a life insurance policy or an interest in a life insurance policy.

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Section 3. License Requirements

- A. A person shall not operate as a viatical settlement provider, viatical settlement representative, or viatical settlement broker without first having obtained a license from the commissioner.

Drafting Note: Insert the title of the chief insurance regulatory official wherever the term "commissioner" appears.

- B. Application for a viatical settlement provider, viatical settlement representative or viatical settlement broker license shall be made to the commissioner by the applicant on a form prescribed by the commissioner, and these applications shall be accompanied by the fees specified in Section [insert appropriate section].
- C. Licenses may be renewed from year to year on the anniversary date upon payment of the annual renewal fees specified in Section [insert appropriate section]. Failure to pay the fees by the renewal date results in expiration of the license.
- D. The applicant shall provide information on forms required by the commissioner. The commissioner shall have authority, at any time, to require the applicant to fully disclose the identity of all stockholders, partners, officers, members and employees, and the commissioner may, in the exercise of the commissioner's discretion, refuse to issue a license in the name of a legal entity if not satisfied that any officer, employee, stockholder, partner or member thereof who may materially influence the applicant's conduct meets the standards of this Act.
- E. Viatical settlement sales agent shall obtain and maintain a licensure as a life insurance agent as set forth in [insert appropriate State Statute].
- EE A license issued to a legal entity authorizes all members, officers and designated employees to act as viatical settlement providers, viatical settlement brokers, or viatical settlement representatives, or viatical settlement sales agents, as applicable, under the license, and all those persons shall be named in the application and any supplements to the application.
- FG Upon the filing of an application and the payment of the license fee, the commissioner shall make an investigation of each applicant and issue a license if the commissioner finds that the applicant:

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- (1) Has provided a detailed plan of operation;
- (2) Is competent and trustworthy and intends to act in good faith in the capacity involved by the license applied for;
- (3) Has a good business reputation and has had experience, training or education so as to be qualified in the business for which the license is applied for; and
- (4) If a legal entity, provides a certificate of good standing from the state of its domicile.

G.H. The commissioner shall not issue a license to a nonresident applicant, unless a written designation of an agent for service of process is filed and maintained with the commissioner or the applicant has filed with the commissioner, the applicant's written irrevocable consent that any action against the applicant may be commenced against the applicant by service of process on the commissioner.

Section 4. License Revocation and Denial

A. The commissioner may suspend, revoke or refuse to renew the license of a viatical settlement provider, viatical settlement representative, or viatical settlement broker, or viatical sales agent if the commissioner finds that:

- (1) There was any material misrepresentation in the application for the license;
- (2) The licensee or any officer, partner, member or key management personnel has been convicted of fraudulent or dishonest practices, is subject to a final administrative action or is otherwise shown to be untrustworthy or incompetent;
- (3) The viatical settlement provider demonstrates a pattern of unreasonable payments to viators;
- (4) The licensee has been found guilty of, or has pleaded guilty or *nolo contendere* to, any felony, or to a misdemeanor involving fraud or moral turpitude, regardless of whether a judgment of conviction has been entered by the court;
- (5) The viatical settlement provider has entered into any viatical settlement contract with a viator who is a resident of this State that has not been approved pursuant to this Act;

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Includes: The NAIC Model Act
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- (6) The viatical settlement provider has failed to honor contractual obligations set out in a viatical settlement contract;
- (7) The licensee no longer meets the requirements for initial licensure; or
- ~~(8) The viatical settlement provider has assigned, transferred or pledged a viatical policy to a person other than a viatical settlement provider licensed in this state or a financing entity; or~~
- ~~(9)~~(8) The licensee has violated any provision of this Act.

- B. Before the commissioner shall deny a license application or suspend, revoke or refuse to renew the license of a viatical settlement provider, viatical settlement broker, or viatical settlement representative, or viatical settlement sales agent, the commissioner shall conduct a hearing in accordance with [cite the state's administrative procedure act].

Section 5. Approval of Viatical Settlements Contracts, Viatical Settlement Purchase Agreements, and Disclosure Statements

A person shall not use a viatical settlement contract, viatical settlement purchase agreement, or provide to a viator a disclosure statement form in this state unless filed with and approved by the commissioner. The commissioner shall disapprove a viatical settlement contract, viatical settlement purchase agreement, or disclosure statement form if, in the commissioner's opinion, the contract or provisions contained therein are unreasonable, contrary to the interests of the public, or otherwise misleading or unfair to the viator or purchaser.

Section 6. Reporting Requirements and Confidentiality

- A. Each licensee shall file with the commissioner on or before March 1 of each year an annual statement containing such information as the commissioner by rule may prescribe.
- B. Except as otherwise allowed or required by law, a viatical settlement provider, viatical settlement representative, viatical settlement broker, viatical settlement sales agent, insurance company, insurance agent, insurance broker, information bureau, rating agency or company, or any other person with actual knowledge of a viator's identity, shall not disclose that identity as a viator to any other person unless the disclosure:

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Includes: The NAIC Model Act
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- (1) Is necessary to effect a viatical settlement between the viator and a viatical settlement provider and the viator has provided prior written consent to the disclosure;
- (2) Is necessary to effect a viatical settlement purchase agreement between the viatical settlement purchaser and a viatical settlement provider and the viator has provided prior written consent to the disclosure;
- ~~(2)~~(3) Is provided in response to an investigation by the commissioner or any other governmental officer or agency; or
- ~~(3)~~(4) Is a term of or condition to the transfer of a viaticated policy by one viatical settlement provider to another viatical settlement provider.

Drafting Note: In implementing this section, states should keep in mind privacy considerations of viators. However, the language needs to be broad enough to allow licensed entities to notify commissioners of unlicensed activity and for insurers to make necessary disclosures to reinsurers and in similar situations.

Section 7. Examination

- A. The commissioner may, when the commissioner deems it reasonably necessary to protect the interests of the public, examine the business and affairs of any licensee or applicant for a license. The commissioner shall have the authority to order any licensee or applicant to produce any records, books, files or other information reasonably necessary to ascertain whether or not the licensee or applicant is acting or has acted in violation of the law or otherwise contrary to the interests of the public. The expenses incurred in conducting any examination shall be paid by the licensee or applicant.
- B. Names and individual identification data for all viators shall be considered private and confidential information and shall not be disclosed by the commissioner, unless required by law.
- C. Records of all transactions of viatical settlement contracts and viatical settlement purchase agreements shall be maintained by the viatical settlement provider and shall be available to the commissioner for inspection during reasonable business hours. A viatical settlement provider shall maintain records of each viatical settlement contract and purchase until five (5) years after the death of the insured.

