EXECUTIVE SUMMARY

The Florida Legislature directed the Office of Insurance Regulation to “review Florida law and regulations to determine whether there are adequate protections for purchasers of life insurance policies in the secondary life insurance market to ensure that this market continues to exist for Florida seniors.” In preparation for this report, the Office held an informational public hearing, accepted materials and comments, and surveyed Florida life insurance companies.

Florida law requires that insurable interest exist at inception under a life insurance contract. If the owner of a policy lacks an insurable interest in the life of the insured, the policy is void ab initio because it is considered a “wagering contract” contrary to public policy. After inception, the policy is an asset that may freely be sold, transferred, or devised. The initial sale of a life insurance policy in Florida is a “viatical settlement,” which is governed by statute. Vicatedated policies may then be sold to an investor in the “secondary market.” The secondary market may contain policies that were not transacted through licensed viatical settlement providers.

Stranger-Owned Life Insurance (“STOLI”) is one of the many schemes that have arisen in the history of the viatical settlement industry. STOLI is a scheme to initiate a life insurance policy for the benefit of a third party investor that, at inception of the policy, had no insurable interest in the insured. STOLI policies are distinct from legitimately obtained policies; often obtained via fraudulent means; designed to circumvent insurable interest laws; and usually conducted so as to conceal from life insurance companies the subsequent transfer of ownership.

The size of the secondary life market in Florida is difficult to assess. The licensed viatical settlement providers have reported a large number of viaticated policies and a large total face value of viaticated policies. A much smaller number and face value of policies were identified as viaticated by the surveyed life insurance companies, indicating that they may be
largely unaware of which policies on their books have been viaticated and, consequently, may not be adequately prepared for expenditures that will arise upon the maturity of the policies. It is unknown how many viaticated policies or other life insurance policies have been sold on the secondary market.

At the hearing, interested parties expressed differing views as to the legislative directive. Fortress Investment Group (a large secondary market investor) asserted that “a small handful” of insurance companies pose a threat to the market by claiming a lack of insurable interest, asking courts to invalidate policies from inception, and seeking to retain the premiums. Fortress proposed five legislative changes: (1) make subjective intent irrelevant to insurable interest; (2) prohibit insurable interest challenges after the contestable period; (3) require a notice of validity of a policy from insurance companies within ninety days of inquiry; (4) require return of premiums to the policyowner if a policy is voided; and (5) monitor cost-of-insurance rate increases.

The American Council of Life Insurers (ACLI) contended that the legitimate markets are “doing just fine” and that the policies Fortress purchased were STOLI. ACLI asserted that whether a particular policy can be rescinded, whether an insurable interest existed, and whether premiums are returned depend on the facts of each individual case. ACLI opposed Fortress’s proposals because there is no need for legislation if this is a one-company issue, it would be difficult to legislate fairness, and the legislation would encourage toxic assets in the marketplace.

The Life Insurance Settlement Association (LISA) asserted that the litigation at issue does not concern policies transacted through a regulated viatical settlement, as STOLI is designed to circumvent this system. In LISA’s view, the law should require the return of premiums if the policy has gone through a regulated viatical settlement transaction, which involves a level of scrutiny and diligence. LISA also raised five issues that it asserted impede
the ability of seniors to enter into a viatical settlement or diminish the value received.

The Institutional Longevity Markets Association (ILMA) supported each of Fortress’s proposed legislative changes, stating that institutional investors seek protections because they have limited access to information to evaluate policies in the secondary market. In ILMA’s view, insurance companies are in the best position to conduct the proper diligence at policy origination. ILMA asserted that there is uncertainty in the market and that issues such as whether a policy can be challenged after the two-year contestable period are not settled in the case law.

Jim Tollerton of Professional Benefits spoke as a typical Florida insurance agent, stating that an agent is in the business of insuring lives for families, businesses, and charities, and that the vast majority of legitimate agents in Florida have no interest in participating in the viatical settlement market because of the ongoing problems that naturally happen once a policy is sold.

The Florida Insurance Council (FIC) asserted that life insurance companies do, in fact, conduct the proper diligence in underwriting, but may receive falsified or misleading documents. With respect to premium-return, FIC argued that a court needs to be able to assess the facts of each case in order to dispense equity.

Based on the evidence and testimony provided, the Office concludes that there appear to be adequate protections for purchasers of life insurance policies in the secondary life insurance market. The five legislative changes proposed by Fortress, and supported by ILMA, appear to be proposed in order to address the actions of a small handful of insurance companies. The courts are addressing these issues based on the fact-specific circumstances of each case, and there is a significant concern that enacting these legislative changes may have the unintended consequence of encouraging STOLI and fraud. The treatment of life insurance solely as a commodity from inception is at odds with the purpose of life insurance and may have negative ramifications for
the industry, to the detriment of Florida consumers, life insurance companies, and the legitimate viatical settlement industry. The Office has identified issues that may merit further investigation administratively, but has no recommendations for legislative action at this time.
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I. INTRODUCTION

The Florida Legislature directed the Office of Insurance Regulation (the “Office”) to “review Florida law and regulations to determine whether there are adequate protections for purchasers of life insurance policies in the secondary life insurance market to ensure that this market continues to exist for Florida seniors.”

The Office conducted an informational public hearing with respect to the legislative directive in Tallahassee, Florida, at the Knott Building, Room 412, Capitol Complex, on October 25, 2013. The hearing was broadcast via the Internet and was recorded by the Florida Channel. A transcript is attached as Appendix A. Presenters at the hearing were Fortress Investment Group (an investor in the secondary life insurance market); the American Council of Life Insurers (ACLI); the Life Insurance Settlement Association (LISA); the Institutional Longevity Markets Association (ILMA); Professional Benefits, Inc. (an insurance agent); and the Florida Insurance Council (FIC). The presenters expressed differing views on the issue presented.

In addition to holding the public hearing, the Office also accepted materials and comments via e-mail. The materials and comments received are available on the Office’s website at http://www.floir.com/Sections/LandH/SecondaryLife.aspx.

In preparation for this report, the Office also conducted a survey of Florida life insurance companies to inquire as to their knowledge of the status of their policies and whether those policies had potentially been viatcated or sold on the secondary market. The survey asked, as of June 30, 2013, for the number and face value of Florida in-force policies owned by a trust, owned by a bank or financial institution, financed through a premium-finance company or other

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1 Ch. 2013-40, §6, at 316, Laws of Fla.
structured loan program, and that have been viaticated. The survey allowed responses to these questions based on estimates. The survey also asked each company whether it has procedures in place to evaluate the impact of viaticated policies on the net-present-value of the life insurance book of business. Of the 426 companies surveyed, 393 completed the survey. Of those companies, 327 have active in-force life insurance policies in Florida that could be subject to viatication. The survey questions and a summary of the results are attached as Appendix B.

II. BACKGROUND & OVERVIEW

A. Definition of “Secondary Market” and “Viatical Settlements”

The Florida Administrative Code defines the “secondary market” as the “assignment, transfer, sale, devise, or bequest of the death benefit or ownership of all or a portion of a viaticated life insurance policy or viaticated certificate of insurance.”3 A “viatical settlement,” or viaticated life insurance policy, is a life insurance policy that has been sold by the policyowner in exchange for compensation or anything of value, usually for more than the policy’s cash surrender value, but less than the face value of the policy. The purchaser becomes the new owner, assigns the beneficiary or beneficiaries, and is responsible for making future premium payments. Although a distinction is often made in the terms used based on whether the insured is terminally ill—“viatical settlement” for terminally ill insureds and “life settlement” for everyone else4—Florida law does not make this distinction.5 Accordingly, this report will use the term “viatical settlement contract” or “viaticated policy” regardless of whether the insured was terminally ill when the policy was sold.

B. History and Regulation of Viatical Settlements in Florida

Since the regulation of viatical settlements came under the purview of the Florida Department of Insurance (“Department”)—now the Office—in 1996, the Office has endeavored to protect not only the insureds, but also consumers investing in the viatical settlement market, through seeking the passage of legislation as well as examining viatical settlement providers. The Office has encountered a number of fraudulent practices detrimental to Florida consumers, life insurance companies, and the legitimate viatical settlement industry. Accordingly, the Office has, and continues to, endeavor to uncover and address fraudulent practices.

Early viatical settlements offered an alternative way to provide terminally ill individuals with the necessary money for medical and living expenses in their final days. Specifically, the idea of viatical settlements developed in the mid-1980s to allow AIDS patients to sell their existing life insurance. Many of these patients had short life expectancies and lacked the money to pay for their medical bills and treatments. In order to address this need, some individuals and companies began offering to purchase the patients’ life insurance policies for a portion of the death benefit amount, giving the patients money to pay their bills.

In 1996, the Florida Legislature established a framework for the regulation of the viatical settlement industry, commonly referred to as the “Viatical Settlement Act” (the “Act”). The initial purpose of the Act was to protect policyowners selling their policies by requiring licensure of viatical settlement providers and viatical settlement brokers. Subsequently, in late 1997 and

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6 Before 2003, the entity regulating, among other things, life insurance companies and viatical settlement companies was the Florida Department of Insurance. In 2003, the Department was reorganized, and the Office is now the entity tasked with regulating and licensing these companies.


9 See generally id. at 184-86 (providing an overview of the early viatical settlement industry).

10 See ch. 96-336, Laws of Fla. The Viatical Settlement Act is now codified as Part X, Chapter 626, Florida Statutes.
1998, the Department began to receive numerous investor complaints from individual investors who were not receiving promised returns because the insureds were outliving estimated life expectancies. The typical investors of these viatical settlements were individuals, often seniors who had risked their life savings in what was represented as a safe investment and marketed as a compassionate way to help dying individuals.\(^{11}\) With the advent of new, more effective drugs and medical treatments, the insureds had begun living longer and, in some cases, outlived investors.

The Act at this point did not specifically provide for regulation of investments. The Act did, however, authorize the Department to conduct pre-licensure examinations of viatical settlement provider applicants. In early 1998, during one such pre-licensure examination, evidence revealed, among other things, that the subject company knowingly and willfully engaged in the business of buying and selling “cleansheeted”\(^{12}\) insurance policies. As a result, the company’s application was denied, and two of its officers were indicted and convicted of fraud. Subsequent examinations conducted by the Department of other licensed providers and applicants disclosed that such business practices appeared to be commonplace and widespread throughout the viatical industry.

Meanwhile, in view of increasing consumer complaints, mostly from individuals who had invested in viaticals, the Legislature enacted additional consumer protection legislation. In 1999, the Legislature gave the Department jurisdiction over viatical settlement purchase agreements, required minimum disclosures to purchasers, and prohibited fraudulent or misleading practices.\(^{13}\)


\(^{12}\) “Cleansheeting” is the practice of obtaining life insurance policies via materially false information.

\(^{13}\) See ch. 99-212, Laws of Fla. (codified as § 626.9911, Fla. Stat. (1999)).
As a consequence of insureds outliving their projected life expectancies, some viatical settlement providers ceased new sales of policies. Other viatical settlement providers engaged in pyramid schemes, escalating new sales of policies to generate revenue to pay past obligations. One such example of a company participating in a pyramid scheme was Mutual Benefits Corporation (“MBC”), a Florida viatical settlement provider. In 2004, the Office filed an action against MBC and suspended its license. Simultaneously, the United States Securities & Exchange Commission (“SEC”) filed an action in the federal district court seeking an injunction and the appointment of a receiver. The receiver appointed by the court reported that MBC had procured, through fraud, insurance policies with a total face value of as much as $1.4 billion. In December 2005, the SEC agreed to a $25 million settlement in its civil action against MBC, Joel Steinger, Steven Steiner, and MBC’s president, Peter Lombardi, and referred the case to prosecutors for criminal proceedings. The civil case against MBC, S.E.C. v. Mutual Benefits Corp., established a precedent that investments in viatical settlement contracts are securities under federal law.14

Federal prosecutors charged former company employees, including Mr. Lombardi, most of whom pled guilty and were sentenced to lengthy prison terms.15 In a factual statement filed with his plea agreement, Steven Steiner acknowledged that he and other MBC employees falsely promised investors a fixed rate of return. However, MBC could not deliver on those inflated returns, because the insureds continued to live longer than expected, and their premiums had to be paid to keep the underlying policies in force. The scheme relied on sales growth to generate new investor dollars in order to continue to pay premiums on previously viaticated contracts.

14 S.E.C. v. Mutual Benefits, Corp., 408 F.3d 737, 738 (11th Cir. 2005).
15 Joel Steinger and a one-time MBC lawyer, Anthony M. Livoti Jr., are the only remaining defendants in the case. Livoti’s trial is currently ongoing in federal court. Joel Steinger recently received another postponement.
Viatical investment scams in Florida resulted in losses to investors, many of whom were seniors. As of April 22, 2009, the impact of these scams was as follows (may include nationwide book of business):

<table>
<thead>
<tr>
<th>Company</th>
<th>Face Value of Policies Sold to Investors</th>
</tr>
</thead>
<tbody>
<tr>
<td>Justus Viatical Group</td>
<td>$ 2 million</td>
</tr>
<tr>
<td>American Benefit Services / Financial Federated Title &amp; Trust</td>
<td>$ 117 million</td>
</tr>
<tr>
<td>Accelerated Benefits Corporation</td>
<td>$ 114 million</td>
</tr>
<tr>
<td>Future First Financial Group, Inc.</td>
<td>$ 203 million</td>
</tr>
<tr>
<td>Resource Funding Group / Viatical Capital / Life Settlement Network</td>
<td>$ 61 million</td>
</tr>
<tr>
<td>Lifetime Capital</td>
<td>$ 100 million</td>
</tr>
<tr>
<td>Mutual Benefits Corporation</td>
<td>$ 1.4 billion</td>
</tr>
</tbody>
</table>

A list of all Florida regulatory and enforcement actions pertaining to viatical settlement providers from October 1, 1996, through November 30, 2013, is attached as Appendix C.

A practice known as Stranger-Originated Life Insurance ("STOLI") was the next in a long line of schemes. STOLI policies are distinct from legitimately obtained policies. Generally, a party purchasing life insurance must have an "insurable interest" in the person being insured at the inception date of coverage under the life insurance contract.16 STOLI is a scheme to initiate a life insurance policy for the benefit of a third party investor that, at inception of the policy, had no insurable interest in the insured and seeks to profit by purchasing life insurance on a stranger.17 In a typical STOLI transaction, the promoters and investors may establish an irrevocable trust, obtain an insurance policy on a senior, obtain a premium-finance loan, and pay the life insurance policy premiums for two years (i.e., the contestable period). The money needed to pay these premiums, which can be substantial, is financed through premium-finance

lenders. Typically, these premium-finance loans are non-recourse loans, meaning that the life insurance policy is the only collateral for the loan and the premium-finance lender can pursue only the collection of the collateral if there is a default. The beneficial interest in the trust is then sold without the life insurance company being aware of the sale, as the trust remains the policyowner in the insurance company’s records.

STOLI transactions often use fraudulent means such as misrepresentation, falsification, or omission of material facts in the life insurance application. This may also entail misrepresenting the true net worth of the applicant to obtain large face value life insurance policies. Further, STOLI policies are designed to circumvent insurable interest laws, and the sale of the policy is usually completed after the two-year contestable period has expired. Finally, as illustrated above, STOLI policies are usually conducted in such a manner so as to conceal the sale from the life insurance company. More information regarding STOLI can be found in the Office’s Report on Stranger Originated Life Insurance (“STOLI”) and the use of Fraudulent Activity to Circumvent the Intent of Florida’s Insurable Interest Law (January 2009), which is available at http://www.floir.com/siteDocuments/STOLIRpt012009.pdf.

The viatical settlement market in Florida has evolved since its inception—both in the kind of policies being transacted by viatical settlement providers and the type of investors that are investing in these policies. The market now encompasses more than the sale of policies for terminally ill insureds. Viatical settlements of policies for non-terminally ill insureds, often

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18 Id. at 14.
19 Id. However, not all life insurance policies obtained by the usage of a non-recourse loan are STOLI transactions. Id.
20 Transcript at 119-21.
21 STOLI Report, supra note 17, at 12.
22 See id. at 2.
23 Id. at 14.
24 See also Martin, supra note 8, at 187-88.
called “life settlements” (a term used by many of the participants at the public hearing) offer the opportunity for some insured individuals who no longer want, need, or can afford their life insurance policies to sell them. Rather than allowing a policy to lapse and forfeiting the value or selling the policy back to the insurance company for the current cash value, an insured can sell, or “viaticate,” the policy for more money than he or she would receive if the policy was surrendered. According to a source submitted by Fortress, one study calculated that an individual with a $2 million life insurance policy can receive up to $300,000 more for it in the viatical settlement market than by surrendering it back to the insurance company.25

The individual investors involved in the early viatical settlement market have since been replaced primarily by institutional investors and investment firms, such as hedge funds or pension funds, which often invest in large blocks of policies sold as a portfolio in the secondary market.26 In addition, viatical settlement investments are now considered securities under both federal27 and Florida law.28 Some life insurance companies are currently litigating what they assert are STOLI policies that were purchased by investors in the secondary market.29


27 S.E.C. v. Mutual Benefits, Corp., 408 F.3d 737, 738 (11th Cir. 2005).

28 In 2004, the Florida Legislature passed legislation promoted by the viatical industry that made the Office the exclusive regulator of viatical settlement investments in an attempt to avoid the classification of these investments as securities. See ch. 2004-390, § 78, Laws of Fla. In 2005, viatical settlement investments were reclassified as securities under Florida law. See ch. 2005-237, Laws of Fla. The new law subjected these investments to the Florida Securities and Investor Protection Act, which included, among other things, requiring persons selling these investments to be licensed securities brokers.

29 See Martin, supra note 8, at 206-16 (discussing STOLI litigation in various courts and states).
The requirement of an insurable interest for life insurance policies is well-settled in American jurisprudence, dating back to the nineteenth and early twentieth century.\(^{30}\) If the owner of an insurance policy lacks an insurable interest in the life of the insured, the policy is void \textit{ab initio} (null from the beginning\(^{31}\)) because it is considered a “wagering contract” contrary to public policy.\(^{32}\)

Florida’s insurable interest law requires that insurable interest exist at the inception date of coverage under a life insurance contract and sets forth nine categories in which an insurable interest is recognized to exist.\(^{33}\) Examples include that an individual has an insurable interest in his own life; an individual has an insurable interest in the life of “another person to whom the individual is closely related by blood or by law and in whom the individual has a substantial interest engendered by love and affection”; and a trust or trustee “has an insurable interest in the life of an individual insured under a life insurance policy owned by a trust.”\(^{34}\)

Florida law expressly provides that “insurable interest need not exist after the inception date of coverage under the contract.”\(^{35}\) Thereafter, life insurance is an asset that may freely be sold, transferred, or devised.

The initial sale of a life insurance policy in Florida is called a “viatical settlement”\(^{36}\) and is governed by statute.\(^{37}\) A written agreement to transfer ownership or change the beneficiary designation of a life insurance policy is called a “viatical settlement contract” and must establish

\(^{30}\) STOLI Report, \textit{supra} note 17, at 7-9.
\(^{32}\) \textit{TTSI Irrevocable Trust v. ReliaStar Life Ins. Co.}, 60 So. 3d 1148, 1150 (Fla. 5th DCA 2011).
\(^{33}\) \textit{See} § 627.404(1), Fla. Stat.
\(^{34}\) \textit{See} § 627.404(2), Fla. Stat. (listing the nine categories where an insurable interest is recognized).
\(^{35}\) \textit{See} § 627.404(1), Fla. Stat.
\(^{36}\) \textit{See} § 626.9911(10), Fla. Stat. (defining viatical settlement contract).
the terms under which the life insurance policy is transferred or sold. The Office does not have authority to regulate the amount paid as consideration for a viatical settlement contract. The Act requires an insurance company be notified if a policy is viaticated within the two-year contestable period. A viatical settlement contract entered into within the contestable period is enforceable only if certain conditions are met.

A viatical settlement provider is a person who effectuates a viatical settlement contract and must be licensed. Viatical settlement providers are required by law to file annual reports with the Office. Individuals acting as viatical settlement brokers are also required to be licensed, and viatical settlement providers are permitted to use only licensed viatical settlement brokers.

Viatical settlement providers or brokers must make certain minimum disclosures to viators (policyowners who seek to enter into viatical settlement contracts), including that there are possible alternatives to viatical settlements for persons who have a catastrophic or life-threatening illness, that the proceeds from a viatical settlement could be taxable, that the proceeds could be subject to creditors’ claims, and that income from the proceeds could adversely affect the recipient’s eligibility for Medicaid or other government benefits.