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With Wraparound

Section 8. Disclosure

A. A viatical settlement provider, viatical settlement representative or viatical settlement broker shall disclose the following information to the viator no later than the time of application:

- (1) Possible alternatives to viatical settlement contracts for individuals with catastrophic, life threatening or chronic illnesses, including, any accelerated death benefits offered under the viator's life insurance policy;**
- (2) Some or all of the proceeds of the viatical settlement may be free from federal income tax and from state franchise and income taxes, and that assistance should be sought from a professional tax advisor;**
- (3) Proceeds of the viatical settlement could be subject to the claims of creditors;**
- (4) Receipt of the proceeds of a viatical settlement may adversely effect the viator's eligibility for Medicaid or other government benefits or entitlements, and that advice should be obtained from the appropriate government agencies;**
- (5) The viator's right to rescind a viatical settlement contract fifteen (15) calendar days after the receipt of the viatical settlement proceeds by the viator, as provided in Section 9C;**
- (6) Funds will be sent to the viator within two (2) business days after the viatical settlement provider has received the insurer or group administrator's acknowledgment that ownership of the policy or interest in the certificate has been transferred and the beneficiary has been designated pursuant to the viatical settlement contract; and**
- (7) Entering into a viatical settlement contract may cause other rights or benefits, including conversion rights and waiver of premium benefits that may exist under the policy or certificate, to be forfeited by the viator and that assistance should be sought from a financial adviser.**

B. A viatical settlement provider shall disclose the following information to the viator prior to the date the viatical settlement contract is signed by all parties:

- (1) The affiliation, if any, between the viatical settlement provider and the issuer of an insurance policy to be viaticated;**

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- (2) If an insurance policy to be viaticated has been issued as a joint policy or involves family riders or any coverage of a life other than the insured under the policy to be viaticated, the viator shall be informed of the possible loss of coverage on the other lives and be advised to consult with his or her insurance producer or the company issuing the policy for advice on the proposed vatication; and
- (3) The dollar amount of the current death benefit payable to the viatical settlement provider under the policy or certificate. The viatical settlement provider shall also disclose the availability of any additional guaranteed insurance benefits, the dollar amount of any accidental death and dismemberment benefits under the policy or certificate and the viatical settlement provider's interest in those benefits.

C. A viatical settlement provider or its viatical settlement sales agent shall disclose the following information to the viatical settlement purchaser prior to the date the viatical settlement purchase agreement is signed by all parties:

- (1) No person shall misrepresent or fail to clearly and affirmatively disclose the nature of the return or the duration of the time to obtain the return of any investment related to one or more viatical settlements sold by a viatical settlement provider.
- (2) The viatical settlement provider AND THE VIACICAL SETTLEMENT SALES AGENT, itself or through another person, shall provide in writing the following disclosures to any viatical settlement purchaser or purchaser prospect:
 - (a) That the return REPRESENTED AS BEING available under the viatical SETTLEMENT purchase AGREEMENT is directly tied to the projected life span or date of death of one or more viators;
 - (b) If a return is represented, the disclosure shall indicate the projected life span or date of death of viator or viators whose life or lives are tied to the return period.
 - (c) If required by the terms of the viatical settlement purchase agreement, that the viatical settlement purchaser may be responsible for the payment of insurance premiums on the life of the INSURED viator or late or surrender fees, or other costs related to the life insurance policy on the life of the INSURED OR INSUREDS viator or viators which may reduce the return.

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- (d) The amount of any trust fees, COMMISSIONS, DEDUCTIONS, or other expenses, if any, to be charged to the viatical settlement purchaser.
- (e) The name and address of the person responsible for tracking the viator.
- (f) **THE GROUP POLICIES MAY CONTAIN LIMITATIONS OR CAPS IN THE CONVERSION RIGHTS, THAT ADDITIONAL PREMIUMS MAY HAVE TO BE PAID IF THE POLICY IS CONVERTED, AND THAT THE PARTY RESPONSIBLE FOR THE PAYMENT OF SUCH ADDITIONAL PREMIUMS SHALL BE IDENTIFIED.** ~~There are certain risks peculiar to group policies owned by employers or other organizations. The primary risk is the possibility the owner or the insurance company may terminate the group policy. This termination will trigger the need to convert the group coverage to an individual policy. Viatical settlement providers shall disclose if there are any limitations or caps in the conversion rates and the additional premiums will have to be paid once the policy is converted, as well as identify the party responsible for the payment of such additional premiums.~~
- (g) **THAT THE LIFE EXPECTANCY AND RATE OF RETURN ARE ONLY ESTIMATES AND CANNOT BE GUARANTEED.** ~~The person who determines the life expectancy of the viator, e.g. with in-house staff, independent physicians, specialty firms that weigh medical and actual data, etc. These parties make the determination of life expectancy based on medical evidence presented to the viatical company by the insured's physicians and/or hospital. Developments in medical treatments or unexpected changes in the viator's medical condition could affect the accuracy of such determination.~~
- (h) Insurance companies may contest death claims for policies that have not been in effect more than two (2) years at the date of death and the death benefit payment could be denied on various grounds. If the viator commits suicide within two (2) years of the policy, the insurance company may not pay the death benefits.
- (i) The purchase of the viatical settlement should not be considered a liquid purchase, since it is impossible to predict the exact timing of

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its maturity and the funds may not be available until the death of the INSURED viator.

- (i) **THE NAME AND ADDRESS OF THE PERSON WITH THE RESPONSIBILITY FOR PAYING THE PREMIUM UNTIL THE DEATH OF THE INSURED.** ~~Under certain conditions, the insurance company may cancel the waiver of premium status on certain policies. In this event, premium payments will then be required and viatical settlement providers shall identify the party or parties who shall be required to make those payments.~~

The written disclosures required under this subsection shall be conspicuously displayed in any viatical settlement contract or purchase agreement furnished to the viator or viatical settlement purchaser by such VIATICAL SETTLEMENT provider and shall be in contrast in color and in not less than 10-point type or not smaller than the largest type on the page if larger than 10-point type.

Section 9. General Rules

- A. A viatical settlement provider entering into a viatical settlement contract shall first obtain:
- (1) If the viator is the insured, a written statement from a licensed attending physician that the viator is of sound mind and under no constraint or undue influence to enter into a viatical settlement contract;
 - (2) A witnessed document in which the viator consents to the viatical settlement contract, acknowledges that the insured has a catastrophic, life threatening or chronic illness or condition, represents that the viator has a full and complete understanding of the viatical settlement contract, that he or she has a full and complete understanding of the benefits of the life insurance policy and acknowledges that he or she has entered into the viatical settlement contract freely and voluntarily; and
 - (3) A document in which the insured consents to the release of his or her medical records to a viatical settlement provider or viatical settlement broker.
- B. All medical information solicited or obtained by any licensee shall be subject to the applicable provision of state law relating to confidentiality of medical information.
- C. ~~All viatical settlement contracts entered into in this state shall provide the viator with an unconditional right to rescind the contract for at least fifteen (15) calendar days from the receipt of the viatical settlement proceeds. If the insured dies during the~~

~~reversion period, the viatical settlement contract shall be deemed to have been rescinded, subject to repayment to the viatical settlement provider of all viatical settlement proceeds, conditioned on the return of such proceeds.~~

- D. Immediately upon the viatical settlement provider's receipt of documents to effect the transfer of the insurance policy, the viatical settlement provider shall pay the proceeds of the viatical settlement to an escrow or trust account in a state or federally chartered financial institution whose deposits are insured by the Federal Deposit Insurance Corporation (FDIC). The account shall be managed by a trustee or escrow agent independent of the parties to the contract. The trustee or escrow agent shall transfer the proceeds to the viator immediately upon the viatical settlement provider's receipt of acknowledgment of the transfer of the insurance policy.
- E. Failure to tender consideration to the viator for the viatical settlement contract within the time disclosed pursuant to Section 8A(6) renders the viatical settlement contract voidable by the viator for lack of consideration until the time consideration is tendered to and accepted by the viator.
- F. Contacts with the insured for the purpose of determining the health status of the insured by the viatical settlement provider, viatical settlement broker or viatical settlement representative after the viatical settlement has occurred shall only be made by the viatical settlement provider or broker licensed in this state or their authorized representative and shall be limited to once every three (3) months for insureds with a life expectancy of more than one year, and to no more than one per month for insureds with a life expectancy of one year or less. The provider or broker shall explain the procedure for these contacts at the time the viatical settlement contract is entered into. The limitations set forth in this subsection shall not apply to any contacts with an insured under a viaticated policy for reasons other than determining the insured's health status.

Section 10. Authority to Promulgate Regulations.

The commissioner shall have the authority to:

- A. Promulgate regulations implementing this Act;
- B. Establish standards for evaluating reasonableness of payments under viatical settlement contracts and viatical settlement purchase agreements. This authority includes, but is not limited to, regulation of discount rates used to determine the amount paid in exchange for assignment, transfer, sale, devise or bequest of a benefit under a life insurance policy;

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- C. Establish appropriate licensing requirements, fees and standards for continued licensure for viatical settlement providers, representatives, and brokers and sales agents;

Drafting Note: Fees need not be mentioned if the fee is set by statute.

- D. Require a bond or other mechanism for financial accountability for viatical settlement providers; and
- E. Adopt rules governing the relationship and responsibilities of both insurers and viatical settlement providers, brokers, and representatives and sales agents during the viatication of a life insurance policy or certificate.

Section 11. Unfair Trade Practices

A violation of this Act shall be considered an unfair trade practice under Sections [insert reference to state's Unfair Trade Practices Act] subject to the penalties contained in that Act.

Section 12. Effective Date

This Act shall take effect on [insert date]. A viatical settlement provider, viatical settlement representative, or viatical settlement broker, or viatical settlement sales agent transacting business in this state may continue to do so pending approval or disapproval of the provider, representative or broker's application for a license as long as the application is filed with the commissioner by [insert date].

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
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MEMORANDUM

TO: House Labor & Commerce Committee Members

FROM: Rep. Norman Rokeberg, Chairman
House Labor & Commerce Committee

DATE: April 16, 1999

RE: HB 190

As the Committee indicated during the debate on HB 83 (Alaska Securities Act), a bill concerning viatical settlements has been introduced. We will be hearing this bill on Monday, April 19, 1999.

Enclosed in your file are the following:

1. HB 190
2. Request for changes from Terry Elder, Division of Banking, Securities & Corporations
3. Proposed CS for HB 190 (L&C), Version G, Bannister, 4/14/99 (incorporating changes)
4. Sponsor Statement
5. Sectional Analysis to proposed CS
6. Viatical Settlement information from DCED
7. Testimony of Patrick Lemieux in support of Maine legislation concerning viatical settlements
8. "The Lottery of Lives", by Jane Bryant Quinn, as contained in the March 15, 1999 edition of *Newsweek*
9. "Viatical Investments: Caveat Emptor" from Kiplinger's Retirement Report as found on Kiplinger's WEB site.
10. "Death Watch" by Kim Lankford, from Kiplinger's Personal Finance Magazine, as contained on Kiplinger's WEB site.
11. March 3, 1999 letter from David Suiter, G.A., Future First Financial Group
12. "What is a Viatical Settlement" and "Viatical settlements are not limited to HIV disease" From American Viatical Corporation's WEB page. Obtained February 12, 1999
13. "Devonshire Holdings Guarantees & Limitations" obtained from Devonshire Holdings WEB page, February 12, 1999
14. February 19, 1999 letter from Terry Elder
15. February 19, 1999 information from Gwaltney & Gwaltney, Inc.
 - i. Testimony of Jack Gwaltney
 - ii. Future First letter dated February 19, 1999
 - iii. February 18, 1999 letter to Mr. Gwaltney from DCED
 - iv. February 19, 1999 letter to Mr. Salvesson from David Gwaltney
 - v. "Viaticals Not Securities, Court Rules" unidentified paper
 - vi. November 5, 1998 Future First memorandum
16. February 22, 1999 letter from David Gwaltney to Rep. Rokeberg

FISCAL NOTE

STATE OF ALASKA
1999 LEGISLATIVE SESSION

BILL NO. HB 190

Revision Date/Time (Note if correction) _____ Dept. Affected Commerce & Econ. Dev.
 Title Viatical Settlements BRU Banking, Securities and Corporations
 Component Banking, Securities and Corporations
 Sponsor Rep. Rokeberg
 Requester House 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)

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)

The division anticipates a minimal number of exemption filings. Since the division currently views viatical settlement contracts as a investment contract, which is a security covered by the Alaska Securities Act, we do not anticipate significant increase in workload or expenses.

Prepared by Franklin T. Elder, Director Phone 485-2521
 Division Banking, Securities and Corporations Date/Time 4/14/99 2:03 PM
 Approved by Commissioner Deborah B. Sedwick
 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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April 14, 1999

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

Dear Rep. Rokeberg:

Re: HB 190 An Act relating to viatical settlement contracts

We want to thank you, Mr. Chairman, and the House Labor and Commerce Committee for introducing HB 190. This important legislation will provide clarity for the viatical settlement industry by explicitly including these securities in the definition of a security in the Alaska Securities Act (the Act). By providing a new exemption, the industry will find the law easy and inexpensive to comply with. The required disclosures to investors and the registration of agents will provide needed investor protection. We appreciate the good working relationship we have had with the committee and staff in developing this legislation.

We did notice, however, some of the comments we provided when we proofread the bill were not incorporated in the final draft before it was introduced. These are not substantive corrections, but they are needed. Therefore, we will be asking the committee to make the following amendments to the bill when it comes before the committee for reconsideration:

1. At page 1, line 3, renumber existing Section 1 as Section 2 and insert a new Section 1 to read as follows:

Section 1. AS 45.55.900(d) is amended to read:

(d) The administrator may by order deny or revoke an exemption specified in (a)(5), (7) or (11) of this section or in (b) or (g) of this section with respect to a specific security or transaction. The order may not be entered without appropriate prior notice to all interested parties, opportunity for hearing, and written findings of fact and conclusions of law, except that the administrator may by order summarily deny or revoke any of the specified exemptions pending final determination of a proceeding under this subsection. Upon the entry of a summary order, the administrator shall promptly notify all interested parties that it has been entered and of the reasons for it and that within 15 days of the receipt of a written request the matter will be set down for hearing. If no hearing is requested and none is ordered by the administrator, the order remains in effect until it is modified or vacated by the administrator. If a hearing is requested or ordered, the administrator, after notice of and opportunity for hearing to all interested persons, may modify or vacate the order or extend it until final determination.