38 § 626.9911(10), Fla. Stat.
40 See § 626.9924(7), Fla. Stat. (requiring notification of a viatical settlement if it takes place at any time during the contestable period); § 627.455, Fla. Stat. (providing that every insurance contract shall contain a provision that the policy shall be incontestable for a period of two years).
41 See § 626.99287, Fla. Stat.
42 § 626.9911(12), Fla. Stat. (defining viatical settlement provider); § 626.9912, Fla. Stat. (requiring licensing for viatical settlement providers and setting forth the application requirements).
43 § 626.9913, Fla. Stat. (setting forth the annual reporting requirements).
44 § 626.9916, Fla. Stat.
45 § 626.992(1), Fla. Stat.
46 § 626.9923, Fla. Stat. (setting forth the required disclosures to viators). An emerging issue in the viatical settlement market is whether viatical settlements are an option for funding long-term care expenses, including for policyowners qualifying for Medicaid. LISA Submission, supra note 26, at 1. In 2013, Texas passed legislation
The Office has the authority under the Act to examine the business and affairs of viatical settlement provider applicants and licensees.\textsuperscript{47} In addition, under the Act, the Office is required to suspend, revoke, deny, or refuse to renew the license of a viatical settlement provider if the Office finds that it has, among other things, “engaged in fraudulent or dishonest practices, or otherwise has been shown to be untrustworthy or incompetent to act as a viatical settlement provider”; demonstrated “a pattern of unreasonable payments to viators”; dealt “in bad faith with viators”; or “been found guilty of, or has pleaded guilty or nolo contendere to, any felony, or a misdemeanor involving fraud or moral turpitude, regardless of whether a judgment of conviction has been entered by the court.”\textsuperscript{48}

A person who determines life expectancies or mortality ratings used to determine life expectancies is a life expectancy provider and must be registered under the Act.\textsuperscript{49} The Act prohibits a viatical settlement broker, viatical settlement provider, or insurance agent in the business of viatical settlements in Florida from directly or indirectly owning or being an officer, director, or employee of a life expectancy provider.\textsuperscript{50}

Viatical settlement providers and registered life expectancy providers are required to adopt an anti-fraud plan and file it with the Division of Insurance Fraud. The plan must include a description of the procedures for detecting and investigating possible fraudulent acts and prohibited practices.\textsuperscript{51}

\textsuperscript{47} § 626.9922, Fla. Stat.
\textsuperscript{48} § 626.9914(1), Fla. Stat.
\textsuperscript{49} § 626.9911(4), Fla. Stat. (defining life expectancy provider); § 626.99175, Fla. Stat. (requiring registration).
\textsuperscript{50} § 626.99175(6), Fla. Stat.
\textsuperscript{51} § 626.99278, Fla. Stat. (setting forth what must be included in an anti-fraud plan).
An agreement for the sale or transfer of a viated policy on the secondary market is
called a “viational settlement investment,” and is regulated as a security. A viational settlement
provider is not required to notify the insurance company when the viational policy is sold on the
secondary market. Rather, the insured must be notified of a change in ownership or beneficiary
the first time that the policy is sold after being viational. The insured is not required to be
notified of subsequent sales of the policy in the secondary market.

III. SECONDARY LIFE INSURANCE MARKET REVIEW

The Office begins its review by discussing the size of the viational settlement and
secondary markets in Florida and the reasons that the size of those markets is difficult to assess.
Then the Office presents a summary of the differing viewpoints presented at the hearing.
Finally, the Office reviews each legislative change proposed by Fortress Investment Group and
the Life Insurance Settlement Association (LISA).

A. Florida Market Size

The size of the secondary life insurance market in Florida is difficult to assess. Fortress
submitted an article that indicated that there was approximately $35 billion in life insurance in
force on the secondary market in the United States as of 2009. However, this number
represents the size of the market four years ago in the United States, not Florida.

The difficulty in assessing the size of the market in Florida is the result of several factors.
The first factor is that the exact number of life insurance policies in Florida that have been sold

52 See § 517.021(23) (defining a viational settlement investment).
53 See § 517.072(3), Fla. Stat. (providing that viational settlement investments are not subject to the registration
provisions of sections 514.07 and 517.12, Florida Statutes, provided that certain conditions are met).
54 See § 626.9924(9), Fla. Stat. (providing that if the viational settlement provider sells the policy, it must
communicate the initial change in ownership to the insured).
55 Oliver Suess, et al., Death Derivatives Emerge From Pension Risks of Living Too Long, BLOOMBERG (May 16,
by policyowners is not known. Currently, as of November 30, 2013, there are 17 licensed viatical settlement providers in Florida.\textsuperscript{56} The licensed viatical settlement providers in Florida have reported a large number of viaticated policies and a large total face value of viaticated policies. However, it is important to recognize that many STOLI transactions may not be included in the above-referenced count because they are not transacted through licensed viatical settlement providers.\textsuperscript{57}

The reported viatical settlement business in Florida from 1996 through December 31, 2012, is follows:

<table>
<thead>
<tr>
<th>Year</th>
<th># of Policies</th>
<th>Total Settlements Paid</th>
<th>Total Face value</th>
</tr>
</thead>
<tbody>
<tr>
<td>1997</td>
<td>595</td>
<td>$28,092,334.15</td>
<td>$52,647,174.53</td>
</tr>
<tr>
<td>1998</td>
<td>926</td>
<td>$42,743,130.07</td>
<td>$112,543,865.37</td>
</tr>
<tr>
<td>1999</td>
<td>457</td>
<td>$14,897,514.34</td>
<td>$46,343,838.87</td>
</tr>
<tr>
<td>2000</td>
<td>226</td>
<td>$8,660,583.96</td>
<td>$24,597,165.56</td>
</tr>
<tr>
<td>2001</td>
<td>159</td>
<td>$10,953,111.97</td>
<td>$50,886,210.00</td>
</tr>
<tr>
<td>2002</td>
<td>149</td>
<td>$30,214,217.62</td>
<td>$165,846,096.00</td>
</tr>
<tr>
<td>2003</td>
<td>177</td>
<td>$39,601,642.92</td>
<td>$216,633,538.00</td>
</tr>
<tr>
<td>2004</td>
<td>213</td>
<td>$64,023,628.00</td>
<td>$398,437,492.01</td>
</tr>
<tr>
<td>2005</td>
<td>263</td>
<td>$100,569,253.00</td>
<td>$612,021,215.00</td>
</tr>
<tr>
<td>2006</td>
<td>416</td>
<td>$181,362,091.00</td>
<td>$932,908,140.82</td>
</tr>
<tr>
<td>2007</td>
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<td>703</td>
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<td>783</td>
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<td>$2,233,276,397.92</td>
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<td>2010</td>
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<td>$52,423,952.37</td>
<td>$504,781,652.00</td>
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<td>2011</td>
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<td>93</td>
<td>$30,444,088.75</td>
<td>$241,651,032.00</td>
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<td><strong>TOTAL</strong></td>
<td><strong>6,096</strong></td>
<td><strong>$1,638,962,786.67</strong></td>
<td><strong>$9,550,594,258.00</strong></td>
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Although Florida licensed viatical settlement providers have reported in excess of $9.5 billion in face value of death benefits transacted on just over 6,000 Florida policies from 1997 through 2012, only 15.7\% of that face value amount was identified as viaticated by surveyed life

\textsuperscript{56} A list of licensed viatical settlement providers is attached as Appendix D.

\textsuperscript{57} At the hearing, LISA stated that viatical settlements in Florida are regulated transactions and asserted that much of the STOLI litigation involves policies that did not occur through regulated transactions and were not conducted by licensed viatical settlement providers. Transcript at 118-20.
insurance companies actively writing policies in Florida. A summary of the survey results, which reflects that Florida life insurance companies may be largely unaware of which policies on their books have been viaticated, is attached as Appendix B. It is unknown how many of these policies have matured since being reported. Sixty-four insurance companies estimated or were aware of only a total of 1,928 viaticated Florida policies with a total face amount of approximately $1.5 billion. Of the 327 active Florida life insurance companies that responded with policies that could be subject to viatication,58 263 companies did not report any viaticated policies.

Although an assertion was made at the hearing that insurance companies know which policies have been sold, because they are notified of a potential sale of the policy (via a verification of coverage request) as well as when the policy is actually sold (via a change of ownership form),59 this was not substantiated by the survey results. The reason for this discrepancy is not clear. With respect to the verification of coverage request, insurance companies may receive such a request for various reasons, not only the potential sale of a policy. Further, a verification of coverage request would only provide notification of a potential sale, and it is unknown how many such requests insurance companies receive as compared to the number of policies sold. With respect to change of ownership forms as a means of notification, it may be the case that many insurance companies are not tracking change of ownerships for the purpose of evaluating how many of their policies have been viaticated. It may also be the case that a change of ownership form does not always indicate that the ownership was changed to an

58 This excludes companies that expressly indicated that they do not have life insurance business in Florida as of June 30, 2013, or write only the kinds of policies that would not be subject to viatication (e.g., credit life, group, term, or accidental death and dismemberment).
59 Transcript at 122. An assertion was also made that insurance companies treat viaticated policies differently at every stage than non-viaticated policies. Id. at 122-23.
investor as the result of a sale. Regardless, notification of change of ownership may not occur with STOLI policies as the true owners are typically concealed via a trust or other means.

The survey also inquired as to Florida in-force policies that were owned by a trust, owned by a bank or financial institution, or financed through a premium-finance company or other structured loan program, because such policies have the potential to represent policies that have been sold. For example, in a STOLI transaction, a life insurance agent may convince an elderly individual to form a trust, which would purchase and become the beneficiary of a newly issued life insurance policy with a large face amount. The beneficial interest in the trust would then be transferred to the investor, and the trust would continue to own and be the beneficiary of the policy—without the insurance company knowing that the transfer had occurred.

Of the 327 active Florida life insurance companies that responded with policies that could be subject to viatication, 186 of the companies relied on estimates to respond as they were not able to readily identify trust-owned, bank-owned, and/or premium-financed policies. Of the companies that responded, 169 identified 52,418 in-force Florida policies that were owned by a trust, with a face value of $72.2 billion; 85 companies identified 9,633 policies owned by a bank or financial institution, with a face value of $6.274 billion; and 64 companies identified 8,134 policies that were financed through a premium-finance company or another structured loan program, with a face value of $1.340 billion. However, it is unknown whether these numbers are an accurate reflection of the number and face value of trust-owned, bank-owned, and/or premium-financed policies in Florida as many responding insurance companies relied on estimates. Further, it is unknown whether these policies, in fact, represent policies present in the secondary market.

60 STOLI Report, supra note 17, at 14-15.
61 Transcript at 119-21.
The second factor contributing to the difficulty in assessing the size of the secondary market in Florida is that it is unknown how many viaticated policies or other life insurance policies have been sold on the secondary market. In addition to policies transacted through licensed viatical settlement providers, the secondary market likely contains a large number of policies acquired by banks, financial institutions, or premium-finance companies upon default of a financing or lending agreement. The exact number of these policies in the secondary market is not known.

In sum, the size of the viatical market in Florida is difficult to assess and, in turn, the size of the secondary life insurance market in Florida is even more difficult to assess given the data currently available to the Office. Additionally, many life insurance companies appear to be largely unaware of the future potential financial impact of viaticated policies. Only eight life insurance companies acknowledged having “procedures in place to evaluate the impact of viaticated policies on the net-present-value of the life insurance book of business.” Many of the life insurance companies actively writing in Florida acknowledged that they had not established procedures to track viaticated policies and had no way of knowing the volume of policies that have been viaticated. Accordingly, insurance companies appear to be unaware of the financial impact of viaticated policies on their current and future portfolio and, consequently, may not be adequately prepared for expenditures that will arise upon the maturity of these investor-owned policies, which are generally less likely to lapse than non-viaticated policies.

B. Viewpoints Presented at the Hearing

The presenters at the public hearing expressed differing views as to the legislative directive. Those views are summarized below.

62 A financial institution that takes an assignment of a life insurance policy as collateral for a loan is not a viatical settlement provider regulated under the Viatical Settlement Act. § 626.9911, Fla. Stat.
1. **Fortress Investment Group**

   Present at the hearing on behalf of Fortress Investment Group, a large investor in the secondary life market, were Mr. Tom Welsh and Mr. Jerry Kroll. Fortress is an investment management firm that manages $54.6 billion in investment assets on behalf of clients that include university endowments, public pensions, and non-profit foundations.\(^{63}\) In 2010, Fortress began buying portfolios of life insurance policies on the secondary market.\(^{64}\) All of the policies were past the standard two-year contestable period and available at reduced rates because other investors were struggling to pay the premiums.\(^{65}\) About 200 of these policies were issued by Phoenix Life Insurance Company, which has asserted in court that a number of these policies are void because they lacked an insurable interest at the time of inception.\(^{66}\)

   In Fortress’s view, secondary market investors provide liquidity to the viatical settlement and secondary markets. Viatical settlement providers frequently look to move the policies into a secondary market and, thus, need access to well-managed secondary market players, which provide the capital necessary to continue to acquire policies.\(^{67}\) In a well-regulated market, investments in life insurance policies are desirable because they are not vulnerable to wild fluctuations like other equities. Fortress asserted that a market will not exist if investors do not believe that there is some degree of certainty and predictability.\(^{68}\)

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\(^{63}\) Transcript at 6-7, 13.


\(^{65}\) Id.

\(^{66}\) Id.

\(^{67}\) Id.

\(^{68}\) Transcript at 14-15.
According to Fortress, “a small handful of insurers,” primarily Phoenix Life Insurance Company, pose a threat to the secondary market that will ultimately reduce Florida seniors’ ability to access the market and achieve the values that they would receive in a well-regulated market. These companies refuse to honor policies owned by investors after collecting premiums for years and are asking courts to invalidate policies from inception for lack of insurable interest.

Fortress contended that the remedy being sought for lack of insurable interest is nothing more than a rescission remedy. According to Fortress, it is a basic principle of law that when one party rescinds an agreement, the opposing party must be put back in the position it occupied when the agreement was entered, which includes returning the premiums paid. However, Fortress asserted that the insurance companies challenging policies are not only seeking to void the policies, but also to keep the premiums. Fortress alleged that they are accomplishing this objective by litigating cases with particularly bad facts and by misleading judges. Fortress asserted that the consequence of such tactics is that investors will refuse to buy policies in a state where a policy can be rescinded after the contestable period and the premiums not returned.

Fortress asserted that Phoenix in particular has tried to game the system in order to avoid paying its obligations. According to Fortress, Phoenix is resisting and denying a large percentage of claims in a demonstrable upward trend that far exceeds the national average.

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69 Transcript at 20.
70 Transcript at 20-22.
71 Transcript at 22.
73 Transcript at 22-24, 26.
74 Fortress asserted that Phoenix resisted or denied less than 1% of claims in 2008 to almost 21% in 2011, as compared to the national average of 1.5%. Fortress submitted a chart illustrating Phoenix’s denial rates. Transcript at 17, 24-25; see also Chart of Life Insurance Policy Resistance/Denial Rates, available at http://www.floir.com/siteDocuments/FortressGPHLDenialRateChart.pdf.
the hearing, Jerry Kroll spoke about his experience handling a case involving Phoenix on behalf of two life settlement funds. When the investors requested a change of ownership, Phoenix responded months later threatening rescission if various documents were not provided. At that point, the investors sued Phoenix, and Phoenix sought to void the policies and keep the premiums.75 Depositions revealed that Phoenix had encouraged its sales personnel to sell policies attractive to investors.76

Although many investors are no longer buying Phoenix policies, Fortress argued that this means that Phoenix’s behavior has dramatically diminished the market value of the Phoenix policies owned by Florida seniors.77 Fortress further argued that there is a “contagion risk” of other insurance companies following suit because Phoenix is generating case law that they can avoid the two-year contestable period by asserting a lack of insurable interest.78

Fortress asserted that investors want a marketplace free of fraud and STOLI policies. They endeavor to do as much underwriting as they can; however, they have access to a more limited data set than what is available to life insurance companies and, as a result, sometimes buying portfolios with STOLI policies is unavoidable. Fortress argued that fraud prevention is best addressed at the front end by the life insurance companies. Fortress contended that the law

75 Transcript at 52-54.
77 Transcript at 27-28.
78 Transcript at 31-32.
79 For example, according to Fortress, investors can find and evaluate the address of the underlying insured in order to figure out whether he or she lives in a neighborhood that suggests that he or she should have a $2 to $3 million life insurance policy. Transcript at 43.
should not allow insurance companies to turn a blind eye to fraud and then later claim a lack of insurable interest, void the policy, and retain the premiums.80

Fortress proposed five legislative changes: (1) make subjective intent irrelevant to insurable interest; (2) prohibit insurable interest challenges after the contestable period; (3) require a notice of validity of the policy from the insurance company within ninety days of inquiry; (4) require return of premiums to the policyowner if a policy is voided; and (5) monitor cost-of-insurance rate increases.81 Each proposal is addressed in detail below in section III.C.

2. American Council of Life Insurers (ACLI)

Mr. David McDowell was present at the public hearing on behalf of the American Council of Life Insurers (ACLI).82 According to its website, ACLI is an association of more than 300 member companies, which advocates for public policy that supports the industry market place and the millions of American families that rely on life insurance products for financial and retirement security.83 ACLI opposed Fortress’s proposed legislative changes.84

Mr. McDowell stated that the issue presented involves two markets. The first is the legitimate life settlement market (termed “viatical settlement” market in Florida law), which has existed for a long time. With respect to these policies, when the insured bought insurance coverage, he or she was buying it to address a legitimate insurance need.85 ACLI does not believe that this market should be abolished as it provides a third option—other than lapse or

80 Transcript at 42-44.
81 Transcript at 33-51.
82 Transcript at 56-57.
84 See Transcript at 67-76.
85 Transcript at 57.
cash surrender—to insureds who no longer need or want their policies. ACLI asserted that this market “is doing just fine.”

According to ACLI, the second market is what the hearing was actually about—a market of stranger-originated life insurance (or “STOLI”), which is not life insurance at all. Those buying STOLI policies suffer no financial consequences when the insureds die. Instead, those investors want the insureds to die as quickly as possible in order to ensure a greater profit. These STOLI policies were disguised to look like legitimate life insurance transactions in order to induce the insurance companies into issuing them. ACLI argued that the notion that insurance companies turn a blind eye to fraud is belied by the fact that the STOLI policies had to be obtained by deceit.

When life insurance companies and regulators became aware of STOLI policies in 2006 and 2007, they both reacted. Because of the combination of legal and regulatory forces, the value of these toxic assets on the secondary market was “absolutely crushed.” These assets were not able to be sold on the legitimate secondary market; however, the hedge funds smelled a bargain. Fortress and other companies were able to buy these blocks of policies for pennies on the premium dollars already paid. In seeking the funds to buy these toxic assets, Fortress issued notices to the investing public, in which it alerted the investing public that they were

86 Transcript at 57, 92.
87 Transcript at 57.
88 Transcript at 57-58.
89 Transcript at 59.
90 Transcript at 60.
91 A recent article stated that Fortress bought the $6.2 billion KBC Bank NV portfolio for $332.5 million in late 2010. It later acquired the SageCrest portfolio with $514 million in face value for $27.6 million in a bankruptcy sale, and the $1.34 billion HM Ruby fund portfolio through a default on a $65 million loan by fund manager Himelsein Mandel Fund Management LLC. See Donna Horowitz, Fortress Told Investors Its Portfolio Could Contain STOLI, THE DEAL PIPELINE (Nov. 20, 2013), http://www.thedeal.com/content/private-equity/fortress-told-investors-its-portfolio-could-contain-stoli.php [hereinafter Horowitz, Fortress Told Investors]. This totals $425.1 million paid for $8 billion in face value.
looking to buy assets that may lack an insurable interest, may have been procured by fraud, that may be subject to litigation and regulatory risk, and may be outright illegal. They told the investing public that if any of these factors came to pass, it would have a significant and profound effect on the value and liquidity of the policies in the portfolio.92

Now, Fortress is having difficulty selling these policies in the legitimate secondary marketplace.93 ACLI opined that the Office should view the legitimate secondary life insurance marketplace’s hesitancy and unwillingness to purchase these policies as a healthy vital sign of a thriving marketplace and not an indication of a weakness that needs to be addressed through legislation.94

In resorting to court, ACLI contended, the life insurance companies are simply seeking to affirm the three legal certainties that have long existed with respect to life insurance. First, if the applicant lies on a life insurance application, the life insurance company can rescind the policy within two years of policy issuance. Second, if the life insurance policy is issued without an adequate insurable interest, it is an illegal contract and is therefore void ab initio. Third, if a life insurance company knew or should have known of problems on the application or problems associated with insurable interest, that life insurance company should bear the consequences. Nothing has changed these legal certainties.95

According to ACLI, whether or not a particular policy can be rescinded, whether or not an insurable interest existed, and whether or not the premiums should be returned depend on the

92 Transcript at 59-61.
93 A recent article stated that Fortress began “shopping around its portfolio in September, only three years after entering the market.” Horowitz, Fortress Told Investors, supra note 91. At this time, Fortress is not selling the $1 billion in Phoenix policies, which are tied up in litigation. See Donna Horowitz, Fortress Shops Life Settlement Portfolio, THE DEAL PIPELINE (Oct. 22, 2013), http://www.thedeal.com/content/restructuring/fortress-shops-life-settlement-portfolio.php.
94 Transcript at 61-62.
95 Transcript at 62-63.
facts of each individual case. It would be difficult to legislate fairness and craft legislation that would adequately address the equitable issues that could crop up in any individual case, which is why no state has tried to do so, despite similar efforts by hedge funds to get legislation passed.96

Mr. McDowell represented Phoenix in the lawsuit referenced earlier. If those depositions presented an accurate reflection of what Phoenix was actually doing at the time, Phoenix would not have been as successful as it has been in court. Phoenix has won the cases that is has because, like a lot of other companies that were duped into issuing these policies, Phoenix has credible issues it brought before the courts, which were able to look at the equities and reach a reasoned decision. Phoenix has only contested eight death claims in the last four years; the majority of the contest has been on policies that are still in force where the insured is still alive.97

If this is really a one-company issue, then there’s no reason for legislation. The legitimate marketplace is doing just fine, and legislation would encourage toxic assets in the marketplace.98 Life insurance companies do not have any interest in issuing fraudulent policies. Further, life insurance companies have generally been seeking rescissions while the insured is still alive and not collecting the premiums until the insured dies before challenging the policies. Moreover, life insurance companies do adequately police their agents.99

ACLI explained that STOLI transactions are concealed from the insurance companies and disguised to look like normal life insurance transactions.100 During the underwriting

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96 Transcript at 62-65. Fortress provided the Office with copies of legislation that was proposed in Connecticut (Bill No. 409 in 2012 addressing cost of insurance increases), Delaware (HB 87 in 2013 providing for premium-return if a policy is voided), and Minnesota (HF1031 in 2013 providing for premium refund and the right to seek a judicial determination of policy’s validity if the insurance company refuses to state that it will not contest a policy for lack of insurable interest within 120 days of receipt of a verification of coverage request). The text of these proposed bills is available at [http://www.flori.com/siteDocuments/FortressIDEHB87.pdf](http://www.flori.com/siteDocuments/FortressIDEHB87.pdf).