2. At line 6, page 1, delete "at least 10 business days before any offers or sales are made"

3. At line 8, page 1, after the word "transaction" insert "at least 10 business days before any offers or sales are made"
4. At page 2, line 10, after the word "furnished" insert "written"
5. At page 3, line 21, renumber existing Section 2 as Section 3
6. At page 3, line 24, after the word "that" insert "represents or"
7. At page 4, line 7, delete existing Section 3
8. At page 4, line 1, after the word "that" insert "represents or"
9. At page 6, line 2, after the word "consideration" insert "that is less than the expected death benefit of the life insurance policy or certificate"

We hope you and your committee will give favorable consideration to the proposed amendments. We look forward to working with you as this legislation progresses through the legislative process.

Yours truly,



Franklin T. Elder
Director

ALASKA STATE LEGISLATURE

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SPONSOR STATEMENT HOUSE BILL 190

An Act relating to viatical settlement contracts

This bill adds viatical settlement contracts to the definition of a security in the Alaska Securities Act (the Act), and provides an exemption from registration of these securities, while requiring registration of sales agents. The Alaska Department of Commerce and Economic Development (the Department) currently takes the position that viatical settlement contracts are investment contracts, and, thus, are securities under the Act. The industry, however, has no way of knowing this unless they ask the Department. This means that unregistered securities sales may unintentionally take place in Alaska. Currently, the Department is working with the private sector on this matter. This legislation makes the status of these securities explicit, and provides for an exemption mechanism that is relatively easy for the industry to meet, while also increasing the protection of Alaska investors from sales abuses that have appeared in other parts of the country.

Viatical settlement contracts, essentially, are agreements by investors to purchase at a discount the death benefit of an insurance policy of an insured person. The viatical industry has grown rapidly in the last decade. Companies that make the arrangements between insured persons are called viators. People who deal with viators and create a viatical settlement contract and then work through agents to sell those contracts are called viatical settlement providers. These firms created these vehicles as a way a terminally ill person can extract insurance funds for other purposes while the person is still alive. They also provide an investment vehicle for investors. Much of the early growth of the industry was fueled by the AIDS health crisis. As medical advances prolonged the life expectancies of viators, policies did not "mature" as expected, and returns were sometimes less than expected or were even negative. Sales abuses began to surface. It appears that investors often had little idea of the risks along with the potential rewards of these investments. *Sales of these contracts are being made in Alaska today.* Good public policy requires that we take a proactive position to protect Alaska investors from sales abuses that have appeared elsewhere in the country.

The financial press in recent months has published articles describing marketing abuses in the sale of viatical settlement contracts to investors. The abuses often center on inadequate risk disclosure. Investors are lead to believe the investment is a "sure thing." Then they discover these investments, under certain circumstances,

may be illiquid and may even result in losses. One investor's story described how he invested his IRA in a viatical settlement contract. When the viator did not die, the contract became illiquid. Since the investor was reaching the age of 70 and one-half, the IRS required him to make mandatory distributions from the IRA or suffer a large penalty. But, he could not make the distributions due to the illiquid investment.

In the face of these abuses, regulatory agencies across the country have begun to take action. In February 1999, the State of California issued an order against three viatical settlement providers for viatical sales without registration under the California securities act. In April 1999, the State of Oklahoma took an enforcement action against two viatical settlement providers for selling viatical settlement contracts without registration and without making proper risk disclosures to investors. The State of Maine has introduced legislation to add viatical settlement contracts to the definition of a security. Its legislature has determined that sales abuses are serious enough to classify the bill as emergency legislation. The State of North Dakota recently enacted a law adding viatical settlement contracts to the definition of a security in its securities act. The State of Georgia put the industry on notice that it considers viatical settlement contracts to be securities, and requires agents to register. The State of Ohio published a similar position in late 1998. The States of Missouri and Oregon have introduced legislation to add viatical settlement contracts to their securities acts. Finally, in 1998, the SEC for the first time achieved full injunctive and monetary relief in a viatical settlement case when a company agreed to pay \$950,000 to settle charges that viatical settlement contracts were sold to investors without proper disclosures.

The key to investor protection in this bill is the requirement to disclose information relative to risks and any possible negative factors. It also provides a right of rescission to investors that change their minds within specified time limits. In addition, registration of agents will ensure they meet the eligibility requirements of securities agents, and will allow the Department to take action against an agent if abuses are determined. Finally, the exemption from registration is inexpensive and relatively easy for the issuer to comply with, while at the same time making the issuer subject to the anti-fraud provisions of the Act.

It is also important to state clearly what the bill does not do. It does not regulate viatical settlement providers in their relationship with viators. It does not regulate activities between the viator and the viator's family. It does not regulate the use of a life insurance policy as collateral for a loan, or the ability of an insured person to exercise accelerated benefits provisions of the insurance policy. In short, it does not get securities regulators into the regulation of insurance. It does, however, provide a mechanism to regulate viatical settlement contracts when they are marketed to investors. The U. S. Securities and Exchange Commission (SEC) and a number of states have already taken actions to protect investors. Alaska investors deserve no less.

Comments on CS HB 190(L&C) (Viatical Settlement Contracts)

Overview

CS HB 190(L&C) (viatical settlement contracts) adds viatical settlement contracts to the definition of a security in the Alaska Securities Act (AS 45.55). In laymen's terms, a viatical settlement contract is a contract that provides for the sale of some or all of the death benefit or ownership of an insured person's insurance policy to a third party. Most often, a company called a viatical settlement provider buys these from the insured person (called the viator), and resells interests in the contracts to investors. This bill only regulates the sales of these contracts to investors. It does not regulate the viatical settlement providers and viators in any other way other than to provide investor protection to third-party investors.

The bill provides investor protection by requiring issuers such as the viatical settlement providers to file a notice of exemption from registration and to register their sales agents. This exemption may be denied or revoked for cause by the administrator of securities. Also, the exemption requires sellers to provide proper disclosures to buyers concerning the seller's financial condition and a statement of risks. Finally, the bill provides buyers with a right of rescission if they change their mind within three days of the later of receipt of the final disclosure document or payment of the required purchase amount.

This legislation is absolutely crucial for the protection of Alaska investors. Sales of these products around the country have resulted in a list of investor complaints that have been described in the financial media. As sales of these products are made to Alaska investors, it is important that we provide these investors with a reasonable amount of protection from sales abuses. In that way, Alaska investors may be more assured that they will receive adequate disclosures about these investments, and will have their rights protected under the Alaska Securities Act.

At the same time, viatical settlement providers and their agents will know by reading the Alaska Securities Act that these investments are subject to AS 45.55. Currently, the division of banking, securities and corporations considers these to be securities under the "investment contract" theory. By making it explicit in the definition, all parties will be made aware of their status.

Section 1

Section 45.55.900(d)

By adding a reference to the new viatical contract settlement registration exemption to this section, the securities administrator has the authority to deny or revoke the exemption.

Current law does not include a registration exemption for viatical settlement contracts.