97 Transcript at 66-67, 89.

98 Transcript at 76.

99 Transcript at 87-88, 90.

100 Transcript at 78-79.
process, if requests for information continually result in fraudulent information being produced, at some point it is no longer the fault of the insurance company.\textsuperscript{101}

3. Life Insurance Settlement Association (LISA)

Present at the hearing on behalf of the Life Settlement Association (LISA) were Mr. Darwin Bayston and Mr. Michael Freeman.\textsuperscript{102} According to LISA’s website, LISA, established in 1994, is the oldest and largest trade organization in the life settlement market with the goal of advancing the highest standards for market participants and promoting education and awareness.\textsuperscript{103}

According to LISA, the life settlement market (termed “viatical settlement” market in Florida) has evolved from a largely unregulated viatical marketplace to today’s well-regulated market, which has provided billions of dollars to tens of thousands of policyowners. This market is one that includes a lot of lower-to-middle class policyowners in need of financial resources for retirement, and several states are considering the use of life insurance policies for long-term care, including policyowners qualifying for Medicaid.\textsuperscript{104} Any market needs liquidity, and in the current market, the money for the sale of policies comes from institutional investors, which buy portfolios of policies that have already been viaticated.\textsuperscript{105}

LISA stated that it was referring to life settlements, not STOLI.\textsuperscript{106} The litigation being brought by insurance companies is not against life settlement companies and does not concern policies assigned through a regulated life settlement transaction.\textsuperscript{107} Instead, STOLI policies are

\begin{footnotes}
\footnote{101}{Transcript at 91-92.}
\footnote{102}{Transcript at 93, 103.}
\footnote{103}{See LISA, \url{http://www.lisa.org} (last visited Nov. 20, 2013).}
\footnote{104}{Transcript at 94.}
\footnote{105}{Transcript at 101-03.}
\footnote{106}{Transcript at 95.}
\footnote{107}{Transcript at 104-05.}
\end{footnotes}
sold via selling the beneficial interest in a trust, or in the case of premium-financed schemes, there is a relinquishment or abandonment of the policy. The seventeen licensed viatical settlement providers in Florida are not the entities involved in STOLI transactions. There should be a benefit of having a regulated transaction.108

LISA disagreed with ACLI’s statement that investors hope insureds die as quickly as possible. According to LISA, this is not true; rather, the investor assembles an investment portfolio in an attempt to achieve a certain cash flow.109

LISA asserted that certain issues either impede the ability of seniors to enter into a life settlement transaction or diminishes the value received by seniors when they sell those policies. These issues are discussed in more detail below in section III.D. LISA also supported premium return legislation. The life insurance company conducts due diligence at the inception of the policy.110 When a life settlement occurs, the life settlement provider is required to go back to the insurance company and ask for verification of coverage, which effectively notifies the insurance company of the potential sale of the policy. This step provides another opportunity for the life insurance company to evaluate the policy.111 Insurance companies know which policies are being sold, and they treat those changes of ownership differently. They track life settlements and treat them differently at every stage.112

Under Florida law, there is also a requirement that the life settlement company, as part of its anti-fraud plan, evaluate the policy. This requirement includes looking at the original underwriting of the policy, the individual or entity paying the premiums, the issue of insurable

108 Transcript at 118-20.
109 Transcript at 99-100.
110 Transcript at 109.
111 Transcript at 107-11.
112 Transcript at 122-23.
interest, and any potential fraud or misrepresentation in the sale of the policy. Despite each of these steps, sometimes policies will still slip through that should never have been issued.\textsuperscript{113}

LISA argued that legislation should be passed to allow for the return of premiums if the policy has gone through a regulated life settlement transaction. LISA asserted that there is a level of scrutiny and diligence in life settlement transactions, and the investors were not part of any transaction that was originating the policy improperly.\textsuperscript{114} At the point of sale, investors need certainty and clarity that they will be restored to their original position if the policy is voided.\textsuperscript{115}

LISA asserted that anything that is perceived as increasing the risk to the investors results in them paying a lower price to the consumer. If actions are taken that reduce the perception of risks that investors have, then the benefit flows back to the seniors who are selling policies.\textsuperscript{116} LISA has provided its suggested language for a premium-return amendment.\textsuperscript{117}

4. Institutional Longevity Markets Association (ILMA)

Mr. Thomas Weinberger spoke on behalf of the Institutional Longevity Markets Association at the public hearing. ILMA was formed by institutional investors and leading investment banks that were focused on longevity and mortality markets and life settlements.\textsuperscript{118} These investors participate primarily in what ILMA called the tertiary market but is termed the “secondary market” under Florida law (the subsequent trading after a policy is first sold). The

\textsuperscript{113} Transcript at 109.
\textsuperscript{114} Transcript at 109-10, 114-18.
\textsuperscript{115} Transcript at 111-12.
\textsuperscript{116} Transcript at 124.
\textsuperscript{117} LISA Submission, \textit{supra} note 26, at 7.
\textsuperscript{118} Transcript at 125. Members include Wells Fargo, Wilmington Trust, Credit Suisse, Fortress, Neo Partners, and other groups, some of whom are investors on behalf of pension funds. \textit{Id.}
Institutional Longevity Markets Association (ILMA) submitted a written comment supporting each of Fortress’s proposed legislative changes.\footnote{See ILMA, Letter to Commissioner McCarty at 3, available at http://www.flor.com/siteDocuments/ILMAcommentstoOIR.pdf [hereinafter ILMA Submission].}

According to ILMA, the life settlement industry provides a great service to seniors and a reasonable return to institutional investors. In ILMA’s view, the issue presented at the hearing was not STOLI-related, but rather whether what it called the secondary market (termed the “viatical settlement” market in Florida) will continue to exist in Florida. ILMA asserted that the tertiary market (termed the “secondary settlement” market in Florida) is crucial because it provides liquidity. Investors provide the capital that ultimately feeds the life settlement market.\footnote{Transcript at 125-26.} ILMA estimates that the size of secondary and tertiary markets is probably in the billions of dollars.\footnote{Transcript at 136.}

The institutional investors seek protections because investors who buy blocks of policies have limited access to information. Mr. Weinberger stated that he is actively involved in helping the companies do the due diligence on these policies, and they do not have access to the insureds. Typically, the investors are provided with some sale documentation that was provided at the time of the life settlement. When an investor buys a policy, it receives updated medical information. However, due to privacy laws, there are significant limitations on who can contact the insured and when. Despite the limited information available, investors do a good job of identifying fraudulently originated policies and refusing to buy them.\footnote{Transcript at 126-30.}

Insurance companies, however, are in the best position to do the proper diligence—when the policy is originated. In ILMA’s view, it is simple for insurance companies to determine what

is going on with the policy in the two-year contestable period. The insurable interest issues are going to arise in only a small subset of policies—large face-value whole life policies with older age issuances. All the insurance companies need to do is take the inexpensive step of contacting the insured six months after origination. This will enable them to quickly discern if the insured sold the policies. Unfortunately, insurance companies are frequently not interested in taking that step. Institutional investors cannot take the same steps as the insurance companies years later.\textsuperscript{123}

ILMA disagreed with ACLI that there are legal certainties, contending that uncertainty in the market is driving the interest in reforms and legislation. The issue of whether a policy can be challenged after the two-year contestable period is far from settled in Florida. Limiting insurable interest challenges to the contestable period will not open the door to fraud.\textsuperscript{124}

The secondary life market is needed and is poised to grow. Seniors nearing retirement age need to be able to settle their policies to either fund a comfortable retirement or perhaps pay for long-term care needs.\textsuperscript{125} Some states, including Florida, have been considering whether they should get in the market of life settlements in order to fund Medicaid long-term care costs. In order for this market to grow, there needs to be greater legal certainty. The balance of equities has to happen on a more global scale rather than just on individual policy issuances.\textsuperscript{126}

ILMA asserted that STOLI transactions have largely disappeared from the market, and insurance companies and investors have become better at identifying them. ILMA is not aware of any institutional investors that are actively participating in STOLI transactions; the most egregious practices probably took place in the 2007-2008 period. However, this does not obviate the need for more certainty in the market, especially in Florida courts. Because of this

\textsuperscript{123} Transcript at 131-32.
\textsuperscript{124} Transcript at 128-29.
\textsuperscript{125} Transcript at 130.
\textsuperscript{126} Transcript at 136-37.
uncertainty, the prices that investors are willing to pay for Florida policies are much lower than the rest of the country.\textsuperscript{127}

5. Professional Benefits, Inc.

Mr. James Tollerton of Professional Benefits in Sarasota, Florida, was invited by representatives at the Florida Chapter of the National Association of Insurance and Financial Advisors (NAIFA) to speak as a typical Florida insurance agent about his experiences. In Mr. Tollerton’s view, the further we get away from the essential underpinnings of the life insurance industry of insurable interest, the more slippery the slope. When a stranger owns a life insurance policy on an insured, the insured does not know who owns the policy, where the policy is, or what is going to happen. It is a very uncomfortable prospect. Most of the seniors that settle their policies have no idea of the potential tax implications and have no idea what is happening.

Mr. Tollerton does not have a great deal of experience with viatical settlements personally, but he did assist in settling a policy for a friend fifteen years ago who had cancer. Mr. Tollerton became very uncomfortable with the process, because he received phone calls every few months inquiring as to how his friend was doing. In another situation, a senior sold his $2 million policy and subsequently realized that he no longer knew who owned his policy.

Mr. Tollerton expressed that the bottom line from an insurance agent’s perspective is that an agent is in the business of insuring lives for families, businesses, and charities in some instances. The vast majority of the agents in NAIFA and legitimate agents in Florida have no interest in participating in the viatical settlement market because of the ongoing problems that naturally happen once a policy is sold. The secondary life market can be analogized to the

\textsuperscript{127} Transcript at 138-39.
mortgage industry, where mortgages were packaged together and sold in the secondary market, which brought about a great deal of trouble.128

6. Florida Insurance Council (FIC)

Mr. Paul Sanford spoke at the hearing on behalf of the Florida Insurance Council (FIC), Florida’s largest insurance trade association.129 Mr. Sanford stated that when an insurance company receives a verification of coverage request, it is unlikely that any substantial underwriting will take place at that time. With respect to premium-return legislation, the facts are different in every case and a court needs to be able to assess those facts to dispense equity.

The underwriting practices by life insurance companies are about as strong as they can get, unless they expend huge sums of money and large amounts of time, which will increase the cost of insurance. The larger the policy, the more checking that takes place. However, Mr. Sanford has seen, for example, situations in which an insurance company received financial statements from CPAs that did not exist.

In FIC’s view, if legislation is considered, it would be good to review the National Association of Insurance Commissioner’s (NAIC) model act on STOLI transactions,130 in particular, the five-year provision on nonrecourse premium financing and the limitations on transferring these policies and combine those provisions with the trust provisions from the National Conference of Insurance Legislators (NCOIL) model act,131 which would get to the

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128 Transcript at 139-42.
131 NCOIL Life Settlements Model Act (Nov. 17, 2007); see also NCOIL Press Release, NCOIL Closes in on Illegal STOLI, Unanimously Adopts Amended Model Act (Nov. 20, 2007) (describing the model act), http://www.ncoil.org/HomePage/2007/LifeSettlementsPR.pdf; see also Martin, supra note 8, at 201 (discussing the NCOIL Model Act provisions relating to STOLI).
heart of the situations where STOLI originators are able to deceive insurance companies. The implementation of these two measures could possibly eliminate STOLI transactions, which appears to be the real hazard that the secondary market is having.

C. Legislative Changes Proposed by Fortress

Fortress suggested five legislative changes to address what it perceives as the lack of protections for investors in the secondary life insurance market, asserting that one or all of the legislative changes would bring greater certainty and stability to the market. The Institutional Longevity Markets Association (ILMA) supported each of these proposed legislative changes.\(^{132}\) The American Council of Life Insurers (ACLI) opposed these changes. This report discusses each of Fortress’s proposed legislative changes in turn.

1. **Make subjective intent irrelevant to insurable interest.** Fortress’s first proposed legislative change was to clarify that an insured’s subjective intent is irrelevant to the issue of insurable interest.\(^{133}\) Fortress asserted that “[i]nsurers have been able to cloud the issue and successfully create uncertainty in the law where none should exist. By doing so, they have chilled the market. To curb such baseless litigation and provide market stability, the [Office] and Florida Legislature should make clear that intent is irrelevant to the insurable interest requirement under Florida law.”\(^{134}\) In the hearing, Fortress emphasized that, in its view, the subjective intent of an insured, who may have died by the time the issue is in dispute, is a difficult and unpredictable test to apply.\(^{135}\) As a specific example, Fortress pointed to the 2012 federal court decision of *Sciaretta v. Lincoln National Life Ins. Co.*,\(^{136}\) asserting that in that case,

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\(^{132}\) ILMA Submission, *supra* note 119, at 3.

\(^{133}\) See Transcript at 33-37.

\(^{134}\) Fortress Written Submission, *supra* note 72, at 12.

\(^{135}\) Transcript at 35-36.

although the policy was not actually sold, the insurance company nonetheless argued that the insured, Mr. Cotton, had considered settling the policy and, therefore, there was no insurable interest and the policy was void \textit{ab initio.}\textsuperscript{137}

ACLI responded that a determination of insurable interest rarely involves consideration of subjective intent. According to ACLI, the Delaware Supreme Court and other courts have instead looked at the factual circumstances of the policy issuance and decided, based on that set of facts, whether there was an insurable interest.\textsuperscript{138}

A review of the \textit{Sciaretta} decision reveals that the circumstances surrounding the policy indicated many of the classic hallmarks of a STOLI arrangement. The insured, Mr. Cotton, had entered into an Exclusive Rights Agreement with Wealthmodes, LLC, in which Wealthmodes paid Mr. Cotton a fee that was equal to the initial premiums owed to Lincoln, in exchange for a twelve-month exclusive right to arrange for the future sale of any life insurance policies it obtained for Mr. Cotton.\textsuperscript{139} Shortly thereafter, Mr. Cotton formed an irrevocable trust and sought an $8 million life insurance policy from Lincoln. The application represented that Mr. Cotton’s annual income was $730,000, although his tax return from the previous year reflected an annual income of only $170,999. Mr. Cotton also represented in the application that the policy was not being funded via premium financing loan or with funds borrowed, advanced, or paid from another person or entity and that he would not receive any compensation as a result of the policy being issued.\textsuperscript{140} Subsequently, Lincoln issued a $5 million policy to the trust and Mr. Cotton paid for the initial premiums with funds received from Wealthmodes. After the initial premium payments, the trust obtained a premium-finance loan in order to continue to pay

\textsuperscript{137} Transcript at 37; \textit{see also} Fortress Written Submission, \textit{supra} note 72, at 1, 7-8.
\textsuperscript{138} Transcript at 70.
\textsuperscript{139} \textit{Sciaretta}, 899 F. Supp. 2d at 1321, 1325.
\textsuperscript{140} \textit{Id.} at 1321.
premiums. The premium-finance company marketed the policy to secondary market investors, receiving two offers to purchase the policy. Almost two years after the policy was issued, Mr. Cotton was diagnosed with terminal cancer and died six months later. Before Mr. Cotton passed away, the premium-finance company notified the trust that the loan must be repaid in order to satisfy the loan and retain the policy; the premium-finance company later foreclosed on the policy in satisfaction of the loan.

The Southern District of Florida ruled that, consistent with Florida contract law and two other Florida decisions (Pruco Life Insurance Co. v. Brasner and AXA Equitable Life Insurance Co. v. Infinity Finance Group), there is an implied covenant of good faith that attaches to Florida’s insurable interest requirement. Thus, the Southern District held, if the insurance policy at issue was procured with the intention that it would be assigned or otherwise transferred to a person or entity with no insurable interest in the insured, it is void ab initio.

After reviewing the circumstances and the arguments made by the parties, the Southern District found that there was a genuine issue of material fact and denied the life insurance company’s motion for summary judgment that the policy was void ab initio because it lacked an

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141 Id. at 1321-22.
142 Id. at 1322, 1325-26.
143 Id. at 1322.
144 Id. at 1322, 1325-26.
145 The Southern District quoted a Eleventh Circuit Court of Appeals decision, which stated that “[u]nder Florida law, every contract contains an implied covenant of good faith and fair dealing, requiring the parties follow standards of good faith and fair dealing designed to protect the parties’ reasonable contractual expectations.” Id. at 1324 (quoting Centurion Air Cargo, Inc. v. United Parcel Serv. Co., 420 F.3d 1146, 1151 (11th Cir. 2005)).
148 Sciaretta, 899 F. Supp. 2d at 1324-25. Similarly, the Southern District of Florida held in a prior case, AXA Equitable Life Ins. Co., that while “Florida permits the assignment of life insurance policies to persons without an insurable interest in the life of the insured,” that “this rule extends only to assignments made in good faith, and not to sham assignments made simply to circumvent the law’s prohibition on ‘wagering contracts.’” AXA Equitable Life Ins. Co., 608 F. Supp. 2d at 1356.
149 Sciaretta, 899 F. Supp. 2d at 1325.
insurable interest at inception. Subsequently, at trial, a jury found that it was not intended, at the time of procurement, that the policy would later be assigned or transferred to someone with no insurable interest.

2. Prohibit insurable interest challenges after the two-year contestable period.

Fortress’s second proposed legislative change was to prohibit insurable interest challenges after the two-year contestable period. In Fortress’s view, it has been long settled that life insurance companies are afforded the two-year window of time to complete underwriting, identify red flags, and determine if a policy has been issued based on misrepresentations. Fortress contended that insurance companies have attempted to contravene this two-year period by fixating on insurable interest, and the resulting uncertainty diminishes the value of policies and threatens to eliminate or significantly curtail the market. The case law is unsettled as to this issue.

ILMA similarly asserted that “[a]ny question as to whether or not a policy’s validity can be challenged ad infinitum adds prohibitive uncertainty in the market for the sale of life insurance policies, depriving the consumer of the maximum value of her asset.” At the hearing, ILMA asserted that the inability to challenge the lack of insurable interest after the two-year contestable period will not open the door to fraud. IMLA stated that a New York case many years ago held that a policy cannot be challenged on any basis after the end of the contestable period, and it did not lead to a rampant increase in fraud in New York. There are red flags; the

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150 Id. at 1325-26.
152 Transcript at 38.
153 Fortress Written Submission, supra note 72, at 13.
154 Transcript at 38-39.
155 ILMA Submission, supra note 119, at 3.
156 Transcript at 129.
insurance companies know what they are, but sometimes choose to ignore them. ILMA argued that the balance of equities has to happen on a more global scale rather than with individual policies.157

ACLI responded that most states in the country have rejected the principle that there cannot be any insurable interest challenge after the contestable period, reasoning that the public policy behind insurable interest is too important to be subject to a two-year bar. Restricting insurable interest challenges to the two-year contestable period would mean that an illegal contract would not be illegal based on a provision contained in the illegal contract. According to ACLI, such a rule would have unintended consequences. For example, in Florida, there was a case where the insured found out that someone she did not know had forged applications and taken out nine different life insurance policies on her life. If she had found out after the two-year period, there would be nothing that she or anyone else could do to address the situation.158

A review of the case law reveals that the courts are divided on the issue of whether an incontestability clause applies to bar a claim that a contract is void ab initio. The majority view allows insurable interest challenges after the two-year contestable period. As summarized by a recent decision from a Florida federal district court in Pruco Life Insurance Co. v. Brasner159:

Courts following the majority view hold that incontestability clauses have no effect where a policy is void ab initio for lack of an insurable interest. Such courts will allow an insurance company to raise a void ab initio claim even after the incontestability period has expired. In contrast, courts following the minority view hold that incontestability clauses bar insurance companies’ claims regarding the validity of insurance policies.

Florida law embraces both the public policy that prohibits an insurance company from contesting the policy after the contestability period expires and the public policy that an insurable interest is necessary for an insurance policy to be valid in the first place. See Fla. Stat. § 627.404(1); Fla. Stat. § 627.455. Neither

157 Transcript at 133-34, 136.
158 Transcript at 70-71.
party cites binding caselaw requiring this Court to reconcile one policy over the other. However, at least one other court in the Southern District of Florida has conformed to the majority view in the face of a challenge regarding lack of insurable interest after a contestability period had expired. See Rubenstein, No. 09–21741–CIV–UNGARO. In Rubenstein, Judge Ungaro held that “if the Policy is void ab initio because an insurable interest is tacking, the incontestability clause would be of no effect.” Rubenstein, No. 09–21741–CIV–UNGARO, DE 28 at 5, ¶ 4. Furthermore, the minority view decisions are distinguishable from this case . . . as the Florida legislature has promulgated statutes regarding both policies. See Fla. Stat. § 627.404(1); Fla. Stat § 627.455.[160]

The court in that case reasoned that although a compelling policy argument was presented that the minority view encourages insurance companies to timely investigate policies, protects policyowners, and prevents insurance companies from later receiving a windfall, “there is a compelling countervailing view that allowing an incontestability period to bar a lack of insurable interest claim actually encourages fraud.”[161] “[U]nder the minority view, ‘if bad actors can disguise their fraud for two years, their hands; are washed clean . . . and they are free to collect on their ill-gotten gains.’”[162]

A subsequent Florida federal district court in Pruco Life Insurance Co. v. U.S. Bank[163] agreed with the minority view. The court reasoned that in Florida, an insurance company may not challenge a policy based on fraud outside the contestable period and, in the STOLI context, a lack of insurable interest may not be divided from the fraud that created it: “[W]hether the fraud renders the policy voidable or void ab initio is inconsequential; this holds especially true in this case, where [the] lack of insurable interest claim is ultimately traceable to fraud.”[164]

3. Require a notice of validity from the insurance company within 90 days of inquiry. Fortress’s third proposed legislative change was to require insurance companies to,

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[160] Id. at *5-6 (citations and footnotes omitted).
[161] Id. at *6.
[162] Id. (quoting Settlement Funding, LLC v. AXA Equitable Life Ins. Co., 06 CV 5743(HB), 2010 WL 3825735, at *5 (S.D.N.Y. Sept. 30, 2010)).
[164] Id. at *5.
upon inquiry by an investor, provide a notice as to a policy’s validity within ninety days.\textsuperscript{165} Fortress argued that this requirement would provide increased security in the marketplace because, “[r]ather than be permitted to rebuff good faith efforts to receive assurances of a policy’s validity . . ., insurance companies should be required to offer a definitive response. For now, insurance companies are content offering no information and forcing their policyowners to continue making premium payments.”\textsuperscript{166} ILMA added that “[i]f, after two years of policy issuance the insurer has any question as to the validity of a policy, it should be prepared to make those concerns known when asked to do so by a purchaser of a policy,” which would provide stability to the market.\textsuperscript{167}

ACLI countered that this legislative change would essentially privatize the public policy of insurable interest and take it out of the hands of the courts. The life insurance company, however, does not have access to subpoena powers, information from third parties, or even really access to the insured at that point. Instead, the insurance company would be forced to make an insurable interest determination based on information it already had in its possession when it underwrote the policy. The investors, on the other hand, have unfettered access to the insured.\textsuperscript{168}

The Florida Insurance Council (FIC) also opposed this legislative change. FIC asserted that when an insurance company receives a verification of coverage request, it is a question of whether the policy is in force and whether the premiums are paid. FIC argued that it is unlikely that any substantial underwriting is going to take place at that time, so to use it as a vehicle to cut off any questions about insurable interest seems to be way far afield.

\textsuperscript{165} Transcript at 39. \\
\textsuperscript{166} Fortress Written Submission, \textit{supra} note 72, at 13. \\
\textsuperscript{167} ILMA Submission, \textit{supra} note 119, at 3. \\
\textsuperscript{168} Transcript at 72-73.
4. Require return of premiums if a policy is voided. Fortress’s fourth proposed legislative change was to require, even when a life insurance policy is deemed void, that the insurance company return the premium payments.169 Fortress asserted that despite the straightforward principle of law that when a party rescinds an agreement, the opposing party must be put back in the position it occupied when the agreement was entered, some insurance companies have successfully convinced courts that they should be entitled to the premiums paid under the policy. Fortress argued that not only does such reasoning conflict with well-settled law, but “it creates one of the most perverse incentives imaginable” and is chilling the market.170 Fortress argued that the proper remedy should not be to undercut the law of rescission, but rather to execute on remedies against those that are actually complicit in the fraud.171 In Alabama172 and Georgia,173 the insurable interest statutes require the return of premium payments without interest in the event a contract is void.

LISA also supported premium-return legislation and suggested specific wording for a proposed amendment in its written submission.174 LISA argued that although the law has required premium-return for over 150 years, insurance companies “are issuing policies that violate insurable interest laws, failing to take the proper steps to prevent or detect such improperly issued policies, refusing to respond to requests from owners to verify the validity of

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169 During the 2012 legislative session, an amendment was proposed to House Bill 1101 to require the refund of premiums, plus interest, if a life insurance policy is terminated or deemed to be void (including for lack of insurance interest). The amendment was withdrawn.

170 Fortress Written Submission, supra note 72, at 14.

171 Transcript at 47.

172 See § 27-14-3(f), Ala. Code (2013) (“In the case of a void contract, the insurer shall not be liable on the contract but shall be liable to repay to the person, or persons, who have paid the premiums, all premium payments without interest.”). This provision was added in 1994. See ch. 94-576, Ala. Laws.

173 See § 33-24-3(i), Georgia Code (2013) (“In the case of a void contract, the insurer shall not be liable on the contract but shall be liable to repay to the person or persons who have paid the premiums all premium payments without interest.”). This provision was added prior to 2003.

174 See LISA Submission, supra note 26, at 7.
the policies, and then, after collecting the premium for years and years, attempting to keep those premiums.” LISA asserted that the amendment would not require premium return for STOLI policies, but rather for regulated viatical settlement contracts. Because these policies and the subsequent regulated viatical settlement transactions are the subject of “rigorous vetting,” insurance companies should be required to return premiums even when a policy is rescinded. LISA argued that this amendment would “ensure uniform public policy,” would “remove unjust enrichment by any party” and would “ensure the property rights and market value of life insurance for owners of life policies, including investors, who pay premiums and have not violated insurable interest laws.”

ILMA likewise asserted that if the insurance company is not enjoined from keeping the premiums if a policy is determined to be invalid after the contestable period, “this would provide an incentive for the insurer to be lax in its underwriting and its further examination as to the validity of the policy, because if it was later determined that the policy was invalid, it gets to keep the premiums that were paid in good faith by the purchaser.”

In opposition to this proposed change, ACLI submitted a letter from Valmark Securities, an early entrant to the life settlement brokerage business that stated that it “favors a well-organized and regulated secondary market for life insurance” and that “see[s] the benefit of helping a select group of older clients get true market value for their policies.” In that letter, Valmark Securities argued against a premium-return requirement. Specifically, Valmark Securities contended that Fortress knew it was purchasing policies with the indicia of STOLI and is now seeking premium-return legislation in order to profit from these policies it bought on the

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175 id. at 7-8.
176 ILMA Submission, supra note 119, at 4.
secondary market at a deep discount.\textsuperscript{178} Valmark Securities disagreed that such a legislative change is necessary in order to provide stability to the current market:

It is patently false, as the investors’ interests assert, that unless certain states enact legislation requiring the return of premium upon rescission, the availability of funding for seasoned life insurance policies (those originally purchased to protect families or businesses as opposed to being purchased for speculation will be ruined. We can tell from the policies being purchased today, that the market has adjusted and smart investors have adjusted their buying parameters to buy only seasoned policies excluding policies conceived in fraud. In fact, by rewarding investment in speculative pools of policies based on fraud several years ago might, draw capital away from pools of seasoned policies now being assembled that are from client[s] who purchased these policies to protect their families or business.\textsuperscript{179}

Valmark Securities stated that “[i]n those cases where the [insurance] companies have prevailed, fraud was rampant and those who assisted its commission had full knowledge of what was occurring in providing the funds. . . . [W]hen fraud is proven in a court of law, the speculators should not profit from having their premiums returned.”\textsuperscript{180}

At the hearing, ACLI contended that, contrary to Fortress’s assertion that premium refund is a bedrock principle, rescission is an equitable remedy and the court is allowed to weigh the equities and evaluate the facts of each case. Some courts have ruled that the public policy behind insurance fraud is so strong that they were not going to force a life insurance company to give back premiums to the entity that defrauded it, because doing so would make life insurance fraud a low-risk, high-reward proposition. Other courts have ordered premium return, but have allowed the life insurance company to offset against those premiums damages that it suffered separate and apart from the mere issuance of the policy. Finally, courts, including a Florida court, have ruled that if a life insurance company knew or should have known that there was an

\begin{flushright}
\textsuperscript{178} Id. at 2.
\textsuperscript{179} Id. at 2-3.
\textsuperscript{180} Id. at 3.
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insurable interest concern, it is not entitled to retain premiums. Courts across the country have simply applied the three legal certainties of the law to reach equitable resolutions. 181

The FIC also opposed this legislative change, arguing that in order to dispense equity in these cases, it is necessary to ensure that the parties who participated in the wrongdoing are punished to some extent, and those who did not are not punished. The only way such an individualized assessment can happen is through the courts. Requiring a return of premiums in every one of these circumstances may guarantee a large return on a risky investment that was bought with the knowledge of what was being bought. 182

A review of the case law in Florida reveals that rescission “is an equitable remedy where the primary obligation is to undo the original transaction and restore the former status of the parties.”183 As a general rule, restoring the former status of the parties would require the life insurance company to return the premiums paid. However, at least one case from the Fifth District of Florida has distinguished contracts that are void ab initio, holding that “as a general rule, contracts that are void as contrary to public policy will not be enforced by the courts and the parties will be left as the court found them. We see no reason to depart from the general rule where, as in the instant case, the party seeking to enforce the contract is the only party who engaged in deceptive and misleading conduct at the time the contract was entered into.”184 Accordingly, the Fifth District refused to order the refund of the premiums paid to the insurance company. 185 A federal district judge, however, in Pruco Life Insurance Co. v. Brasner, considered departing from this rule when evidence arose that the life insurance company may

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181 Transcript at 67-69.
182 Transcript at 145.
183 TTSI Irrevocable Trust, 60 So. 3d at 1150.
184 Id.
185 Id.
have been on notice of fraud and turned a blind eye to red flags that if timely and properly investigated would have led the insurance company to rescind or seek to void the policy before it was sold to a purchaser on the secondary market.186

5. Require monitoring of any cost-of-insurance rate increases. Fortress’s fifth, and final, legislative proposal was to require the Office to monitor cost-of-insurance rate increases to prevent insurance companies from discriminatorily targeting policyowners that are investors. Investor-owned policies can be identified because when an investor buys a permanent life insurance policy, it does not put extra premium into the product to accumulate value, but rather just enough to keep the policy in force. Fortress asserted that Phoenix identified these policies and targeted them for a discriminatory rate increase in an apparent attempt to force the investors to decide to allow the policy to lapse because of the rate increase.187

Fortress contended that “[i]f investors on the secondary market must accept that any policy they purchase may be arbitrarily subject to premium increases, it decreases the worth of these policies. Accordingly, like many other states, Florida should protect its seniors by scrupulously monitoring and investigating any suspicious cost of insurance rate increases.”188 ILMA stated that “[r]ate increases should only occur in accordance with the provisions of the policy. To arbitrarily and discriminatorily impose premium increases because of the status of the owner of the policy would unnecessarily and illegally reduce the value of the policy to the consumer.”189 Fortress stated that if a policy has been in force for a number of years,

187 Transcript at 48.
188 Fortress Written Submission, supra note 72, at 14-15.
189 ILMA Submission, supra note 119, at 4.
preapproval of a rate increase should be required, which would simply require that the insurance company explain to the Office the reason behind the rate increase.190

ACLI responded that cost-of-insurance increases are heavily regulated by any state, and the language that is included in life insurance policies with respect to cost-of-insurance increases is usually specifically approved by state regulators. ACLI argued that in the rare circumstances that life insurance companies do not follow the language in the policies, the proper remedy is to either complain to the regulators or to the court. In ACLI’s view, the notion that legislation is needed in order to deal with these issues is unfounded.191

D. Legislative Issues Asserted by LISA

In addition to supporting a premium-return amendment, which is discussed above, LISA identified five other issues that, in its view, should be addressed or corrected via legislation.192 Those issues are set forth below.

1. Nonpayment of interest on death claims. According to LISA, life insurance companies often fail to pay statutorily and contractually required interest on death benefits, depriving beneficiaries of the total proceeds due.193 LISA asserted that no interest was paid on 3.4 percent of 1,003 viaticated policies. In 70% of those cases, the insurance company paid the interest once notified of the deficiency.194 Viatical settlement providers or institutional investors in the secondary market know how to remedy the situation. However, if the beneficiary is unaware of the entitlement to interest, such as may be the case with seniors, the interest remains

190 Transcript at 51.
191 Transcript at 75-76.
192 See LISA Submission, supra note 26, at 3-6; Transcript at 95-98, 105.
193 Florida law requires payment of interest on death benefits. See § 627.4615, Fla. Stat. (“When a policy provides for payment of its proceeds in a lump sum upon the death of the insured, the payment must include interest, at an annual rate equal to or greater than the Moody's Corporate Bond Yield Average-Monthly Average Corporate as of the day the claim was received, from the date the insurer receives written due proof of death of the insured.”).
194 LISA Submission, supra note 26, at 3.
unpaid. LISA recommended that the issue be examined and laws be enacted in order to ensure that life insurance beneficiaries receive all of the benefits due from a death claim.195

2. Unauthorized changes of ownership data by insurance companies. LISA asserted that from November 2009 through July 2012, insurance companies made 944 unauthorized changes to ownership data on policies without authorization or knowledge of the policyowner. Although such changes may not be deliberate, they are detrimental—more than 35% of these changes could lead to a loss of coverage. Thus, LISA recommended examining the issue of unauthorized changes to ownership data and enacting laws to ensure that ownership data for life insurance policyowners is protected from unauthorized changes.196

3. Obstruction in obtaining verification of coverage. LISA asserted that a number of insurance companies obstruct policyowners and life settlement providers and brokers from obtaining verifications of coverage. In LISA’s view, these actions impair the market for seniors, and in some cases, the process becomes so complicated or lengthy that the transaction is not completed or the value paid for the policies is negatively affected. LISA also asserted that insurance companies refuse to honor the investor owners’ requests for policy information. Thus, LISA requested legislation to ensure that the insurance companies provide a verification of coverage and policy information.197

4. Preventing life insurance producers or agents from advising or being involved in viatical settlement transactions. The next issue asserted by LISA was that insurance companies are prohibiting licensed life insurance producers from advising and assisting policyowners with life settlements via the use of false information, threats of economic

195 Id. at 3; see also Transcript at 96.
196 LISA Submission, supra note 26, at 3-4; Transcript at 96-97.
197 LISA Submission, supra note 26, at 4; Transcript at 97.
sanctions, and termination. Seniors consider their agents to be a source of financial advice and counsel and, consequently, this prohibition creates a negative impression of a viatical settlement transaction. Accordingly, LISA suggested examining insurance companies for violations of the Viatical Settlement Act and the Unfair Insurance Trade Practices Act and enacting laws to ensure that insurance companies do not impair insurance producers from being able to advise and assist their clients with viatical settlements.198

5. Life expectancy provider registration requirement. Finally, LISA argued that certain provisions of the Viatical Settlement Act are outdated, fail to provide consumer protection, and impair the functioning of the viatical settlement market for seniors. In LISA’s view, not only is the requirement ineffective and improperly viewed as a validation of registered life expectancy providers, it is impairing the functioning of the market. The requirement does not allow for viatical settlement providers to use expectancies generated in-house. Thus, LISA suggested that the Legislature repeal all provisions pertaining to life expectancy providers, including the prohibition on a viatical settlement provider or broker from being an owner or office, director, or employee of a life expectancy provider.199

IV. CONCLUSION

Based on the materials submitted and testimony provided, there appear to be adequate protections for purchasers of life insurance policies in the secondary life insurance market to ensure that the market continues to exist. The five legislative changes proposed by Fortress, and supported by ILMA, appear to be proposed in order to address what Fortress asserted is only a “small handful,”200 or “2 percent,”201 of insurance companies seeking to, in Fortress’s view,
improperly invalidate policies. The current legal structure provides an avenue of relief, and the courts are addressing these issues by applying equitable principles based on the fact-specific circumstances of each case.

There is a significant concern that enacting these legislative changes may have the unintended consequence of encouraging STOLI and fraud. An attendant problem to the existence of STOLI schemes is that individuals are encouraged at the outset to procure more life insurance than would be needed if being purchased for legitimate insurance purposes. This treatment of life insurance solely as a commodity from inception is at odds with the purpose of life insurance and may have negative ramifications for the industry, to the detriment of Florida consumers, life insurance companies, and the legitimate viatical settlement industry.

As a result of the hearing and its review of the materials submitted, the Office has identified issues that may merit further investigation administratively, but has no recommendations for legislative action at this time.

\[201\] Transcript at 33.
APPENDIX A

TRANSCRIPT OF SECONDARY LIFE INSURANCE MARKET PUBLIC HEARING ON OCTOBER 25, 2013
STATE OF FLORIDA
OFFICE OF INSURANCE REGULATION

IN RE: SECONDARY LIFE
INSURANCE MARKET

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PUBLIC MEETING

October 25, 2013
10:00 a.m. - 1:35 p.m.

Knott Building, Room 412
The Capitol Complex
404 South Monroe Street
Tallahassee, Florida

Reported by:

LISA A. BABCOCK, Court Reporter
For the Record Reporting, Inc.
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PRESENT

BELINDA MILLER, ESQUIRE
TOMA WILKERSON
JAN DAVIS
WENCESLAO TRONCOSCO
ALYSSA LATHROP, ESQUIRE
BRUCE CULPEPPER, ESQUIRE

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PROCEDINGS

MS. MILLER: Thank you all for coming today. My name is Belinda Miller and I will be refereeing today.

I do appreciate everyone coming, and also for your submissions, for everything that you've given to us. If they're not already on our website, they will be. We will post everything that is submitted so that those who didn't have a chance to review it prior to this hearing will have a chance to go to the website and access the materials. So welcome to the hearing.

Good morning. My name is Belinda Miller. I'm the general counsel for the Office of Insurance Regulation. I will be presiding at the public hearing today. I'd like to take this opportunity to welcome you to this informational hearing on the secondary life insurance market in the state of Florida.

For the record, today's date is October the 25th, 2013. We are conducting this hearing in the Knott Building, Room 412, the Capitol Complex, Tallahassee, Florida. Notice was published in the Florida Administrative Register. The hearing is being broadcast thanks to the Florida Channel and FOR THE RECORD REPORTING TALLAHASSEE, FLORIDA 850.222.5491
will be available for viewers on our website at www.floir.com.

Interested parties, and anyone, may offer materials and comments by sending an e-mail to the Office at secondarylife@floir.com no later than October the 30th. Material received on this matter will be available to the public and posted on the Office's website.

I'd like to take a moment and introduce my colleagues. To my left is Wenceslao Troncosco, who is the deputy commissioner for life and health insurance. To his left, Alyssa Lathrop, who is our lead attorney on this case; Bruce Culpepper, also our senior attorney.

Toma Wilkerson is on my right. She is the director of Life and Health Financial Oversight responsible for the solvency of life and health insurers; and Jan Davis in Market Investigations, who is our resident expert on secondary life and viaticals and life settlements. And that's not in the script so -- I'll find my way.

We would like to allow time for everyone to have the opportunity to address the issues raised in this public hearing. Therefore, we ask that everyone be respectful of the time and allow
everybody else to be heard.

That being said, this hearing starts at 10:00, and we did not put an end time on the agenda, so we will have ample time for those who want to speak to put everything they want to into the record.

The Office is recording this proceeding. Therefore, to help clarify the record, please state your name prior to making comments and speak one at a time.

The agenda is fairly simple. We are going to have representatives of Fortress speak first, and then representatives of the life insurers and the life settlement companies, and anyone else who wishes to speak.

If you haven't already filled out a speaker card and you would like to make comments, please see Eddie in the back of the room. He's got speaker cards and will be glad to help you.

Before we begin, I'd like to go over the issues involved. The Office was given a specific task by the Florida Legislature to review Florida law and regulations to determine whether there are adequate protections for purchasers of life insurance policies in the secondary life insurance
market and to ensure that this market continues to exist for Florida seniors.

Our purpose today is to solicit different viewpoints -- and we know that there are a variety of viewpoints that have some conflict in them so it won't be boring -- and look into legal arrangements and implications of the secondary life insurance market.

The Office will also inquire how consumers benefit or are harmed by these arrangements. We would welcome any thoughts on the role that the Office should play with regard to any new products that might be coming into the marketplace.

I know that some of the participants will have specific legislative recommendations and not sure whether the Office will or not at this point. We'll wait and see what happens. So if anyone wishes to speak, again, see Eddie in the back of the room for a speaker card.

With that, I will recognize our first speaker, Jerry Kroll -- well, I will recognize Fortress and you can introduce yourselves. I think Mr. Welsh will be our first speaker.

MR. WELSH: Thank you, Ms. Miller.

My name is Tom Welsh -- there we go. Is that
good?

Good morning and thank you very much. My
name is Tom Welsh.

(Brief interruption.)

MR. WELSH: Thank you. My name is Tom Welsh
from Orrick, Herrington & Sutcliffe. We're an
international law firm that -- I'll try to make
myself shorter so you can hear me.

MS. MILLER: Yeah, I don't know that that's
going to work.

MR. WELSH: We are an international law firm
specializing in complex finance, complex
litigation and regulatory, specifically insurance
regulatory, matters. And I'm here to speak on
behalf of Fortress Investment Group, which is a
large investor in the secondary market in the life
insurance space.

We -- first, I want to let you know how much
we appreciate the time and energy and resources
that OIR and the Commissioner have put into this
issue. It's really an important issue. It can be
a very emotionally-charged issue, and we really
appreciate the fact that the Commissioner and his
senior staff is taking it very seriously.

Briefly, let me -- let me give you a quick
overview on my comments, which I'll try to keep as
brief as possible. But being a lawyer, you know, I
I can only do so much. We're problematic when it
comes to --

MS. MILLER: Well, if we're going to go past lunch, we will take a break for lunch, so take your time.

MR. WELSH: I promise not to take up the whole morning. What I want to do first is provide a brief overview of the life and -- the life settlements market, primarily just identify who the major stakeholders are, because I think that's important as we look at what your charge is and the primary focus being on the role of the secondary market investors and keeping that market alive, well functioning and available for seniors.

And next, I'll move on and I'll talk about that secondary market investors' perspective on the market. After that, I'll talk about some very serious problems that have emerged in the market that have had a negative impact on actually many different stakeholders within the market, most notably consumers, who are the ultimate concern for OIR and a lot of the players in the marketplace.
Finally, what we've done in our submission on behalf of Fortress is identify potentially five legislative and/or regulatory corrections that can be made to address some of these serious problems that we've seen in the marketplace. And by all means, while I'm talking, feel free to interrupt me with any questions that you have.

As you mentioned, you've referred to yourself as a referee today. I've been involved in the life settlements market advising clients at different levels for a long, long time, for many, many years; and there's no question that probably everyone in this room has really seen the fur fly when we talk about these issues, because it is -- it's an emotional and can be a challenging space to talk about.