Section 2

Section 45.55.900(g)

A new subsection is added to create an exemption from registration of viatical settlement contracts. The exemption requires the filing of a notice with the state and payment of the exemption fee, currently \$40, disclosing basic information about the issuer. It also

requires that commissions are paid only to agents registered under AS 45.55, and requires basic risk disclosure to investors. Issuers must have a three-year history of operations and must be in good financial standing. Certain limitations are placed on issuers that have had legal problems in the recent past.

Current law does not provide an registration exemption, and does not require risk disclosure to investors.

Section 3

Section 45.55.933

A new section is added providing investors with a right to rescind the transaction within three days of the later of the receipt of the final disclosure document or the payment of the purchase consideration.

Current law only provides rescission rights in the event the security is sold without proper registration or exemption.

Section 4

Section 45.55.990(7)

The definition of "issuer" is amended to add persons, other than broker-dealers and agents, who effect viatical settlement contract transactions with the investor, or creates the pooled or fractional interests in those contracts for sale to investors.

Current definition of issuer does not include persons effecting transactions in viatical settlement contracts.

Section 5

Section 45.55.990(12)

The definition of a "security" is amended to include viatical settlement contracts.

Current definition includes "investment contract" at line 13, page 5 of HB 190, but does not explicitly include viatical settlement contracts.

Section 6

Section 45.55.990(14)-(16)

New definitions are added to include "viatical settlement contracts," viatical settlement providers," and "viators." Viators are insured persons who sell the policy or the death benefits of a policy to viatical settlement providers, whose purpose is to sell these contracts to investors. The sale by the viator to the viatical settlement provider is excluded from the definition of viatical settlement contract, and will not be regulated by the Alaska Securities Act. Also excluded are the transfer of the policy or death benefit to a friend or relative, assignment of the policy as collateral for a loan, and the exercise of accelerated benefits by the insured under terms of the insurance policy.

Current law does not include these definitions.

TESTIMONY OF PATRICK LEMIEUX
IN SUPPORT OF L.D. 1693

AN ACT TO CLARIFY THE REGULATION OF VIATICAL SETTLEMENT
CONTRACTS WHEN SOLD AS INVESTMENTS

Senator LaFountain, Representative Saxl, members of the Joint Standing Committee on Banking and Insurance, my name is Patrick Lemieux. I am a licensed insurance agent who has had personal experience selling viaticals, and am here to speak in support of L.D. 1693, An Act to Clarify the Regulation of Viatical Settlement Contracts When Sold as Investments.

In early 1998, I decided to begin contracting with agents who work for me to sell viaticals, and to sell them to my own clients. I had seen ads in professional publications seeking sellers, and had also done some research on viaticals. I also knew other agents who were selling them. Viaticals looked like a win-win product -- a way for my clients to make a very good return while helping terminally ill people, and an excellent way for me to make money.

The brochure that the company gave me to give to potential investors stated, among other things, that investor profits were "guaranteed" and "insured." When I met with officials of the company that I sold viaticals for, and in telephone conversations as well, they told me that the company had banked \$10 million worth of policies, that they would personally guarantee my clients' money, that the escrow agent handling client money had a 3 million-dollar bond, that the company was in compliance with Maine law, and that viaticals are not securities. I was also told that if a policy was contested by the insurance company that issued it, the company would provide a replacement policy to the investor. I asked for the investor guarantees to be put in writing, and was assured that they would be ..

forthcoming. The purchase agreements that my clients signed stated that investors had an unqualified right to rescind the agreement for any money not already invested in a policy. The purchase agreements also offered policies with three different life-expectancy ranges and levels of profit, and I was told that investors could also diversify their money into more than one policy.

The hype and the reality turned out to be drastically different. When the paperwork showing which policies my clients had invested in was not provided, I complained. I was told that the company did not have money to buy policies, even though they had my clients' money, and in any case supposedly already had a bank of \$10 million worth of policies to sell! When my clients tried to exercise their right to rescind, they received paperwork that was backdated to look as if their money had already been invested in policies, even though I had been told on the telephone that it had not. In one case, the paperwork was backdated to a date before the company even had my client's money! Also, my clients' instructions were not followed regarding the life-expectancy ranges they chose or the number of policies they chose to invest in to diversify their investment. I never received the written guarantees that were promised to me.

At least two of the policies my clients invested in appeared to be fraudulent on their face. In each case, the terminally ill viator had been diagnosed HIV-positive several years before the insurance policy was even issued.

Although policies were supposed to be bought from people who are terminally ill, some of my clients were put into the policy of a person who appears from the medical information provided, simply to have high cholesterol. When another policy that two of my clients invested in was contested and cancelled by the insurance company that issued it, the viatical

company offered to put them into another policy. It was the policy on the person with high cholesterol.

When I demanded that my clients get their money back, the company told me that the money would be returned if I returned the commissions I had made. I told them I would put the commission money in an escrow account with my lawyer, which I did. Needless to say, the company did not return my clients' money as promised.

I never would have become involved in selling viaticals if they had not been represented to me as a risk-free, guaranteed investment. The investor brochure that I received from the company stated that viaticals are gaining in popularity because in 1996 "the court battle to make them a security failed in the U.S. Court of Appeals." In other words, the scam artists are having a field day. I urge members of the committee to support this legislation, so that the Securities Division's authority to regulate viatical sales in Maine will be absolutely clear, and so that others will not have to experience the nightmare that my clients and I have experienced.

THE LOTTERY ON LIVES

Investors are wagering on when other people might die, and there's fraud involved

BY JANE BRYANT QUINN

IN AMERICA'S *FIN DE SIECLE* CASINO CULTURE, NO WAGER seems *outré*. So how about betting on how long a stranger is likely to live? You can buy part or all of his or her insurance policy, becoming the beneficiary. Your gamble: that death will come soon enough to yield a high return on the money you put up. The Viatical Association of America says that \$1 billion worth of coverage went into play last year. Buyers are told they're not gambling, they've got a sure thing. Yeah, sure.

The game began as "viaticals"—policies bought from the terminally ill, especially those in the later stages of AIDS. Roughly speaking, it's a three-way deal. Patients get extra money for care in their final year or so; the viatical company sees that the premiums are paid; at death, the investor collects the policy's face value. It felt safe because AIDS victims seemed to die "on time."

But by the mid-'90s, protease inhibitors were changing the life-expectancy tables. People with AIDS no longer died by the clock. Investors were stuck in policies that didn't—as they say—*mature*. The longer the insured stayed alive, the longer the buyers waited to get their money out, and the lower their annual rate of return. Some had to start paying the premiums on the policies themselves. Disenchantment arose. The industry trolled for something else.

At first, it recruited sellers with other terminal illnesses, such as cancer and heart disease. But life expectancies proved hard to predict. Hearts kept beating, messing up an investor's plan to, um, make a killing.

Today, the viatical biz has pounced on the idea of "senior settlements"—policies bought from older people who don't need coverage anymore. There's a market for term, cash-value and employee group insurance. For seniors in poor health, an investor might offer more than they'd get if they cashed their policies in.