And I think OIR's role as a referee of this discussion will really assist everyone in allowing you to focus on the real public policy drivers of how this -- how this market can be and should be regulated in a way that really keeps it safe and sane.

So first, about Fortress, some of you are familiar with Fortress, but let me briefly describe them. Fortress is an asset management
firm that makes and manages investments for public
and private pension funds, unions, university
endowments, nonprofits.

Their investor client base, the people they
manage money for, are people like fire fighters,
police officers, teachers, nurses and other
public employees, as well as corporate pensioners
from all walks of life.

Fundamentally, they are an investment
manager. Their job is to find good investments
that are well-priced, manage them carefully, if
necessary, manage them aggressively so that their
underlying clients receive the returns that they
deserve.

Fortress has about 11,000 employees here in
the state of California (sic) through
its portfolio businesses and the industries that
it's involved in, and it regularly invests
hundreds of millions of dollars on behalf of its
pensioners and universities and foundations right
here in Florida. They're a significant player
here in your community and in your state.

We believe this is actually a relatively
typical profile for the type of investors who are
involved in the secondary market for life
Another good example out where I'm from --
I'm from California -- and the California Public
Employees Retirement System is also a significant
large investor that has seen many of the same
problems that Fortress has seen in its
marketplace. So this -- you know, the type of
people who are looking for this particular asset
class is relatively similar, and Fortress is just
one example of many.

One of the -- as I mentioned and I think
you're all aware, one of the major investments
that Fortress made for its clients in the midst of
the recession was the purchase of nearly 1500
permanent life insurance policies that previously
had been owned by major financial institutions,
national and international banks that had provided
financing of one sort or another, and found
themselves owning these very large portfolios but
being unable to maintain them and service them,
because when you own these things, you have to
continue to pay premium on the policies and keep
them in force.

Obviously, the recession created a very, very
significant dislocation in the credit markets, and
these major financial institutions simply couldn't afford to keep and maintain a portfolio of this size all the way through to maturity.

Fortress saw the opportunity to buy up the policies and did. And from that time, it spent the ensuing years very aggressively and assertively managing the rights that existed under the policies and working -- attempting to work cooperatively with the life insurers that had issued those policies, talking to them about how the policies were performing and establishing the long-term relationships that you would expect and want to see between a large policy owner and the life insurance company underwriters that were involved.

As a result of that, they really, I think, became experts in the management of this particular asset class. They have a very deep staff, and I think they're particularly well situated to assist OIR as it carries out its charge of looking at the secondary market, seeing what problems exist there, what potential protections may be needed there to make sure that the entire market stays alive and is available for Florida seniors.
Let me -- let me give you a real brief overview of the market and really only for the purpose, since I know the staff is very well acquainted with the life settlements market, particularly here in Florida, but I want to sort of identify who the real key stakeholders are, and why they're important, and why each one of them requires notice and consideration.

The first and foremost, obviously, is the consumers, the Florida seniors who have acquired life insurance, and at some point down the road, may decide, for whatever reason, that they need to access the life settlements market and convert those life insurance properties into cash.

And, you know, ultimately, the reasons why a senior might choose to access the life settlements market is about as varied as life itself. Everybody has different reasons for looking to that market.

The key is that, regardless of the reason, it's longstanding law throughout the United States that that's a piece of property that they own and have the right to sell if, for whatever reason, they decide that that's a move that they want or need to make.
So it's an important market from their perspective, and as we work through today, Fortress obviously keeps its eye on its role in the marketplace and ultimately how that drives towards benefiting seniors by keeping the market available.

The next biggest stakeholder and constituency obviously is the life insurance industry, those people who have underwritten the policies and undertaken contractual commitments to, first, the original policy owner, and then subsequently, to investors who may have to step in, or do step in, to the ownership of those -- of those policies. So those contractual obligations that the life industry undertakes are flowing to whomever ends up owning the policy.

The next constituent that we don't speak on behalf of are those originators who are out in the marketplace, the Coventries and others; the agents and brokers who are on the front lines with the consumers explaining the risks and benefits of accessing the life settlement market; and next, and from our -- from Fortress's perspective, importantly, is the set of investors who ultimately provide the liquidity to the market.
Obviously, the originators, for the most part, are not there to buy and to hold to maturity. They frequently are looking to transact and move those policies into a secondary market. That's the way our financial system in the United States works.

And they need that access to good, solvent, well-managed secondary market players who can allow them to continue to outreach to consumers who want to access the market and have the capital necessary to acquire the policies.

Now, during the -- I'll pause for a second and say that, you know, during the course of the hearing and through submissions, I imagine that there will be a certain amount of -- "invective" may be the wrong word, but we have seen in these kinds of public hearings and legislative hearings that there's often an attempt to vilify the investors as vultures and as people who are simply there to make a buck without regard to anything else.

And I will acknowledge that Fortress's job, and the other -- and the job of CalPERS and the others, is actually to take investments, invest in an asset class and try to make a healthy positive
return for the underlying investment clients that they work for. There is -- there is actually no shame in that, and Fortress is very, very good at it.

But I think the focus -- you know, your job today as referee is to try to cut through some of that hyperbole and invective and an attempt to divert your attention away from the key issues. You're going to hear it, no doubt, because we hear it all the time, but the secondary market space is much bigger than just Fortress, and it needs to be, in our view, protected so that the entire market holds together.

There's not a market if you don't have the investors who feel comfortable putting their clients' money into the asset class with some degree of predictability and knowledge of how that asset class and how that space is going to work, from a regulatory standpoint in particular.

So the last big stakeholder is you all. The regulatory community in the United States is vitally important to the functioning of this market. We have here in the U.S., as you know, a 50-state -- well, 50-plus-state insurance regulatory system where the regulators are able to
focus on the business of insurance that happens within their borders, and they coordinate with other states.

But you will see that some life insurers, one in particular that we'll talk about, has really tried to take advantage of and game that a little bit at the expense of all the players, in our view, in the market. That's one of the problems that we'll identify.

But your regulatory role here is incredibly important and plays a big part in what we see as appropriate remedies to help deal with the problems that we're seeing in the marketplace right now. So those are the major stakeholders in the market.

The -- let me -- let me turn to the investors' perspective and essentially ask the question why investors, like CalPERS, Fortress's clients, find this asset class of life settlements attractive, and it really is relatively simple.

In theory, in a well regulated market, this asset class is not correlated to or vulnerable to the wild fluctuations that can happen in the stock market and in other equities indices. The asset class shouldn't have to worry about a eurozone
crisis. It shouldn't have to worry about the
shutdown of the United States Government and the
volatility that happens from those things.

In a well regulated system, the investors are
essentially looking at mortality curves, and the
risk that they're taking is essentially a
mortality risk. They're going to pay fair value
at the outset for policies, and pay the premiums
through the maturity date.

And the return, in a large enough portfolio,
ultimately should be driven by mortality trends.
It should stay predictable and insulated from the
fluctuations that happen in other markets. So
it's that non-correlated market feature that has
largely made this asset class, especially during
the recession, attractive to secondary market
investors.

It's just a way to balance a portfolio and
identify assets that have a particular risk that
you can look at, like what mortality experience is
going to do and develop over time. That's
something that you can get your arms around. You
can predict, you can price, provided that the
market is well regulated and is not subject to
unpredictable behavior on the part of, frankly,
any of the stakeholders who are involved in the
marketplace.

So what do secondary market investors really
want and need to feel comfortable continuing to
fund the market? They really want predictability
and certainty. And not certainty as to investment
return: How much money am I going to make,
guaranteeing that I'll make a profit? That's not
the kind of certainty we're talking about.

We're really just talking about
predictability as to the behaviors of the key
players, and most importantly, the behaviors of
the life insurance companies who have underwritten
the policies. That's probably the single most
important element of it; but also, you know, the
predictability of the originator behaviors and the
consumer behaviors.

Because there's no question that if problems
occur and aren't well regulated at that level, if
we allow any consumer to commit fraud, if we allow
originators to not originate life settlements in a
way that's consistent with consumer interests and
consistent with the law, that creates an
unpredictable environment for investments in the
secondary market. And that's ultimately what
secondary market investors are looking for is a well regulated market that is predictable and isn't exposed to, let's say, irrational or inappropriate behavior.

So that's a good segue into what some of the current problems are in the market. There really, right now, is a real threat to the life settlements market, we believe, that will ultimately reduce, for Florida seniors, their ability to access the market and achieve the values that they should get in a well regulated market.

And the specific problem that we -- that Fortress has seen is an effort by a small handful of insurers to refuse in one way or another to honor those policies after they've collected premiums for years and years, sometimes a decade or more on the policies.

I want to stress at the outset that by no means is this an indictment of the entire life insurance industry. This actually may be a good example of that, you know, 90/10 rule, maybe even 98/2 rule, where, you know, regulators and regulation often don't need to be there for the 90-plus percent of companies and market
participants who are behaving well.

Really, you have to be there to have the
tools to address that minority of companies who
don't behave well, who, for whatever reason, have
decided to try to game the system and avoid paying
their obligations when and as they come due.

And so Fortress doesn't want its comments and
its submissions to be seen as a broadside across
the life insurance industry, because in many
respects, the life insurance industry is the
partner of the secondary market investors. You
don't have this asset class, candidly, if you
don't have solvent, reputable life insurers in the
marketplace.

So let me focus on the problems of the
minority. What the biggest issue the secondary
investors are seeing is that after collecting
premium, and frequently long after the two-year
contestability period in California, a couple of
carriers are making aggressive moves to try to
invalidate the policies that are now held and
owned by secondary market investors.

And they're asking the courts to invalidate
the policies from inception by asserting, again,
long after the running of the contestability
period, that the policy was void from inception because it lacked an insurable interest. In short, they're trying to end around the contestability period and go back and invalidate a policy based on an argument that essentially it was STOLI at its inception.

And the argument that they're making is that, in legal jargon, it's -- the contract is void ab initio -- lawyers can never get through any kind of remark without throwing in a Latin phrase; right -- so void from the very inception.

This is ultimately just a rescission remedy, the kind of rescission remedy that you frequently see in the life insurance industry in the first two years. If a policy matures and an insured dies within the first two years, the life insurance company legally can and should investigate the claim, investigate the application, see if there was fraud.

And if there was, if there was material misrepresentations in the application, they have the right to rescind that policy. It happens on a fairly regular basis, and it's not necessarily an unusual remedy within the contestability period.

What makes this particular problem so serious...
are two facts: One is that these kinds of challenges are being made well outside the two-year contestability period; and two, the insurers have doubled down and said, "Not only do we want to rescind, but we want to be able to keep all of the premium that's been paid to us as damages, because we were damaged by the fraud."

And they actually have now been successful in picking out cases with particularly bad facts. And as -- you know, our other favorite saying as lawyers is bad facts can make for bad law. And we're actually seeing that here in Florida where the really bad facts of a particularly egregious STOLI case where a consumer and an unscrupulous agent of the life insurance company commits fraud, they lie to the company in the application about their net worth and their sources of income that they have to get bigger policies, and those cases have a tendency to cause judges to look for remedies.

They don't want to reward an original insured or anyone else who just happens, through the secondary market to have ended up owning that policy, to reward that bad behavior.

So we've seen clear examples, and we've
provided them in our submissions, of judges
essentially being misled by bad facts and allowing
a situation where an insurance company, long after
the contestable period, which is that window for
them to really complete underwriting and make sure
that they've got a policy that was applied for
appropriately, being able to rescind and create a
windfall for the life insurance company. And I'll
talk about that in a little bit more.

But just to give you a sense of how big this
problem is -- again, it depends on the insurer,
but this process of resisting claims, especially
with one particular insurer -- the members of the
Phoenix Group of companies which are headquartered
in -- their business headquarters are in
Connecticut. The parent company, Phoenix Life, is
domiciled in New York. The largest underwriting
company is PHL Variable. It's domiciled in
Connecticut.

We have statistics that are in our
submission, and these are from Phoenix's own sworn
statutory financial statements filed with OIR and
all the regulators in all the states where they're
licensed to write business, but you saw this trend
start prior to 2008. They were resisting or
denying less than 1 percent of their aggregate death claims.

In 2009, that grew to 12.37 percent. By 2010, it had grown to 16.2 percent. And by 2011, Phoenix was resisting or denying 20.87, almost 21 percent, of its incurred death benefit claims. So the math tells us that over that three-year period, that's a 1900 percent increase in the amount of claim resistances and denials.

Now, Phoenix quibbles with these numbers, and they point out accurately that the number is based on the aggregate death claims, not the claim count that comes in. And that is an important distinction.

But the statement and the data is -- it can't be refuted that during this period of time, there has been a demonstrable, empirically identifiable trend at Phoenix and a few other companies to increase the extent to which they're denying claims.

Now, the national industry average for resisting and denying claims is about one half of 1 percent. So you look at a 21 percent ratio for a particular company that has a big place in this particular market for reasons I'll explain in a
minute having that level of resistance rate is striking. It's something that we believe regulators should note, because it's a serious problem for secondary investors if it continues and is allowed to go unchecked.

So, you know, when we look -- again, since your charge is to look at the interests of the secondary market and how that impacts Florida consumers, there really -- the tie-in is pretty obvious.

The simple fact is investors are simply not going to buy policies in a state where that kind of law exists and they have to worry about the possibility that they can buy a policy long after the contestable period, pay premium for 10, 15, 20 years until maturity, and then find that they have an insurer who has rights under, what we think is, anomalous Florida law that allow the insurance company to not pay anything.

MS. MILLER: Let me interrupt you for just a minute. Would it be that bad -- I mean, I know this is a loaded question -- but would it be that bad if, as a result of this case law, investors said, "Well, you know what, I'm not going to buy a Phoenix policy anymore"?
How does that harm the average consumer or the average person who might be considering selling their policy or maybe not? I mean, is that going to hurt the people in the state of Florida?

MR. WELSH: I think it does for a couple of reasons: One, there's consumers and then there's actually Fortress consumers -- or Phoenix consumers. So if you stop and, you know, if you're looking at it broadly, there are significant negative impacts.

But stop and think about what Phoenix has accomplished. And you're absolutely right. As we pointed out in our -- in our submission, there already is, in the secondary market, a "no Phoenix paper" standard.

When investors identify for the originators the types of policies and the profiles that they're looking at purchasing and investing in -- they want an issue age of X and a death benefit of a million-plus -- whatever those criteria, just general criteria, are, they'll list them for the originators so the originators know that there's going to be a market for them.

And now, many investors are simply putting a
bullet in there that says "no Phoenix paper."
They just -- they don't want it. Now, if you
happen to be, say, a -- an 80-year-old Phoenix
policyholder in Florida, what Phoenix's behavior
has now done is taken the market value of your
policy and destroyed it or dramatically diminished
it.

And now you really have those classic just
two choices: You can either let that policy lapse
if you find yourself unable to afford it at 80, or
you don't need it anymore, you can let it lapse;
or you can see if you can surrender it for some
relatively modest cash surrender value, which, of
course, you know, was originally your money paid
in.

MS. MILLER: Well, was it? Because my
understanding was that these policies were what we
refer to as STOLI policies. So for people
watching at home, that is a stranger-originated
life policy where I, my understanding -- you can
correct me if I'm wrong -- is someone goes to a
consumer and says, you know, "You're not using
your asset, which is the capacity to buy more life
insurance. I've got a good deal for you.

"All you have to do is fill out an
application form, and you don't have to pay money. I'll pay the premium for the first two years. And then at the end of that period of time, you can decide, do you want to keep the policy and repay my loan, or do you want to sell me the policy?"

So if the policy is in the first two years, have the consumers actually paid anything? Or is this a -- an issue among investors and the life insurers?

MR. WELSH: Well, first, we have no information that suggests that the only business that Phoenix was writing was STOLI, and you'll hear a presentation shortly that will demonstrate to you that Phoenix was actually out in the marketplace looking for premium-financed life insurance with high dollar values.

That was a market niche that they had identified and really aggressively went after, knowing at the outset that there was a high likelihood that that policy, over time, would end up in the hands of investors and would be less likely to lapse. So, you know, that's one issue.

But, you know, right now, Phoenix has created a situation where there may be people who went ahead and acquired their insurance in that way,
borrowed some money to pay the premium for the first couple of years, and then maybe because of an adverse health event or an estate planning reason decided to pay off that loan and keep the policy for their beneficiaries.

I don't know exactly. I don't have Phoenix's customer list here in Florida. Phoenix would be the one who would have to tell you if they have any policies that are still in the hands of the original insurers. I have to believe that that's the case but --

MS. MILLER: Would they know?

MR. WELSH: I would think that they should.

MS. MILLER: I don't want to jump ahead, but, you know, in preparation for this hearing, one of the things we did was we sent a questionnaire to the life insurance companies.

We already get an annual report from all of the life settlement companies about how many policies have been, for lack of a better word, viated; and the life insurers reported to us their estimate of how much they think their book is subject to a contract of viatation, and the numbers are dramatically different.

I mean, the viatical settlement companies
have identified a tremendous number of viaticated policies that I think the life insurers may be unaware of. They may not know that's been viaticated.

They may not -- it could be that they just don't track it. It could be the ownership hasn't actually changed yet. You know, I'm not sure. They should have gotten notice. You know, if it's in that two-year period, they may not have notice yet.

MR. WELSH: That is -- that is true. And actually, you know, if we take a step back, really, what the secondary market investors are looking for is a regulated market that is agnostic as to who owns the policy.

And the reason we were talking about this was identifying, you know, what's the adverse consequence if Phoenix continues on this path and other insurers start to replicate that because now you're generating case law that lets other insurers know that they could potentially avoid the two-year contestable period if they missed something by claiming that there was a lack of insurable interest at the outset?

So there is this contagion risk that exists
when bad facts make bad law, and suddenly it's not just Phoenix. It could be other companies that feel as though they've been wronged, perhaps correctly, but they missed the contestability period, their window under your law to figure that out.

And they will start to take advantage of that. That's the overarching concern and problem that will exist in the marketplace. And it's not just a problem for life and set -- life settlements investors. It's a problem for original insureds.

Somebody who, you know, smokes 12 cigars a year or 10 cigars a year or whatever insurance companies will typically allow -- I don't smoke that many but you can -- you can do that and still be a non-smoker and apply for a non-smoker-rated policy.

And if suddenly you unfortunately pass away for totally unrelated reasons, three years later and the insurance company comes back and says, "Hey, we want to invalidate that policy," there's now jurisprudence, there's case law that will support invalidating that policy even afterwards.

Now, my example wasn't a good one because I
haven't settled the policy. But if a policy gets settled and you have that kind of a circumstance, that case law is going to be there for any life insurance company to take advantage of it.

And that's the contagion risk that Fortress sees coming out of bad behavior by that 2 percent of companies that are looking for ways, right or wrong, to avoid their policy obligation. Does that answer your question?

MS. MILLER: Yes. Thank you. I know your colleague has more to say about all of that.

MR. WELSH: And again, you know, we -- investors, I think, would like to see a market that doesn't make distinctions between life settlement companies or investors as owners of the policies and the original purchasers.

So let me -- let me turn, having identified some of those problems, what are -- what are some of the potential fixes? In Fortress's submission, we identified five potential legislative fixes that could help clarify the marketplace.

The first one I'll go over briefly is a possible reform that would try to clarify and create certainty and end a lot of this needless litigation by establishing that the subjective
intent of the original insured who may, you know, by the time of the challenge, have died, isn't relevant to determining whether there was an insurable interest at the inception of the policy on day one.

Insurable interest, just for the record and for the audience, just refers to the interest, either personal or financial, that the beneficiary has in the life of the person who is being insured.

I think as everyone is aware, the insurable interest requirement is there to avoid that moral hazard of having a stranger take out a life insurance company (sic) on you and then, you know, running you over with a car, which actually is a real example from Los Angeles.

And, you know, that insurable interest requirement is essential. It has to be preserved. The issue is that under Florida law and under most state laws, the insurable interest requirement applies to the initiation of the policy. At the time the policy is issued, there has to be an insurable interest.

After that point, consistent with the notion that a policy is a piece of property that can be
sold if the owner wants to, it has to be freely
transferable, even to someone who doesn't have an
insurable interest in the life that's being
insured. I mean, that's the fundamental principle
in the life settlements market.

And what we're seeing, unfortunately, is that
some of the companies have begun to challenge the
policies claiming that they're void for lack of an
insurable interest by focusing on what the
consumer, the applicant's, original intent was
when they took out the policy.

And that is absolutely chilling the market,
and, you know, they're keeping a lot of lawyers
busy. But the real problem is if you use that
kind of an intent standard to determine -- let
me -- let me back up for a second.

The argument they make is that if, at the
time of application, they intended to sell the
policy, that, by definition, there was no
insurable interest. The policy can be voided,
right.

There's a lot of devil in the details of
establishing or applying an intent standard. You
know, we ask the rhetorical question in our
submission, is it enough that they thought maybe
there is a 50/50 chance that they might settle the policy and sell the policy in the future, is that enough to establish that they had an intent to settle, and therefore, the policy was void?

What if they just entertained the prospect of doing it? What if they were simply aware of the fact that policies are property, and down the road, I can sell them if I want to? Is that enough to demonstrate an intent to settle the policy such that years, maybe decades later, the insurance company can go back and void that policy and try to hold onto the premiums as a form of damage?

And ultimately, you know, should it matter whether a policy is actually sold? Even if you have someone who has the intent to settle the policy, takes it out but then, you know, in all likelihood, I'm going to -- I'm going to settle this policy and get rid of it, but then they don't.

I mean, that's a real case from here in Florida involving Mr. Cotton and -- where the case wasn't settled -- or the policy wasn't settled, and the insurance company nonetheless was able to find intent that he wanted to settle the policy.
when he applied for it, and they argued that there
was no insurable interest and the policy was void
and they didn't want to pay the death benefit.

What's -- the judge in that case, I think,
did a very good job of identifying what really the
underlying problem is with an intent standard.
The quote from the case is, the judge said, "In
this case, discovering the intent of Mr. Cotton at
the time he procured the policy is complicated by
the fact that he is dead."

You know, our view is that an appropriate fix
would be a legislative change that establishes
that intent of the policyholder is not relevant to
an analysis of whether there is an insurable
interest that exists at the time of the policy
inception.

Without that, you get into this contagion
risk that insurance companies, as this kind of
jurisprudence continues to arise, will start to
think that the contestable period is discretionary
and optional. And that's not good for seniors,
whether they settle or not.

The second potential legislative option
is clarifying that these types of insurable
interest challenges can't be made after the
contestable period. You know, it has been long settled that life insurance companies are afforded this window of time, two years, to complete the underwriting and identify red flags and follow up on those red flags to see if they've issued a policy that was issued based on misrepresentations.

And we think, you know, candidly, it makes a lot more sense to conduct that inquiry about insurable interests while the original insured, the applicant, is still among the living and can tell the insurer and a court what he or she was thinking at the time they bought the policy.

So if you are going to -- if the law is going to evolve in a way that allows intent to remain relevant that, at a minimum, those kinds of challenges need to be put back where they belong under the contestable period so that the market understands that, after that window, the investors have the certainty they need to dump money into the market and provide higher values for those seniors who actually want to sell a policy.

I can -- in our submission, I'll point out that we've provided some case law to illustrate some of these. Actually, a Florida federal judge
agrees with the investor community that the better rule is that those kind of challenges need to happen within the contestable period, but there has been case law to the contrary that opens up this uncertainty that is so problematic.

The third option is notices of validity, is just ensuring that when an investor decides they want to buy a policy, allow them to be able to contact and obligate the insurance company to respond with an affirmative indication that the policy is valid, it was validly issued. And as long as the premium remains -- is paid, the policy will remain in force and the death benefit will be paid.

The fourth option is a legislative change that establishes that these kinds of challenges will remain subject to the traditional rule of rescission, which is that you have to give back the premium.

So if you're an insurance company, and within the contestable period, your insured dies and you realize there's been fraud in the application and you rescind, the law of rescission says that the parties have to be put back into their original position. The policy is ripped up. You don't get
the death benefit, but we're going to give you
back all of the premium that you paid into the
policy.

The litigation that I mentioned has had a
number of insurers asserting claims that they
should be able to rescind but not put the policy
owner back into the position of getting all their
premium back. They want to retain that as a form
of damages.

Their theories vary but, you know, the
biggest driver of this is that life insurance is a
very high commission business, and the life
insurance company gets the premium and they turn
around and pay very, very large commissions to
their life insurance agents. That's their
business model. That's the way they've chosen to
do business.

And the insurance companies don't want to
spend the time and effort to go after bad agents
who put a bad policy into their book, one, because
it's easier for them to just ask the judge to let
them keep the premium and they can -- they can
recover that damage, if it is damage, rather than
having to go --

MR. TRONCOSCO: Can I interrupt you for a
second? You bring up a good point. So this goes back to Option A. And I mean, really, what you're getting to is, you know, fraud, because you kind of opened the door a little bit to fraud when you -- you know, what about the public policy implications when you're talking about, you know, closing off the door to the intent of the consumer when they purchased the policy?

You know, when you're talking about doing that, you obviously could open the door to fraudulent situations. And have you thought through what impact it could have on the marketplace?

And then also, you know, have you thought -- is this legislative fix that you're seeing, are you thinking to direct this specifically towards the life insurance industry, or are you thinking in a more general sense? Because, you know, insurable interest obviously has rather large impact across several markets.

MR. WELSH: It does. First, our thought was focusing just on the life insurance, because this is -- this is, by definition, a life settlements context that we're talking about. But -- and most of the moral hazard actually exists with respect
to life insurance.

It does -- lack of insurable interest does raise moral hazards in property and casualty as well. If you buy a homeowner's policy on your neighbor and then burn their house down and collect the premiums -- the damages, that's the same type of moral hazard.

But really, the focus of moving away from intent is to say to the life insurance industry, "You have to underwrite. You have to police your own agents. These are your agents. You file an appointment saying that this person is authorized to act on your behalf to work with consumers, to solicit applications for life insurance. Police those people."

And if they do their underwriting, if they do their selection of agents and training of agents properly and invest in that the way they should, the way you as regulators would want them to, that's where fraud abatement -- that's where the fraud prevention is most easily addressed at that front end agent selection and underwriting process, and not allow insurance companies to essentially just turn a blind eye to that fraud, because they know that if they can prove it ten
years down the road, they can claim that there was no insurable interest, get out from underneath the policy and keep all the premiums.

MR. TRONCOSCO: So you bring up a good point. So the other thing that's going through my head when I heard your options is, what effort on your part do you do to underwrite the policies that you're investing in?

Because obviously, you know, if you're concerned about that situation happening, so what effort do you take on your own underwriting to prevent that for yourself and your own investors?

MR. WELSH: As much as they can, given the access to information that they -- that investors in the secondary market have.

So the investors in the secondary market can do things like, you know, find the address of the underlying insured on the policy and figure out if they actually live in a trailer park, or, you know, do they live in a country club gated property that actually suggests that they should have a 2 to $3-million-dollar policy on their life? If they live in a trailer park, it's a problem.

So there are certain types of information
that investors can have access to and do look at as they do their own diligence. But frankly, it's a more limited data set. They can't always go directly to the consumer and sit down and interview them about what their original intent was. That wouldn't be a functional finance-driven market.

But they do, by all means, as much diligence as they can and try to avoid situations where they buy a portfolio that has some fraudulently-procured STOLI policies in it. Sometimes that's unavoidable when you buy large portfolios and you're a secondary investor, but, you know, you can do as much as you can.

But that's the wrong time, in our view, to be looking at fraud abatement. The right time to be looking at fraud abatement is long before an investor ever comes on the scene. This gets back to the need for predictability and certainty that investors want. They want a marketplace that's free of STOLI and free of fraud.

Because the last thing they -- they didn't buy portfolios to become involved in the business of litigation with life insurance companies. That was never anyone's expectation. Sometimes it
happens and you have to just face up to the fact that you're going to have to litigate with some insurance carriers who clearly don't want to honor their contracts.

But the right place to police fraud is the life insurance underwriting, agent select period. That's what Fortress believes is the best marketplace where the secondary market's investors can provide the liquidity to the market, not having to worry that bad behavior has happened, at that end.

And, you know, frankly, some companies are really, really good at taking care of their policies, doing the underwriting at the front end, selecting really good agents. Just by way of example, you never see a -- or you rarely see a Northwestern Mutual life insurance policy in the secondary market, because they take care of their customers. It's a mutual company.

And that's an example of the -- maybe the majority of life insurance companies that are doing the right thing, that are doing really good underwriting at the front end. And the more of that that happens, the more stable the life settlements market can be, the higher value
consumers can get because the secondary market
investors are willing to invest at higher levels
in that market, because they don't have to price
for the kinds of risks that you're identifying
that emanate ultimately from fraud or the
appearance of fraud.

So the intent standard is really designed to
drive fraud abatement back to where it belongs,
which is at the insurance company level.

MR. TRONCOSCO: Thank you for clarifying
that.

MR. WELSH: So we talked about premium
return, not essentially giving the insurance
industry a potential windfall and easy recovery.
What -- what's particularly problematic about
allowing them to recover or retain premium based
on a claim that they're damaged because they had
to pay a bunch of commissions to their own agent
and that agent may have been fired or may be long
gone, they don't want to go through the effort,
the secondary investor who now -- secondary market
investor who owned that policy, payed the premium
for years and years and now has been denied
recovery of the death benefit based on this kind
of litigation challenge has no privity of
contract, no direct right to go back after the
agent and recover some of the premium that lines
the pocket of that agent.

The only one who is in a position really to
do that is the company that has a selling
agreement with them, who appointed them as their
agent. And that's where, you know, if the
agent -- I'm sorry, if the company has, in fact,
been defrauded, their remedy is not to undercut
the law of rescission, which says that both
parties are put back in their original position --
rip up the contract, give you back your premium --
but rather, you know, let them execute on remedies
that they have against the people who were
actually complicit in the fraud. And frankly,
sometimes that's people within the insurance
company as we'll hear a little bit later.

The final option -- there's one other tactic
that Phoenix has deployed in this marketplace that
has destabilized the life settlements market,
particularly for Phoenix policies; and that is,
after the recession, they lost a lot of money in
their investment portfolio.

One way they have tried to recover from that
is look at policies that they believe were
investor-owned because of the way they're behaving. And generally, when an investor buys a permanent product, they don't put a bunch of extra premium into the product to accumulate value. They put in enough premium to keep the policy in force through maturity and they retain the rest.

And so what Phoenix was doing was identifying those policies within their book that appeared to be owned by investors, and those policies were targeted for a discriminatory cost of insurance rate increase.

The appearance was that the desire was to try to gut the economics of the policy and force the investors who owned those policies to make the hard decision of allowing the policy to lapse because the rates were going up and could go up to such an extent that they would end up paying more premium through maturity than they would get back in death benefits. And that's a losing investment and that's something that all secondary market investors are trying to avoid.

MS. MILLER: So are you suggesting that the Florida Legislature should require life insurance companies to have their rates regulated, to go through the Office? And I've just got to watch
the reaction.

MR. WELSH: I actually -- I actually think that an appropriate fix might be not necessarily rate regulation at the front end. The open rating market actually works. It's a very competitive marketplace.

And most of the companies are very good at setting fair rates for consumers, and there's enough competition that the environment -- that environment seems to work. But when you get into in-force business and cost of insurance adjustments, that's actually a very rare thing in the life insurance industry.

There's a lot of reputational risk that happens when an insurance company kind of mid-term decides, uh-oh, "We have to confess to all of our policyholders that we goofed up on the pricing and now we have to increase your rates, excuse me, beyond what we originally illustrated to you at the inception of the policy."

That's not something that happens lightly within the insurance industry. So you could actually impose a prior approval rate regulation regime over those kind of post-issuance cost of insurance adjustments. And 90, 95, maybe even 98
percent of the life insurance companies wouldn't mind, because they'd only be working -- well, I'll let them --

MS. MILLER: That will be hilarious. We'll wait for them to respond to that. But -- so you're suggesting the legislature -- that the rate regulation doesn't need to occur at the outset; that there's enough competition in the market; that if you're writing new life insurance policy, you don't need to have that prereg -- preapproved.

But if you've had a policy in force for ten years and a life insurance company is going to increase your rate, at that point, that would have to be preapproved?

MR. WELSH: I think that is a good suggestion. I'm glad you made it.

MS. MILLER: Okay. Well, these are -- these are definitely not our suggestions, but I just want to make sure that we're clear on what the recommendation is. So that's the five recommendations to the legislature that --

MR. WELSH: Correct.

MS. MILLER: Are these alternatives, or do you want all of these things at the same time?

MR. WELSH: Any one and -- or a combination
of them would, I think, achieve the objective of helping create the kind of certainty that investors want to see in the life settlements market so that they will continue to invest and pour money into the marketplace ultimately for the benefit of those seniors who decide they need or want to tap into that market.

And let me -- I will go back and -- with respect to prior approval of COI increases post issuance, if you actually do have a company that is needing to do that, all prior approval requires is that they come and talk to you about it and explain what is happening within the back office of their company that is driving them to need to make these kind of mid-term rate adjustments.

And from a regulatory standpoint, that's probably the time you want to be spending more time with those companies. If they've got a big book of business out there that they've priced incorrectly, this gives you as regulators an opportunity to get a little bit closer to that and really have an opportunity to understand that.

So those are -- those are Fortress's comments. We are happy to continue the process of helping analyze these issues, and we'll answer any
questions or do whatever you need us to do to help you complete the report.

MS. MILLER: Thank you very much.

MR. WELSH: And at the risk of appearing to try to control or dictate the order of things --

MS. MILLER: No. Mr. Kroll is next. That's fine.

MR. WELSH: Okay. I didn't want to be presumptuous. But Jerry Kroll, an attorney, has a presentation that he would like to show that provides a little more color on some of the issues that I've touched on briefly.

MS. MILLER: Thank you.

MR. WELSH: Is there -- is there someone who can help boot that up for those of us who are technology challenged?

MS. MILLER: We don't have a remote control so we're going to come around.

(A pause in the proceeding.)

MR. KROLL: Good morning. My name is Jerry Kroll. I'm an attorney from a small fishing village in California.

MS. MILLER: Small fishing village?

MR. KROLL: Yes. It's called Santa Barbara.

And I handled a case on the opposite side from PHL
Variable Insurance Company and Phoenix Life Insurance Company on behalf of two life settlement funds, one of which was called XLI, and the other, Olive Tree.

And they purchased a number of beneficial interests in trusts that owned 32 policies, and collectively, I'll call them Phoenix policies, totaling approximately $300 million in face. Each policy was held by life insurance trust, and at some point, each of these funds purchased that beneficial interest.

Since the policies were freely transferable after approximately one-and-a-half years, XLI wrote to Phoenix asking to change ownership of the policies from the trust to the fund, and thereby, be able to dispense with the trust and the expense of that.

About four months later, Phoenix responded by letter. What did they say? "We'd like some documents from you," and there were requests for over 20 categories of documents, everything from lists of your financial advisors to documents substantiating net worth, annual income, life expectancy evaluations and so on.

And the threat, if the information wasn't
provided in 14 days, Phoenix would consider all of its legal options, including potential rescission. This is when I was involved. I was hired and we sued Phoenix.

It seemed like a rather simple case at first: Request to transfer ownership, failure to change the ownership. Well, what transpired was something that was beyond what I knew at the outset, but it was a great education. I have come here today to share some of this education with you, because I think it may be helpful to some of the issues that you're addressing here today.

Phoenix cross complained, and in essence, it became a battle about some of the things that have already been mentioned here this morning. Phoenix wanted to void the policies and keep the money, and that's the battle.

In this case, we took approximately 200 depositions all across the United States. For a time, I felt like I was living in New York, Pennsylvania, got to know the great state of Florida very well. Many of the insureds lived in South Florida, and that's why obviously this is very important, what we're doing here today.

And as you'll see in a moment, the
deposition -- I brought some clips here for you to see. These are excerpts from Phoenix personnel who testified in this case. For me, this was a great education. The case, we'll talk about it in a moment, but this is -- this reminds me -- so many times, it was like Forest Gump. You never know what you're going to get.

So if I may, I would like to share with you these deposition experts.

MS. MILLER: Okay.

(Whereupon, a video was played.)

MR. KROLL: That is the education that I got during the course of the case and --

MS. MILLER: Can you get closer to the mic?

MR. KROLL: Sorry? Oh, I'm so sorry. I was trying to say that that is the education I received during the course of the case, the Fenton vs. Phoenix case, and that has now gone on to become evidence that has been used in a variety of cases around the United States that are pending as we speak.

And I will tell you that just generally, what's out there -- you probably know -- that there was so many policies put on the books during these years, that was coming. Maybe one day,
there is going to be a tsunami of death claims
that are going to have to be dealt with, and these
issues will be dealt with.

But I thank you for letting me share this
with you, because it was an education for me and I
hope for you as well.

MS. MILLER: Thank you.

MR. KROLL: Thank you.

MS. MILLER: At this time, I think what we
need to do is take a ten-minute break, and if that
concludes Fortress's presentation -- does it?

MR. WELSH: Yes, it does.

MS. MILLER: Okay. Then when we come back, I
believe the ACLI has one or more witnesses, and we
will -- we will hear from them.

So thank you. We'll be back in ten minutes.

(Whereupon, a recess was had in the
proceeding.)

MS. MILLER: Okay. We're ready to go back on
the record.

At this point, I will allow you to make your
introductions and tell us who you are and who you
represent.

MR. MCDOWELL: Thank you, Ms. Miller.

My name is David McDowell. I'm a lawyer from
Edison, McDowell & Hetherington in Houston, Texas, and I'm pleased to be here today on behalf of the American Council of Life Insurers. As I'm sure you know, the American Council of Life Insurers is an organization dedicated to protect the interests of life insurance companies and their policyholders.

What we're really talking about here today is the tale of two markets. On the one hand, you have the legitimate life settlement marketplace, a marketplace that has existed for a very long time that is designed to allow Florida citizens and other policyholders around the country to sell their policies if they no longer need or want the insurance coverage they had.

When they bought the insurance coverage, they were buying it to address legitimate insurance need. Their needs changed over time, and they now wish to sell it onto the secondary market. As evidenced by the information that's been provided by others to this panel, that market is doing just fine.

There has been information provided to the Office indicating that that market is still viable. It's still available. It still allows
insureds to sell unwanted or unneeded policies
into the marketplace as long as that insurance was
originally purchased to address legitimate
insurance needs.

I highly doubt that this office has been
flooded with calls from Florida seniors saying
they can't sell their policies on the secondary
market. What we're talking about today isn't
really addressing that market.

What we're talking about today is addressing
a very different market, a market of
stranger-originated life insurance. The Office
knows what stranger-originated life insurance is.
Stranger-originated life insurance is not life
insurance at all.

Life insurance is purchased to address the
financial consequences of the insured's death.
Those buying stranger-originated life insurance
suffer no financial consequences when the insureds
die. Instead, they want the insureds to die as
fast as possible. The quicker the insured dies,
the greater the profit margin that they're able to
lock in over time.

Obviously, this creates a very dramatic
difference than what typically goes on in the
traditional life insurance marketplace. A life insurance company is not going to issue a life insurance policy if it believes that the person purchasing that policy is doing so for reasons other than legitimate life insurance purposes.

For that reason, people had to disguise these policies, disguise these applications when they originally sought to buy them so that they would look like legitimate life insurance transactions. That's how they induced the life insurance companies to issue these policies.

This whole notion that the life insurance companies wanted to turn a blind eye to the obvious risks that were presented on paper are belied by the fact that so often in these transactions, the individual seeking to buy the policies had to lie in order to get them.

If the life insurance companies didn't care, why lie? Why do you have to -- why do you have to tell a lie on an application? Why do you have to lie about a person's financial means, about their net worth, about the reason they're purchasing the insurance if the life insurance industry didn't care about them?

When regulators and life insurance companies
became aware of the STOLI threat in 2006 and 2007, they both immediately reacted. State legislatures around the country passed anti-STOLI legislation. They firmed up their insurable interest laws to rededicate the notion behind the public policy behind insurable interest.

Life insurance companies went into court to seek rescission of these policies that were procured by fraud, and they were largely successful. Because of the combination of these legal and regulatory forces, the value of these toxic assets on the secondary market was absolutely crushed.

They were unable to sell on the legitimate life insurance -- on the legitimate secondary market, because the legitimate secondary market didn't want to have anything to do with these assets. And so the hedge funds, they smelled a bargain.

And as Mr. Welsh indicated, I'm not here to vilify Fortress for smelling a bargain, but I am here to set the record straight that the reason why Fortress and other companies got involved and bought these blocks of policies was because they were able to do so for pennies on the premium
dollars already paid.

And in doing so, in seeking investors, in seeking funds to buy these -- buy these toxic assets, they issued notices to the investing public. And in these notices to the investing public, they told the investing public that they were looking to buy assets that might lack an insurable interest, that might have been procured by fraud, that were subject to litigation and regulatory risk and that might be outright illegal.

And they told the investing public that if any of those factors came to pass, if any of those things were actually true, it would have a significant and profound effect on the value and the liquidity of the policies in the portfolio they were looking to purchase.

So with these dire warnings and with the characteristics of these policies, is it any wonder that they've had difficulty selling those policies in the legitimate secondary life insurance marketplace?

I would offer to the Office that the legitimate secondary life insurance marketplace's hesitancy, unwillingness to purchase these
policies is actually a very healthy vital sign of a thriving marketplace and not an indication of a weakness that needs to be addressed through legislation.

What life insurance companies did when they learned about the stranger-originated life insurance threat is the only thing they could do, which was to resort to court. And when they resorted to court, they seek to affirm the three certainties that have long existed with respect to life insurance:

Number one, it is a legal certainty that if you lie on a life insurance application, the life insurance company can rescind that policy within two years of policy issuance; number two, it is a legal certainty that if the life insurance policy is issued without an adequate insurable interest, that the policy is void ab initio. It is terminated. It is an illegal contract because it violates the public policy of insurable interest; and number three, it is a legal certainty that if a life insurance company knew or should have known of problems on the application or problems associated with insurable interest, that the life insurance company has to bear the consequence of
that knowledge.

And nothing that has happened in the courts over the last five or six years has changed those legal certainties. Those are the legal certainties that have governed the insurance marketplace for decades. Those are the legal certainties that exist today, and those legal certainty certainties don't need additional legislation to firm them up at all.

When life insurance companies went into courts, they found judges who were willing to listen, who were willing to balance the equities. These are complicated cases. And whether or not a particular policy can be rescinded, whether or not premiums should be given back in a certain situation, whether or not an insurable interest exists will come down to the facts of each individual case.

So for example, if a life insurance company issues a policy to a person claiming to be worth $40 million and they are really a taxi cab driver or a blackjack dealer or an indigent person, well, what did the life insurance company do during underwriting?

If the life insurance company requested tax
returns and received falsified tax returns, is the
life insurance company at fault? If the life
insurance company asks to speak to a CPA and was
presented with an impostor, a fake CPA, is the
life insurance company at fault?

If the life insurance company asked for
appraisals of significant assets making up a
person's net worth and false fake appraisals were
provided, is that the life insurance companies
fault?

When these matters are brought before the
courts, the courts have an opportunity to look at
the individualized facts and make a decision
whether, under that particular circumstance, the
life insurance policy in that situation should be
rescinded, and if it is rescinded, who should get
the premiums on the -- on the policies?

And I would submit to the Office that it
would be very, very difficult, despite the
collective talent of the legislature and this
Office, to craft legislation that would adequately
address the potential equitable issues that could
crop up in any individual case, and that's why no
state has tried to do so.