Are these good speculations? Possibly yes, when the illness is truly terminal. But how do you know? The chronically sick might live for years—and unexpected longevity takes the profit out.

For example, you might be told that a policy pays a "fixed 12 percent in three years." That's not an annual average, it's the total, taxable gain from the time you buy until the insured person dies. If death comes in three years, you'll earn 12.4 percent annually. If it takes 10 years, you'll get just 3.6 percent—something the hyped-up viatical Web sites fail to mention.

New twist: And here's a new twist: some firms recruit people, old and young, to buy life-insurance policies *solely for resale*. The insured gets a tidy lump-sum payment for completing the application. The new policy is placed with investors before the ink is dry on the contract (hence the nickname, "wet ink"). The investors put up a sum projected to cover all premiums due until the insured person dies, plus commissions and fees.

But how can you earn a high return on a wet-ink deal, if you're paying not only the premiums but also the extra investment costs? Viatical companies generally agree that there's normally no profit there. Where these deals are on the market, they are probably cases of "outright fraud," says Joseph Belin, editor of the influential newsletter *The Insurance Forum*. For example, take someone who's gravely ill. He applies for a term policy of modest size (up to \$100,000), requiring only a medical questionnaire. He gives false answers and no doctor checks. His premiums are based on a normal life span. If he dies in a couple of years, an investor could cash in big.

Florida recently charged the Justus Viatical Group of Pompano Beach, along with two of its principals, with selling wet-ink policies that were fraudulently obtained. Justus didn't return calls. (Its Web site brags that "Ethics, Honesty and Trust are NEVER Compromised!")

Investors face a special risk with policies less than two years old, even if they're not wet ink. They're "contestable"—meaning that the insurer can revoke them for various reasons, including fraud. Investors could lose the money they put up.



Anne Di Leo, of the year-old Alpha Capital Group in New York City, says she

likes contestable policies because they can sell for a higher price when two years have passed. What if a customer's policy is revoked? Di Leo says she'll replace it from a trust account containing backup policies. She says she can afford backups because she's "taking less money out" of her firm than other viatical companies do. Contestable policies are riskier investments. Time will tell if Di Leo's system works.

Risks aplenty: Viatical firms aggressively tout these investments as "safe" and "guaranteed"—because, of course, eventually the insured will die. But there are risks aplenty, detailed in the book "Viatical Settlements, An Investor's Guide," by Gloria Greenig Wolk (\$35.95; call 888-798-2685). One simple risk is that the insured might deliberately vanish—say, somewhere abroad. No death certificate, no insurance payout.

Some viatical companies soothe the potential investors by offering "fixed" monthly incomes or "guaranteed" buyouts after three years. But they won't have the money if policies don't pay on time.

What if you buy a "senior settlement" policy that's safely past the two-year mark? You're betting that the life expectancy, in the sales material, is a disinterested doctor's best guess. But it might not be. Last year, Missouri issued a cease-and-desist order against the now defunct Life Options International, charging that it misrepresented the life expectancy on some policies it sold. If the insured lives longer, your investment loses altitude. You might have to pay the policy's premiums to keep it in force.

Rightly sold, a viatical might be an interesting gamble. But the industry's shabby sales practices heighten your risk. Only seven states effectively require full disclosure to investors, and viatical companies don't openly sell there. Florida is working on a decent disclosure law, and some investigations are underway. Still, most states can't get their act together. Maybe they will, the first time an angry investor decides to take action to accelerate "maturity." There's more danger than we think in wagering on lives.

Reported by TIZIANA THIBETZELD

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Kiplinger's
RETIREMENT REPORT

December 1998

RETIREMENT LIVING

Viatical Investments: Caveat Emptor

John and Susan Smith (not their real names), retirees living in northern Calif., recently invested \$10,000 of their savings in what they were told was a guaranteed safe investment. Only after they plunked down their money did they have second thoughts about their decision to invest in the shadowy world of viatical settlements.

With a viatical settlement a terminally ill person sells his life insurance policy for a lump sum. The size of the discount on the payment depends on how long he is expected to live. The purchaser may be a viatical company or the deal may be handled through a broker who, for a fee, finds a buyer for the policy. The new policy owner/investor can hold the policy and collect the death payment or resell it to one or more investors.

Misleading Claims

There are legitimate viatical companies and brokers in the business, but too many people hear about viaticals from marketers operating on the periphery of the industry. And too many investors are ignoring warning bells and the old adage: If it sounds too good to be true, it probably is. Take a look at some of the come-ons prospective investors encounter.

Guaranteed returns. 12%, 28%, 42%! Fact is, your return depends on when the insured person dies. Pay \$100,000 for the \$124,000 policy of an individual who is expected to live two years and the expected return is 11.4% per year. That drops to a 5.5% annualized return if the person lives four years.

On top of that, your return could be negative if the escrow funds set aside to pay policy premiums run out before the insured passes on. You and the other investors will be left to pick up the tab for the premiums or allow the policy to terminate and lose your investment.

It's a humanitarian investment. Hardly. Your investment gives you a vested interest in the timely death of the insured. In addition, terminally ill individuals who want to sell their policies already have plenty of bidders. "We see a lot of investor money floating around and a shortage of viable policies out there," says John Ellis, a lawyer in Missouri's securities division. (Viable policies, from an investor's viewpoint, are those covering the lives of individuals most likely to die within their life expectancy periods.) There is also evidence that the "best" policies are being bought up by big institutional investors.

It's "a perfect no-risk investment." This out-of-context quote comes from a 1995 *60 Minutes* program on the use of viatical settlements by AIDS victims. The show aired before the death rates of those infected with HIV began declining dramatically because of new drug treatments. In addition, what program host Morley Safer actually said was: "And, sadly, the deadliness of AIDS makes [viatical settlements] a perfect no-risk investment: quick profits guaranteed in the death futures market, with enough buyers available for an

AIDS patient to shop around. Value is graded on the bleakness of medical charts."

There's no market risk. True. The investment is in a life insurance settlement, not stocks, bonds or mutual funds, subject to the ups and downs of the market. But market risk is extensively analyzed and widely publicized, something that can't be said about viatical investment risk.

For example, annualized total returns on mutual funds are calculated in standardized ways and are available to all. No one knows what the average annualized return is on viatical investments.

You can't lose your investment. This claim comes from the insurance company's guarantee to make death payments, a promise that's often backed—up to certain limits—by a state insurance pool. The life insurance company's ability to make death payments doesn't guarantee that you can't lose your investment.

A Buyer's Tale

John and Susan Smith put \$10,000 of their savings in viaticals after hearing a California radio station pitch viaticals as a safe, guaranteed investment with a 12% return. They now own fractional interests in three life insurance policies originally sold to investors in 1994.

After mailing the check, the papers they got back from the escrow agent were so vague and unclear, says Susan, that she headed to the library to see what she could find out about viatical investments. She checked out *Viatical Settlements, An Investor's Guide* (\$31.95; Bialkin Books) and was shocked to find the company they purchased from was cited by author Gloria Wolk in ways that did nothing to inspire her confidence. For now, the Smiths are stuck with an investment they don't fully understand and can only hope they'll earn the promised return in a reasonable period.