This is not a new effort by the Fortresses of
the world, by the hedge founds that now own the policies that get legislation passed. We've been in South Dakota. We've been in Minnesota. We've been in Delaware.

No state has decided to go down that road, and I think in part, it's because it would be very difficult to legislate fairness, to provide legislation that would adequately address each individual situation.

The life insurance industry has been very successful in courts. Mr. Welsh said it was because they've been able to mislead judges based on bad facts. I have a greater faith in the judiciary than I guess Mr. Welsh does.

I don't think judges have been misled. I don't think the First Circuit Court of Appeals of the United States, the Sixth Circuit, the Eighth Circuit, federal district courts and state courts across the country, I don't think they've been misled by the facts when they've addressed the situations. I think they've been guided by the equitable principles and the three legal certainties that I spoke about at the outset in arriving at their decision.

We just heard a lot about Phoenix Life
Insurance Company, and I would suggest to the
Office that it look at Phoenix's filings. And
I should say that I appreciate Mr. Kroll beeping
out all of my curse words during the course of
those depositions.

I represented Phoenix in that lawsuit. I was
in most of those depositions, and I can tell you
that those depositions -- he's right. We took 200
depositions and you saw about ten minutes of clips
in those depositions. And if those depositions
presented an accurate reflection of what Phoenix
was actually doing at the time, Phoenix would not
have been successful as it has been in court.

Phoenix tried a case in front of a Los
Angeles, California, jury earlier this year
against a hedge fund and won. Phoenix tried a
case in Minnesota, in a Minnesota federal court
earlier this year and won. The First Circuit and
Eighth Circuit Court of Appeals have ruled in
favor of Phoenix on these type of issues.

Federal courts around the country have done
the same thing. And they've done so because
Phoenix, like a lot of other companies that were
duped into issuing these policies, have credible
issues they have brought before the court, and
courts were able to look at the equitable consideration and reach a reasoned decision.

I do want to note, and I do again ask the Office to look at Phoenix's regulatory findings.
Mr. Welsh indicated that Phoenix is denying about 20 percent of the claims submitted to it, and it's been on an upward spike since then.

When you look at the blue book that's filed by Phoenix with the Office, you're going to see that for the last four calendar years, Phoenix has paid 66,527 claims out of 66,535 claims submitted. They've contested eight claims in the last four calendar years.

That's a payment rate of 99.98 percent, hardly an indication of a company gone wild, of a rogue company that is simply flouting the regulations that Florida and other states have put in place to govern their conduct and their activity.

As it relates to litigation, the one last thing I want to mention is this idea of premium refunds. Mr. Welsh and Mr. Kroll, I believe, indicated the premium refund has been a bedrock principle of rescission, that you always get your premium back when you refund a policy, and that
simply isn't the case.

Rescission is an equitable remedy. And when a court -- when a court provides equitable remedies, it is allowed to weigh the equities, and it is allowed to determine in what situation it's going to allow return of premiums.

Some courts have said that the public policy behind insurance fraud is so strong that we are not going to force a life insurance company to give back to the entity that defrauded it the premiums that were paid, because then you're making life insurance fraud a very low-risk, high-reward proposition.

Other courts have said yes, in a situation of rescission, we're going to require the life insurance company to give the premiums back, but the life insurance company can seek to offset against those premiums the damages that it suffered separate and apart from the mere issuance of the policy, which only seems fair.

And finally, courts, including a court right here in Florida, has said, you know what, if a life insurance company knew or should have known that there was an insurable interest concern, they did have some obligation to initiate legal action,
and they couldn't sit back and simply collect the
premiums and then claim later, well, we don't have
to pay any back.

What that Florida court said is when there is
evidence that the company knew or should have
known, that those premiums that were received
after that point in time are in play, and that a
life insurance company has to be accountable for
its conduct.

So when it comes to litigation, litigation --
the courts across the country have simply applied
the three certainties of law that have existed for
decades to reach equitable resolutions in the
context of individual life insurance policies.

This notion that there is a lack of certainty
simply isn't true. What is true is that the
outcome of a particular policy, of a particular
case, is going to depend on the facts, facts that
shouldn't be neutralized simply by the passage of
black-or-white legislation.

Mr. Welsh offers to the Office five possible
legislative alternatives to address whatever the
problem was that he suggests exists. The first
one is that the subjective intent of the insured
should not matter when it comes to determining
whether or not an insurable interest exists.

I would submit to the panel that the subjective intent rarely does matter to a determination of whether insurable interest exists. The highest court in the land to speak of the issue, the Delaware Supreme Court, said it doesn't matter.

What the Delaware Supreme Court said and what other courts have followed suit in doing is looking at the factual circumstances of the policy issuance and deciding, based on that set of facts, whether there was an insurable interest.

What the courts are trying to do is to make sure that we're not elevating form over substance and allowing STOLI promoters and hedge funds to simply paper around the important public policy of insurable interest.

The second thing that he suggested is that there cannot be any insurable interest challenge after the contestability period. Most states in the country have rejected that principle. Most states in the country have said that the public policy behind insurable interest is too important to simply subject it to a two-year bar. If you subject it to the contestability
period, what you're essentially doing is saying that an illegal contract is not illegal because of a provision contained in the illegal contract. And let me tell you -- let me -- let me talk to you about an unintended consequence of that kind of legislation.

I had a case many years ago right here in Florida involved an insured down in the Miami area who woke up one day and found out that somebody, unbeknownst to her, had taken out nine different life insurance policies totaling about $3 million of death benefit on her life.

Those applications had obviously been forged. But if insurable interest was subject to the contestability period and she found out two years after the policy issuance, there would be nothing she could do about it. There would be nothing that she or anybody else could do to address that situation. That doesn't seem to be sound legislation.

Mr. Welsh suggested that there be verification of coverage legislation, that if a life insurance company is asked by a policyholder whether or not a policy has an insurable interest, a life insurance company should be forced to take
a position, yes or no.

What that legislation is essentially trying
to do and why no state in the country has passed
that kind of legislation is to privatize the
public policy of insurable interest, to take out
of the hands of the courts and of judges whether
or not insurable interest exists in that kind --
in life insurance policies.

If the onus is on the life insurance company,
subject to penalty and potential judicial
sanction, to make a statement as to whether or not
a policy has or doesn't have insurable interest,
what incentive does the life insurance company
really have to go ahead and fight the fight?

The life insurance company doesn't have
access to subpoena powers. It doesn't have access
to information from third parties. It doesn't
even really have access to the insured anymore to
gather the information.

It has to make the insurable interest
determination based on the information that it
already had in its possession when it underwrote
the policy. There would be no reason to do that
and it would privatize the issue of insurable
interest.
And at this point, I do want to make one comment on something Mr. Welsh said, and it was in response to, Mr. Troncosco, your question on what burden is on the hedge funds when they buy these policies to assess whether or not these are toxic assets or whether they were legitimately-issued policies.

And he said, "Well, we have limited access to information." I think if the Office does research into this area, it will find, generally speaking, that hedge funds that buy large blocks of policies have unfettered access to the insureds; that often, the insureds have an ongoing contractual obligation to provide information to these hedge funds; that these hedge funds are very, very particular about how they value their assets, and they frequently are in touch with the insureds to assess their health.

So this notion that we're going to blindly buy a block of policies for hundreds of millions of dollars without actually knowing the risk that we're taking on I don't believe withstands common sense and general knowledge of the life settlement marketplace.

The fourth item that he suggested is return
of premium legislation; basically what we've already talked about, that if a policy is rescinded or declared void, that a life insurance company has to return the premium.

For all of the equitable reasons we've already talked about, that legislation doesn't make sense. That legislation would take out of the hands of the court the right to do equity, the right to rescind policies and then decide whether or not, under the circumstances, the insurance company gets to keep some of the premium, has to give all of the premium back, gets to keep all the premium.

There is no reason to have legislation that deals with that direct issue. And again, let me tell you one unintended consequence, or perhaps an intended consequence, of that kind of litigation -- legislation.

If you have legislation that says if a policy is declared void ab initio for lack of insurable interest, these hedge funds that own blocks, hundreds and hundreds of policies, they know what the mortality horizon is on their particular insureds. They know which policies are going to require premium payments far into the future, far
longer than they want to pay.

They're going to gather those policies. They're going to sell them to an entity, if Florida is the one that passes the legislation, domiciled here in Florida, and then they're going to declare the lack of insurable interest themselves.

They're going to declare that the policies lack an insurable interest and demand that the insurance company return all of the premiums paid for those policies, even the premiums that were paid long before the hedge fund ever took ownership of the policy.

And finally, Fortress suggested a change to how Florida deals with COI, cost of insurance, increases. Cost of insurance increases are heavily regulated by any state. The language that is included in life insurance policies with respect to COI increases are usually specifically approved by state departments of insurance.

Life insurance companies are required and obligated to follow that language. And in the very rare circumstance where they don't, there is remedy either to complain to departments of insurance or to court. The notion that, again, we
have to address legislation to deal with these
issues is simply unfounded.

Finally, about an hour of the presentation by
Fortress and by others, by Mr. Kroll, focused on
Phoenix. I would submit to the Office that if
this is really a one-company issue, there's no
reason for legislation. There may be reason for
review, regulation, et cetera, but there's no
reason for legislation to deal with the supposed
sins of simply one company.

At the end of the day, life insurance
litigation has been around for a long time, and
the certainty that has been derived over time is
no more tenuous today than it was five to ten
years ago before STOLI litigation came to pass.

If what the Office is interested in
protecting is the legitimate life settlement
marketplace, I think a review of the materials
provided to the Office will show that that
marketplace is just fine.

If the Office wants to open up that
marketplace to these toxic assets, that's a --
that's an entirely different situation and one
that, based on everything we just talked about,
simply is not justified by the passage of
legislation.

I'm happy to take any questions the Office might have.

MS. MILLER: Thank you. I have a question and my colleagues may have some, too. First of all, some of us have purchased life insurance before. I've never tried to buy a 2 or 3 or 4 or $5 million-dollar policy.

But if I did, I would expect the life insurance company to ask me a few questions, and I might not get past the first one. But the notion that people can buy a policy for those types of amounts and the life insurance company then does not even know if the policy is sold or not, it just blows my mind.

Can you discuss that and tell me why an insurance company would not be aware -- because under Florida law, as you said, the traditional life settlement market notifies, they are required to notify, the company that the policy has been purchased.

So how does this get so far down the road without the insurance company having a very good idea of why the policy was purchased, and who owns it, and how it was transferred?
MR. MCDOWELL: Sure. And thank you for the question. During the application process, the application will specifically ask questions about a person's net income, about their net worth, about the reasons why they're purchasing the policy, about other policies that might be in force.

Most companies have gone to some form of what's called a statement of client intent where they seek to find out from this particular insured, why are you buying this? Is it for legitimate life insurance purposes, estate planning, et cetera; or is it really with an eye towards selling it?

Are you paying for it yourself? Are you premium financing? Is somebody else giving you a cash inducement or a promise of payment down the road if take out these policies? The insurance company is trying to get out in front of this issue, because they don't want these policies.

The reason we have all this litigation is because the industry doesn't want these policies so they ask those questions. Once the policy is issued, these policies, again, as I said at the outset, are disguised to look like normal life
insurance transactions so --

MS. MILLER: Let me stop you for just a minute. Okay. When I buy a life insurance policy, they're going to get a check from me, and it has my name on the check and my address. Is that what they get, or are they getting a check from somebody else?

MR. MCDOWELL: So when a policy is purchased by an elderly person for estate tax planning purposes, it is almost always purchased by an irrevocable life insurance trust. The irrevocable life insurance trust is, legally speaking, a separate third party. It has a separate trustee, and that trust has a beneficiary.

The way they disguise the transaction is they allow the trust to purchase the policy, and then the trustee, which on paper, looks like somebody that has an insurable interest of the insured, say it's a spouse or a husband -- a spouse or a son or a daughter, that person will then sell their beneficial interest in the trust, often hours after policy issuance, to the third party financier, to the STOLI promoter.

So there's been an effective change of ownership, but the person -- the entity in charge,
the entity that owns the policy and from whom the company is going to receive the checks, hasn't changed. The company never knows about the transfer of the beneficial interest.

MR. TRONCOSCO: I think you brought up a good point. And just for -- we're using a whole lot of acronyms today, and for people that are watching us and trying to understand through the acronyms, and also, the legalese and insurance-ese and everything like that, and a comment that was made during the break to point out -- and you briefly touched on it, I think -- it would be helpful for everyone to understand this issue a little bit more the difference between the traditional secondary market and the secondary secondary market, that is -- that is what Fortress was talking about. If you could explain upon that a little bit further so people could understand, I think it would be beneficial.

MR. MCDOWELL: The history lesson, as all of you know, is that the secondary market essentially rose out of the AIDS epidemic. Individuals that had AIDS back in the '80s essentially had death sentence.

They had these life insurance policies that
were guaranteed to pay off because, at the time, they were going to die, but they had no use for those policies. What they really had the use for was the expensive medicine that was needed to treat their symptoms.

And so the secondary market arose out of that crisis, and these individuals were able to sell their policies on the secondary market for much needed cash, and it expanded from there. People with terminable diseases were able to sell it later on.

And then traditional -- simply insureds, people that had life insurance, they may have bought a large policy when they were 45 or 50 years old. It's 15, 20 years later, their kids are all successful. They don't have to pay for college any more. They have no need for the life insurance policy.

They essentially had under -- without the secondary market, the option of either letting it lapse or simply taking the cash surrender value that was in the policy.

What the secondary market did was give them a third option. It allowed them to shop their current mortality, which could have been worse
than the mortality that existed at the time the policy was issued, they could shop their current mortality and the value of that policy to secondary investors who would purchase the policies as part of a transaction.

The fundamental distinction between that, the legitimate life insurance and life settlement transaction, and STOLI is that everybody was still on the same page at the time the policy was issued. Everybody wanted the insured to live as long as possible.

The insured wanted to live as long as possible. The life insurance company certainly wanted the insured to live as long as possible. And if the concept of insurable interest means anything, the beneficiary wanted the insured to live as long as possible.

That's not the case with STOLI. STOLI, there is no financial consequence to the person procuring the policy. They want to the insured to die as soon as possible, and that really creates a moral hazard and a risk that we as a society have largely said we don't want to deal with.

MS. MILLER: Well, now, if a policy is viated, if it's sold to investors the first
time, in other words, not in the hedge fund
scenario, but say I have a policy that I've had
for ten years and I go to a life settlement
company and I say, "I'd really just like to spend
the money and go to Europe," you know, and so they
pay me a percentage of the face value of my policy
and they take ownership of my policy.

Not to imply that they would ever do anything
wrong with that, but they do have a financial
interest in my early demise. They're better off
if they don't have to pay premiums for a long
period of time after that transaction, so that
interest exists the first time the policy is sold.

The second time it's sold, when that life
settlement company bundles their policies and
sells to an institutional investor, that's still
in place. There's still an investor out there
with an interest in my early demise, which I would
find a rather uncomfortable situation. But in
either event, you have that, and people still do
it because, as you said, that's the only way they
get the liquidity out of their policy in the first
place.

The life insurance companies offer
accelerated benefits if I'm dying, if the
situation is I have AIDS and I need the money for medicine. But why doesn't the life insurance company, to get ahead of this, offer people the opportunity to buy back their policy directly instead of allowing middle men to get involved who really do have -- they have, by nature, they have an interest in the insured dying sooner rather than later?

MR. MCDOWELL: Sure. The life insurance industry is selling death benefit coverage. They're selling peace of mind that the financial consequences of the insured dead are going to be covered should it come to pass. It's insurance. They're not selling a car. They're not selling a house or a building. So the way the product is designed, especially permanent products, whole life and universal products, is that those products can have a cash value.

Depending on the premiums paid over time by the insured, the election made by the insured to pay premium, that cash value could grow to be quite sizable. And at that point in time, a person who doesn't want to sell it to the secondary market can simply take the cash value of the policy.
There's nothing wrong with doing that, and they're not necessarily selling themselves short by simply taking what the policy offers, the cash value of the policy.

If they don't have the concerns that you just raised about having a disinterested third party own the policy -- that's sort of the tension with life insurance is that on the one hand, it's an insurance product. The issue of insurable interest is important.

On the other hand, it is generally considered an asset that can be, after issuance, sold freely on the market. If a person wants to, they have the option of then selling it on the market, but they do have the option.

They're not -- it's not a situation where the only way they could possibly get value out of this policy is to take the cash value or to let it lapse and lose all of the premiums paid. If they want the cash value, they can take it. If they want to shop it on the secondary market, they can do so.

MS. MILLER: Can you, for people that are watching this, give an example or just, I mean, not a -- not a technically-calculated average,
just a ballpark, how much -- if I had a
$100,000-dollar policy and I took the cash value,
how much would that likely be? And how much would
it be if I viated, and how much would it be
the secondary investor would pay? Just, you know,
the --

MR. MCDOWELL: Yeah. I wish I could.
The problem with doing that is you have to know
certain assumptions. You have to know how much
premium has been paid in the past. Have you paid
along the premium schedule? Have you sometimes
paid a little more? Have you sometimes paid a
little less on the policy? Have you taken any
loans against the policy? What's your health?

When you go shop your policy on the secondary
market, in the legitimate secondary market --
marketplace, they can assess your mortality risk
at the time you're selling it. So the unhealthier
you are -- the more unhealthy you are, the greater
value your policy is.

So just to say a hypothetical example,
somebody has a policy, $100,000, what could they
get versus the cash value? It would be impossible
to, at least with my limited knowledge, to give
you an answer to that question.
MS. MILLER: Well, but comparatively, you know, if I have a -- if I'm 65 or 70 years old and I've had the policy for a number of years, I might get, what, 20 percent or something in cash value, maybe not even that?

MR. MCDOWELL: Yeah. Again, I wish I could answer your question. I'm afraid if I did so, it would be pure speculation.

MS. MILLER: I'll ask the life settlement folks because they would know those numbers.

MR. MCDOWELL: There you go.

MS. MILLER: Okay. Does anybody else on the panel have questions? Jan?

Okay. I have a couple of questions. Do life insurance companies police their agents adequately, or is there some criticism, legitimate criticism, of that that might have led to some of these issues?

MR. MCDOWELL: I think the life insurance companies do police their agents and their producers adequately. There are bad apples in every group, and those bad apples can lead to bad consequences.

I think that if a, quote, life insurance agent is actually conspiring with a third party to
defraud a life insurance company and induce it to issue a life insurance policy it wouldn't do so had it known the truth, that person is no longer an agent, legally, agent principal, agent of the life insurance company. It's working with a — with a third party.

The life insurance industry polices its agents. It wants to make sure that it doesn't have any bad apples out there, and I think that it does do so adequately.

MS. MILLER: The implication of some of those videos was that the company encouraged that behavior, that they were looking for the premium and it was increasing their premiums dramatically, and it was increasing their agents' incomes, agent commissions dramatically to write as many STOLI policies as possible. What's the incentive of a company to do that?

MR. MCDOWELL: To do -- I'm sorry, to do what?

MS. MILLER: To try to encourage their agents to sell STOLI policies. Or is there any?

MR. MCDOWELL: Well, I think that you would talk to companies that have been involved in litigation, and they would tell you that they
haven't been making money hand over fist by paying the lawyers.

To purchase policies or to allow the issuance of policies that shouldn't be issued to only then seek their rescission doesn't make good economic sense. Where Phoenix, for example -- using Phoenix as the example because that's what was in the videos -- Phoenix, for example, most of the litigation that Phoenix has filed has not been with respect to death claims.

Again, given the numbers I gave you, they have only contested eight death claims over the last four full calendar years. Their contest has been on policies that are still in force where the insured is still alive.

So if the notion was, well, the insurance companies are just going to sit back and collect all the premium on all these bad policies until the insured dies, that really hasn't been borne out by market conduct, not only by Phoenix but by other life insurance companies.

Life insurance companies don't want the stuff because it's fraught with fraud. Because it's fraught with fraud, they don't understand or necessarily appreciate, on a particular policy
basis, the risk they're actually undertaking.

I'll give you an example. We had a case a
while ago in which a person claimed on an
application to be worth $23 million. This was an
elderly woman about 72 years old. During a review
of the policy as part of litigation, we found
a subsequent medical record, and the medical
record indicated that the insured came into an
emergency room with a cut on her head that she
received walking along the railroad tracks home
from work at midnight.

Now, is it possible that somebody worth
$23 million at the age of 72 is required to work
at a job that has her walking along the railroad
tracks at midnight home? I guess it's possible.
Is it likely? No.

So life insurance companies, they don't have
any interest in issuing these policies because
they really don't understand the risk that they're
being asked to assume. And, again, I think the
best evidence of that idea, that notion, is that
life insurance companies have generally been
filing what we call live rescissions, rescissions
while the insured is alive. They haven't been
sitting back and just collecting premium.
MS. MILLER: I can't imagine that they couldn't have found that out the day the policy was issued.

MR. MCDOWELL: Well, so as, again, you look at --

MS. MILLER: Or before.

MR. MCDOWELL: Sure. So as I indicated, you look at the underwriting process. And look, I'm not going to stand here and tell you that the insurance company is 100 percent perfect in every situation. You know, even Sinatra cleared his throat every now and then.

But what life insurance companies do typically as it relates to a policy is they'll ask for information. And if they continually ask for information time and again, and they get fraudulent information in return, at some point, it's no longer the fault of the life insurance company.

They're being conned by crooks and we have to place the responsibility on the crooks and on the con men and not on the life insurance company if the life insurance company asks the right questions.

And that's why I said one of the legal
certainties that has long governed life insurance litigation is if the company knew or should have known about the issue, they have to bear the consequence of that.

What the STOLI promoters have been unable to do time and again in this litigation is to show that the life insurance company knew or should have known. Because, again, when the life insurance company would ask the questions, they would get fraudulent information in return.