They aren't alone. In Missouri, 250 residents face the prospect of losing close to \$5 million in viatical investments. In California, Dept. of Insurance official Caitlin Smith says she gets "three calls or more a day from individuals wanting to know what they've done." State officials nationwide are bracing for a surge of complaints as policies sold as investments reach the end of their estimated life expectancies and premium reserves run out.

Operating in the Dark

Most investors who buy viatical settlements are flying blind. "Buying viaticals has too many loopholes for the ordinary retiree who can't hire experts to help," concludes Marilyn Davey of Oceanside, Calif. She contacted Senior Citizens Financial Services after seeing their viatical advertisement in a local newspaper but had second thoughts about investing after viewing the tape dropped off at her home. (You guessed it—the tape included excerpts from the old 60 Minutes program.)

Investors run the following risks:

- Longer life expectancies—especially among those diagnosed with AIDS—have made it increasingly difficult to predict when investors will get a payback.
- Little government oversight. Despite being required to register with insurance and/or securities departments in some states, there is no

effective state or federal regulation. These investments, which the Securities and Exchange Commission (SEC) and most state securities regulators would like to see regulated as securities, have simply "fallen between the regulatory cracks," says Leon Orenstein, a lawyer at the SEC.

- Steep barriers to verifying critical information. For example: Is the policy contestable by beneficiaries? Who is the actual owner? Who are the irrevocable beneficiaries? How knowledgeable—and independent—are the medical experts determining life expectancies? How independent is the escrow company handling the funds and making payouts?
- Liability for premium payments to keep policies in force. This is especially hard to determine when the investment is sold in fractional shares. For instance, if one fractional owner refuses to pay, what will happen to the policy?

All things considered, viatical investments are no place for retirees to put their money.

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KIPLINGER'S

PERSONAL FINANCE MAGAZINE

March 1999

Death Watch

By Kim Lankford

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

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.

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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."

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.

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 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 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.

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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.

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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 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 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 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.

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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 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 70 1/2 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 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.

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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 Benefits 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 prostate 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.

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KIPLINGER'S

PERSONAL FINANCE MAGAZINE

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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.

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KIPLINGER'S

PERSONAL FINANCE MAGAZINE

March 1999 - Death Watch - page 6

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 con artists 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). 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.

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MAR 05 1999

David Suiter, G.A.
Future First Financial Group

P.O. Box 222522
Anchorage, Alaska 99521-2522
907-522-6365

March 3, 1999

Norman Rokeberg
Senator
Juneau, Alaska 99801
Facsimile: 907-465-2040

I am writing in reference to a House Bill that is going to be introduced regarding Viatical Settlements indicating Viatical Investments should be regulated by Banking and Securities. I believe that Viatical's should be regulated. If self-regulation is unacceptable then they obviously should fall under the Department of Commerce and Economic Development's Division of Insurance.

Viaticals have to deal with life insurance, beneficiary, underwriting, suicide and incontestability clauses and more. In order to protect the public and keep clients apprised of all the various workings of a Viatical settlement a life insurance agent must know these things. To the best of my knowledge Securities Agents do not know nor do they wish to know these things.

To place Viaticals under the umbrella of Securities is to stamp out a fledgling industry in Alaska. Only one state in the United States has Viaticals regulated as a Security. Approximately eighteen states have them regulated under insurance departments.

This is an important industry and should be encouraged to grow. The humanitarian needs of terminally ill people hinge on their ability to have the option of selling what could be their last tangible asset. Such humanitarian needs can include such things as purchasing medication, paying medical bills in order to continue treatment or improve their lifestyle in their remaining years. Without investors, there would not be the opportunity for terminally ill individuals to sell their life insurance policies.

Since the Securities and Banking Commission demanded all selling of Viaticals cease, my income has stopped. I have not broken any laws and am being deprived of making a living. Please do everything in your power to see that future investors will have an opportunity to involve themselves in this humanitarian effort. It would be an added bonus if you could see fit to lift the Cease and Desist Order until this matter is resolved. Viaticals should be regulated and if they must be regulated by an existing agency, please place it under the auspices of the Division of Insurance.

Sincerely,



David Suiter, G.A.
Future First Financial Group

What is a Viatical Settlement?

A financial option whereby an individual facing a life-threatening illness can sell all or part of his/her life insurance policy to a third party for cash

Individual selling the policy to a third party may receive between 50% - 85% of the policy's face value.



There are NO restrictions on how funds from a Viatical Settlement can be used.

The new owner of the insurance policy becomes responsible for making all future premium payments.

Viatical settlements are not limited to HIV disease.



Although viatical settlements became more mainstream in the wake of the AIDS pandemic, they are in no way limited to people with HIV/AIDS.

Benefits America also helps those fighting:

- Cancer
- Alzheimer's
- Heart and cardiovascular diseases
- Parkinson's
- MS
- ALS (Lou Gehrig's Disease)
- Individuals with multiple conditions which together threaten life
- And a myriad of other life-threatening diseases

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Guarantees & Limitations

Remember, you can never lose any of your money, unlike stocks or bonds, etc. You may have a lower rate of earnings, but - *You cannot lose your principal and your profit is guaranteed!!!* A great place to invest in this program is inside a pension or profit sharing plan, IRA, Keogh, SEP, etc. or you can use these vehicles for education funding since the terms are so short.



Limitations

- \$20,000 minimum investment required

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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.

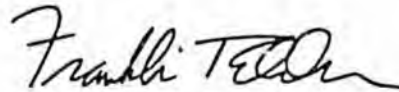
In the November 2, 1998 issue of *Investment News* (pp. 1 and 33), a number of investor complaints are described, and the article states that at that point "...only Maine has formally put life insurance agents on notice that viaticals are subject to state securities laws and that all sales agents be 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

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.

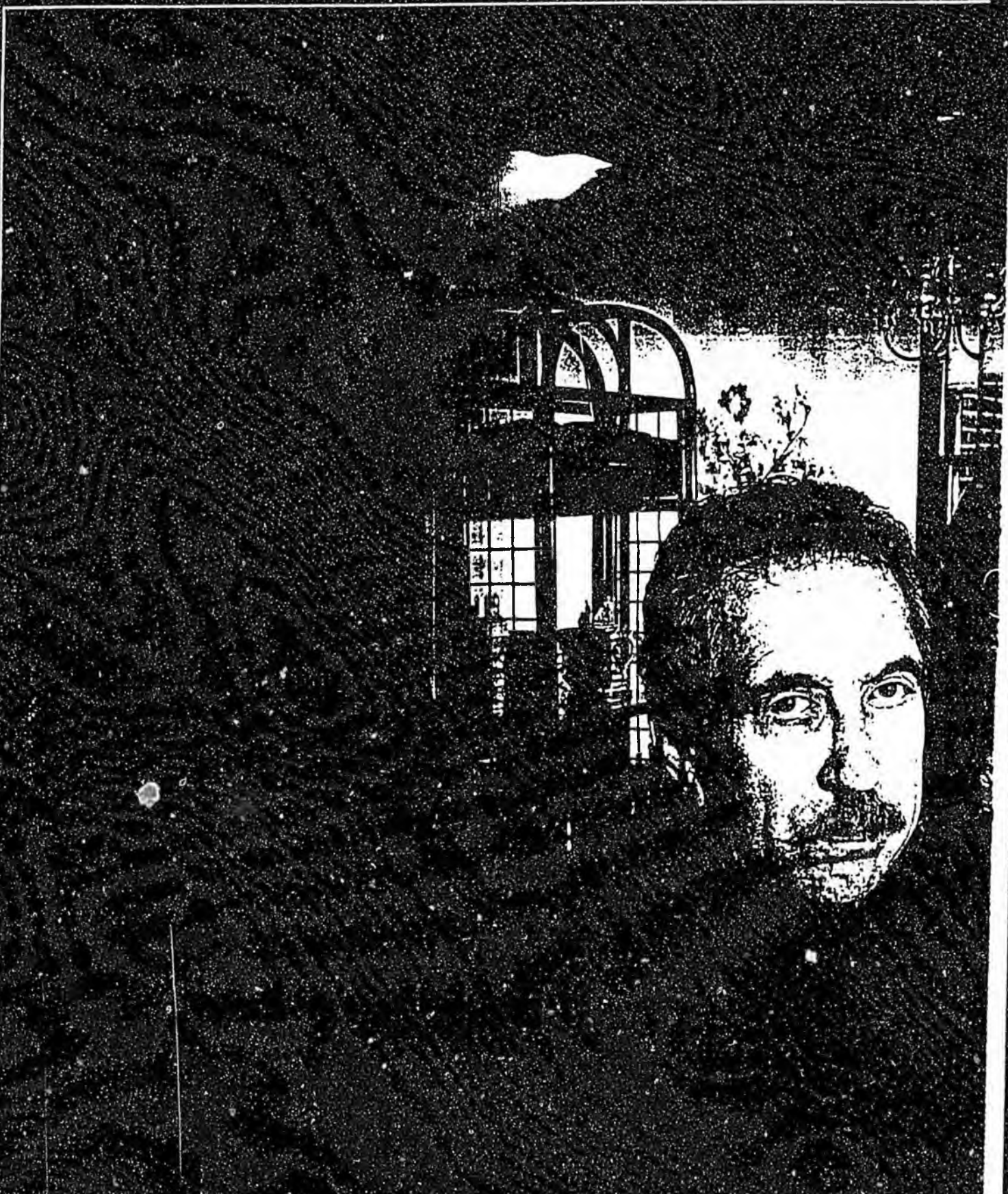
We hope this letter is responsive to the chairman's question. For your added information, we have attached a copy of an article on viatical investments appearing in the March issue of *Kiplinger's Personal Finance Magazine*.

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 pay-off when the viatical company sold its policies. They lost more than \$15,000.



Deceit Wait

By buying life insurance policies 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 Kimberly Lailinger

Photograph by [unreadable]

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.

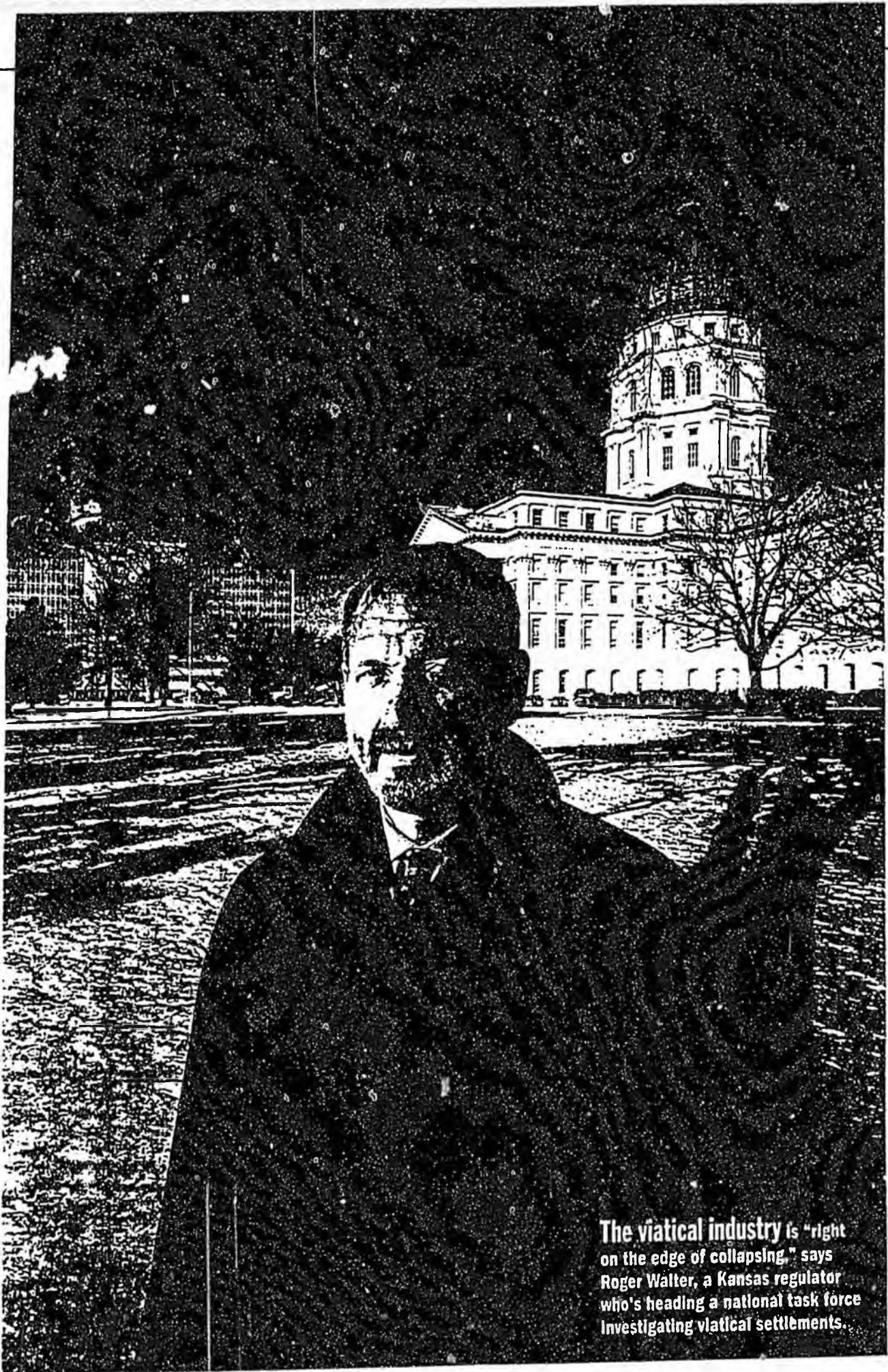
We had little trouble finding people who invested in

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



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.

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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.

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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 con artists 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* (Balkin 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.

Gwaltney & Gwaltney, Inc.

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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 Viator 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.

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