MS. MILLER: Should the legislature consider a law that says that life insurance is not freely tradeable, that after -- maybe you've had the policy for five or ten years -- you can sell it one time but you can't trade it on the secondary market?

MR. MCDOWELL: I don't think so. I think that, again, the legitimate secondary life insurance marketplace provides a third option to insureds who originally procured their policy to address legitimate insurance needs.

And that marketplace, I think, is important to regulators, because it does give a third option to citizens. So I don't think legislation is needed that was recommended by Mr. Welsh. I
frankly don't think that that legislation would be necessary either.

MS. MILLER: Thank you.

Anything else?

Thank you very much.

MR. MCDOWELL: Thank you. Thank you for your time.

MS. MILLER: Mr. Freedman, you want to -- you can go next. It's very dark in that part of the room. I thought -- I thought you were sitting there but --

UNIDENTIFIED SPEAKER: It's very light for you.

MS. MILLER: Yeah, I know it is.

UNIDENTIFIED SPEAKER: Does it make a difference if we sit and testify or do we --

MS. MILLER: Take your choice. We can do it either way.

MR. BAYSTON: My name is Darwin Bayston and I am the president and CEO of the Life Insurance Settlement Association, and I would like to thank you for the opportunity to be here today to provide some comments and some recommendations for this hearing.

We are submitting -- we have submitted formal
comments, so I'll let those stand, and I'm just
going to make brief comments relative to a couple
of the issues in there.

For the past 20 years, the life settlement
market has evolved from largely an unregulated
marketplace where viatical policies were sold to
today's well regulated market in 42 states and
covers about 90 percent of the population that
would qualify for a life settlement transaction.

This market has provided billions of dollars
to tens of thousands of policyholders who
otherwise would not have been able to access the
financial value and resources of their life
insurance policy.

Today's market is one that's including a lot
more lower-to-middle income policyholders who are
in bad need of financial resources for retirement,
even to the extent that several states are
considering the use of life insurance policies for
long-term care, and even in cases of people
qualifying for Medicaid.

So basically, the life settlement market
exists to allow seniors, as was stated earlier, to
sell the policy that is personal property in the
marketplace if they no longer need it, want it or
perhaps can afford it.

Even so, the market evolves. There have been challenges to the ability of seniors to make that life settlement transaction, and I'm going to talk about those -- some of those in a second. But as a preface, I think it's already been distinguished by some of the speakers earlier the difference between the secondary market, which is the larger, broader market; the life settlement market, which is the transaction, the sale of the policy; and STOLI, stranger-originated life insurance.

And I think the definitions of STOLI have been made clear. It is -- it becomes a STOLI policy at the time of issue. I am talking about life settlements, which are not STOLI. STOLI is not a life settlement. Life settlement is the sale and transfer of that policy.

So -- but I would like to focus some comments on some conduct matters that relate to the difficulty in the sale or transfer of life insurance policies by these seniors that may impact transaction happening or may impact the value that the seniors get when they sell those policies.

And the first, of course, is the nonpayment
of interest. I think there's an awareness among
the market participants that when interest is not
paid and it's generally corrected, and in most all
cases, once it's brought to the attention of the
companies that the interest is not paid, it is
then paid.

But I think that there is a broader
issue here on the broader audience of individual
seniors who may not be aware of whether or not
interest is paid or whether or not they have
rights to interest. And so that's why it becomes
an important issue for you all to address to make
sure that all seniors are getting all of the
benefits they're supposed to get from the sale of
that policy including any unpaid interests.

There have been interest -- instances in the
past that we have discussed about unauthorized
changes in ownership data by the insureds, whether
it's addresses, whether it's telephone numbers or
other information, that really is important to the
ownership of that policy.

These may be inadvertent, and certainly,
don't believe that they're done deliberately. It
may result from simply from, you know,
administrative matters, or Lord knows we know the
last few days of difficulties in computer programs
and what they cause. So these may not be done on
purpose at all, but they could, they could, cause
a loss of coverage if the policies lapse as a
result of nonpayment of the death benefit.

There is a third issue in the obstruction in
obtaining verification of coverage.
Those instances seem to be more prevalent, and
clearly, the difficulty in providing verification
of coverage simply is an action that's taken that
significantly slows down the process of whether or
not that policy can be transferred.

And in some cases, it becomes so complicated
and so -- takes so long, that the transaction
simply doesn't get completed or, you know, people
throw their hands up and say, "Look, we're going
to go away from this."

So to that extent, any policies that are
prevented or delayed from being sold, it also
affects the value of the people who paid for those
policies. Therefore, that is an area where
seniors could be harmed through that action, and
we feel and recommend that that is addressed.

Another one that seem -- that has a broader
significance, I believe, is when insurers either
threaten or gaggle producers from advising or being involved in life settlement transactions. In other words, they tell their -- they tell their agents they can't be involved in it. They can't talk about it. They can't discuss it.

And when that happens, there's two things that happen: Seniors are -- seniors consider their agents a very important part of someone who gives them financial advice and counsel. We get a lot of calls from seniors that want help, need help. Where should we go? Who should we talk to?

And the agents -- the agents, of course, and producers are very, very much an important part of the financial advice that these people get, that they should get, and is impacted by. And when carriers don't allow them to participate in the life settlement market, they are really creating a negative environment and a negative attitude by a lot of the seniors of there must be something wrong with this transaction, because my producer is not able to talk about it. Those are serious things, I think, that need to be addressed.

I'm going to let Michael give some comments, but I would like to make one general comment from the testimony and the conversations that have gone
on before. I spent 35 years in the investment
management profession, and I spent a lot of those
years with the (inaudible) institute as a charter
financial analyst.

And it bothers me when conversations go on
about an investor buying insurance policies and
then hoping that the person dies as quickly as
possible so I can make as much money as I can.
Now, look, most of these are bought by
institutional investors.

An institutional investor buys various types
of assets and puts them together in a portfolio to
accomplish some sort of a goal. And when you look
at, as an investor, buying 100 policies or 200 or
300 or however many, you're looking at that total
group of policies, and you're anticipating and
expecting a cash flow.

And you're trying to -- you try to evaluate
the return you're going to get based upon the cash
flows that you're going to get over time. And to
say that I'm sitting there every day as a
portfolio manager thinking, well, I sure hope this
person with a $2 million-dollar policy dies
because I can make more money is ridiculous.

The other side of that that we don't ever
hear is life companies who sell annuities. And if I give them $500,000 in a lump sum and they're going to pay me X amount of money each year until I die, I don't believe they sit there and say, "Well, I hope Darwin dies in a hurry so that we can keep the money, therefore, we make more."

I don't hear the state pension fund saying, "Gee, we have all these unfunded liabilities, and you know one way that would take care of this is if people die early. We wouldn't have to make the minimum retirement payment." We don't hear that.

So I think we need to look at this in the context of -- we could even go up to the next level and talk about social security, you know, if you want. But we need to say these policies are bought by professional investors who are combining those with other assets and they're trying to get certain cash flows.

And it's really the predictability of that cash flow that determines what they get as a return or not. It's not individual ones. You know, I don't buy 100 stocks and then look at one stock and say, this is going to make me or break me. That's ridiculous.

And I would like to see us not talk about it
in that manner. Talk about it in a larger context
of these are investments that they make in hopes
of earning an expected return, and that return is
determined by the cash flows and when they come.

MS. MILLER: Okay. So to be fair, the life
insurers are not sending me vitamins and
memberships to a gym and asking me to really take
care of myself, because they want me to live a
long time either. So I understand your point.

Do you think that -- do you think that it's
important for the State of Florida to maintain the
ability to buy a life insurance policy the second
time? In other words, I understand the consumer
need. If I have a policy, I've had it for ten
years, and I come to you and I say, "I need to get
the money out for whatever," and for me to sell it
to a life settlement company and be able to
liquidate that policy, that's important for me.

But is it important for the State of Florida
to then allow those companies to bundle their
portfolios and sell them again to hedge funds or
to whomever? Can you comment on that.

MR. BAYSTON: Any market needs liquidity, and
I think to not have that happen would deny
liquidity or the ability for these policies to be
sold somewhere else.

You're basically telling the investor that
buys it the first time, "You're buying it. It's
got to be locked up and you're not going to be
able to sell this." And when you -- when you don't
have any liquidity like that in the marketplace,
you basically have investors who are not
interested in locking their money up that long.

I don't know of an institutional investor who
is willing to say that I buy something today and
it's locked up for 10 years or 15 years and with
no ability to be able to get it. So a
secondary market -- I mean, a tertiary market is
very important to this marketplace, just that it's
done correctly is the important part.

MS. MILLER: Right. Is that the source of a
lot of the funding that is used today for life
settlements? In other words, I think when
viatical first came out, there was a lot more
solicitation by viatical settlement companies of
individual investors.

For example, you know, put $10,000 in and buy
a fraction of a life insurance policy. You don't
see that as much today. It's -- I don't think.
Maybe you can correct me if that's wrong. I think
more of the money is coming from institutional investors. Is that correct?

MR. BAYSTON: That is correct. And that -- and that certainly is what we hope continues to happen. And there is a greater recognition by a broader group of institutional investors to put money into this -- into this space.

For example, we introduced at our conference -- at our conference last week a Harvard Business School case study that's been written on the industry, which is -- which is, for certain, going to bring more recognition and consideration by a high level of good institutional investors who are looking to put money into this as a legitimate asset class to go along with all the other assets that they have, types of investments they have, for the diversification and for the noncorrelation benefits and other benefits this particular asset has.

MS. MILLER: Okay. Thank you.

MR. FREEDMAN: My name is Michael Freedman, not Frank Sinatra clearing my throat. I am senior vice president of Government Affairs for Coventry, and I'm here representing LISA today as a member
of LISA and as a member of the External Affairs Committee.

I want to reiterate just one thing that Darwin was saying at the outset in his preface, that there is a very clear and important distinction between the broader secondary market and between this thing called stranger-originated life insurance.

And I think the only thing I could add is if you look at the litigation that is being brought by insurance companies, hundreds of cases, they are not being brought against life settlement companies. The issues that are being litigated do not have to do with the assignment of a policy through a life settlement transaction, a regulated life settlement transaction.

There are some cases that involve policies that were settled, of course, but that's the -- that's one of the issues at hand, which is if the carriers are duped in the issuance of the policy. There's been instances where life settlement companies have not been aware, and in some instances, deceived as to the true nature of the origination of the policy.

The perpetrators of those schemes don't want
anyone to know what their true origins are. So yeah, there have been some. But, again, the litigation -- none of the litigation, none of the litigation is aimed at life settlements and the life settlement market and life settlement participants.

And I think that's important, and very much what Darwin was talking about, the issues about the life settlement market and how that market is important for seniors in Florida, and how there are areas of concern that could be addressed through stronger enforcement and stronger legislation.

I'm just going to pick up on there and make a few other additional brief comments that are covered in our submission, and one deals with a, more or less, regulatory issue that, going back several years, the legislature adopted a requirement that life expectancy providers be registered under Florida law.

And that registration is different than a licensing. It was simply basically telling the state you're going to be in this business. The qualifications were very few, if any really, and there was no judgment, no standard by which the
department could say you are or not eligible to be
a life expectancy provider.

Earlier this year, the Office of Insurance
Regulation proposed legislation that would delete
the requirement of registration of life expectancy
providers. That legislation, which was included
in House Bill 635, was one that life insurance
settlement associations supported.

The life expectancy provider registration
requirements, at this point in time under that --
that law was passed only just about a decade
ago -- were ineffective. There was no
demonstrable consumer or investor protection.

They were anomalous in that no other state
provided such a registration requirement for life
expectancy providers, noting that Texas has a
requirement that LE providers register as brokers.
But, again, no distinction such as this.

And as the OIR has pointed out, it gives the
appearance of an endorsement or an imprimatur that
the life expectancy provider has some sort of
blessing from the state. But even today, it
impairs the market because the market has shifted,
as you've just recognized, Ms. Miller, and as we
know, that there's more institutional investors in
the market.

Investors are buying, using their own underwriting, underwriting that is, because they are themselves either an insurance company or reinsurance company which represents some of the investors in the market, or that differs, if you will, from those registered LE providers. And so -- and as part of that, providers buy for themselves as investors and would use their own underwriting.

But the way the law is written today, with that in the law, we're not allowed. Those investors are not allowed to utilize their own underwriters or underwriters of their choice, because they're restricted to using only registered life expectancy providers.

So we would support, again, an effort to repeal that provision in its entirety that would include any remnant of the life expectancy provider registration or any restriction on who an investor can utilize for a life expectancy provider.

I want to make one comment, though, now also, switching gears a little bit, again, focusing still on life settlements. The issue of return of
premiums does have an impact on our market even though it's not, as I pointed out, subject in the litigation and subject of a lot of this debate, because investors are buying these life insurance policies and we're going to really focus on just, again, the life settlement policies.

When a life settlement occurs, the life settlement provider is required to go back to the insurance company and ask for the verification of coverage. It asks the insurance -- it effectively notifies the insurance company there's about to be a potential sale of that policy.

And the questions are some very basic information about the policy, but it signals to the carrier. In states, many states, it requires them to look back for fraud, misrepresentation in the issuance of the policy.

So the insurance company is given another notification. Hey, there is an opportunity here for you to say this policy was issued properly or improperly at its origination. If there are any other questions about the validity of the policy or things, that's an opportunity for the insurance company.

Under Florida law and every law in the
country that I'm aware of -- I think I'm aware of them all -- there's also a requirement that the life settlement company, the provider, as part of its antifraud plan, due its diligence to look for elements of fraudulent settlement acts that include the original underwriting of the policy, where the premiums are coming from, insurable interest, as well as any potential fraud or misrepresentation in the sale of the policy.

So we're doing our due diligence at that point in time. So the life insurance companies had the opportunity to do due diligence at the inception of the policy. They have an opportunity at the time the verification of coverage is submitted. We have that obligation, too. But yet still, sometimes policies will get through and sold that should have never probably been issued, that would have been void ab initio.

So we believe that among the things that the legislature should look at is strengthen the law that doesn't impair the ability for an insurance company to rescind a policy for lack of insurable interest, or -- but that does provide the opportunity or make clear that if the policy has gone through a regulated life settlement
transaction, that if they find they're going to
rescind that policy for lack of insurable interest
and if that's granted, that the premiums be
returned to the investor of the life settlement
contract.

Because, again, we've gone through elements
of diligence that haven't -- that may not have
happened in other transactions, in other secondary
market transactions. But in a life settlement
transaction, there is that level of scrutiny.

But, again, still mistakes can happen.
Things can still get through, but we are clearly
not part of any transaction that's originating the
policy improperly, and those premiums should be
returned to the investors of life settlements.

And so we have provided you with it in our
testimony. We've provided you with some suggested
language that clarifies the return of premium
that -- just what I just said, that it be
clarified. Because, again, that gives confidence
to the investor, as well as to the life settlement
market so that the seniors can access the market.

MS. MILLER: What about the argument that we
heard earlier that you don't need new legislation
to accomplish that; that courts can already weigh
the equities of the situation? And in your example, you have a legitimate licensed life settlement company that has not engaged in any fraud, has bought the policy. Why wouldn't you already win that case?

MR. FREEDMAN: Again, we're talking about this market, which is not the subject of that --

MS. MILLER: Right.

MR. FREEDMAN: -- that mess. What we are talking about is there needs to be clarity and there should be some level of certainty in this market that provides tremendous value to consumers.

And the idea, again -- I guess we -- there is fallout from all this that is going to affect the life settlement market. Investors become potentially more wary about, well, you know, even if there is a life settlement transaction, even if you've done all this diligence -- as you know, it's a very regulated transaction -- we can still lose all of our investment in the premiums that we've paid since we purchased it.

There should be some certainty. And, again, as I pointed out with the level of scrutiny that's involved with the carrier having to go back for
verification of coverage, the opportunity to look back on that policy, as well as the life settlement company, everyone has done their best efforts, and yet still, there may be cases.

And if a carrier then says, "Well, now we've discovered it," remember they had an opportunity at inception. They had an opportunity throughout. They had an opportunity prior to the sale. I think at that point, there needs to be some certainty and some comfort, clarity for this market, for life settlements, the certainty that the premiums that the investor, from the time they bought the policy from a regulated life settlement transaction, be comforted that they -- they be restored to their original position, because they were not part of it and they did their best efforts as well through the provider.

MS. MILLER: Okay. I think I'm a little lost. It may be just me. The law is already very settled that after two years, the life company can't contest the policy based on fraud, that they can't -- the two-year contestability policy has been in the law for years.

The only issue, I think, that's new, and it may have come out of these cases, is the idea that
yeah, but you can still look at the insurable interest at the time the policy was taken out. I don't even see how they would affect you.

Because the life settlement is typically a contract that is already in force before you see it. I mean, you're not having people go out and apply for insurance and then generate a new contract, are you?

So is that really something that's hindering investment in the products that you're involved in, or is it just this STOLI issue that Phoenix and Fortress are arguing about?

MR. FREEDMAN: I'm sorry if I haven't been clear.

MS. MILLER: It's me.

MR. FREEDMAN: And I said it at one point in what I have spoken here, but we've also made it clear in our submission. We are focused only on insurable interest issues, the issue of insurable interest which carries beyond the contestable period in most states.

In Florida, there is at least some question now because of a recent court ruling as to whether that's applicable. But we're talking about that issue of insurable interest only, which can carry
beyond the two-year contestable period. And so yes, it does have an impact on our market.

And more court-made law is establishing not only is there the ability -- you know, good faith standard or somewhat of a subjective intent standard. If courts, as they are in Florida, allowing carriers to retain premiums for policies that are void for lack of insurable interest, we're saying with respect to life settled policies where there is this extra scrutiny, this extra diligence that has to go on, they should be protected so the investors in the secondary market -- excuse me, in the life settlement market -- I want to make that distinction -- are certain that they're not -- their investments are not at risk because there's been a failure through all of that level of diligence to do that, to ensure the policies didn't have a lack of insurable interest.

MS. MILLER: Anybody else on the panel have any questions?

MS. DAVIS: I'm just not sure I understand. If you've done your due diligence, there shouldn't be a problem with the policy.

MR. FREEDMAN: That's correct.

MS. DAVIS: So why do you need legislation?
MR. FREEDMAN: But does it happen that policies are issued for lack of insurable interest and get through the carrier? Yes. Can they get through the life settlement market? Yes.

MS. DAVIS: And the courts can take care of the issue.

MR. FREEDMAN: Well, again, we're asking and suggesting that the legislature be clear because of the level of scrutiny that's involved in the life settlement transactions that, again -- remember, the carrier gets another bite at the apple, if you will, through the verification of coverage to say, "Hey, this policy is subject to potential life settlement." The carrier gets to ask -- gets the opportunity to say, "Well, we should make sure this policy is valid, whether it should have been issued as well."

We base -- we, as a life settlement company, under our antifraud plans, have to go back and look, where did we get our information from on whether or not the policy was issued accurately -- properly? From the insurance company. So, again, there may be instances where cases are going to get through.

MS. DAVIS: And so for those rare instances,
you want us to do legislation?

MR. FREEDMAN: Well, this is rare, but, you know, again, we're representing our market. And, you know, again, the courts are making the -- making court-made law today saying that carriers can retain premium. We ought to be more clear.

They can retain premium where there was a policy that was void ab initio if that's going to be law. However, they can't do that with respect to policies that have been through a regulated life settlement transaction. I think, you know, they have to return the premium to the owner, the investor owner of the life settlement.

MS. MILLER: What do you think the insurance company should do when they get a request of verification of coverage to make sure that that policy was issued properly?

MR. FREEDMAN: It's what they should do at the inception of a policy, is do their best efforts and do their diligence to make sure the policy is issued properly. What are they going to do if it's not a settled transaction?

MS. MILLER: I guess that's my question. Maybe it's more appropriate to ask the life insurers, and I'll ask them when they get back up.
But the -- I mean, having bought life insurance before, they come and they, you know, they test your blood. They meet you. They see where you live. They see -- or at least they see where you work if they're coming into the office.

Some life insurers actually do due diligence and underwrite the policies. So if a year or two later, they get a request for verification of coverage, should they go back and do the underwriting again?

Would you do that if you've got some indication that -- I mean, it's too late after you buy the policy. It's too -- it's not too late for them until the two years, though, is what you're saying.

MR. FREEDMAN: Again, our point is there's an extra level -- there's several extra levels of scrutiny that are going to take place when the policy is being sold. The carrier is notified it's going to be sold, and they have to do verification of coverage. They have to look to see whether there are issues related to the policy.

It may not specifically involve insurable interest inquiry but it can. And certainly, if
it's past the two-year contestable period on fraud
and misrepresentation, it may not be worth doing
but they -- but they have to -- they're being made
aware the policy is subject to settlement. And is
it valid? Is it a -- is it a valid policy.

The life settlement market has to also do it.
The life settlement company also has to do the
same thing through our antifraud plans. We look
back, take a look, see where premiums come from.
We have to look back at the origination of the
policy. We have to look back for specifically
insurable interest violations. We do our best
efforts.

These are regulated transactions. Again, I
made the point earlier, much of the STOLI
litigation involves policies that are not going
through a regulated transactions. Should there be
a benefit of having a regulated transaction, one
in which we've done our best efforts by law? And
the answer is yes.

There should be some comfort that if the
carrier then later finds out there was a scheme to
deceive the true insurable interest, the ownership
of that policy from inception -- we tried our
best. They tried their best. Now they found out
about it. That -- those premiums should not be
retained by an insurance company at that point for
the life settlement policy.

MS. MILLER: Okay. Thank you.

MS. DAVIS: You're saying most of the STOLI
policies have not gone through a regulated
viatical transaction. Are you saying that that's
because they're premium-financed policies that are
then sold off? Or what are -- what are you saying
that those policies are?

MR. FREEDMAN: Well, I think Mr. McDowell
pointed out as well that these -- it's the
beneficial interest in the -- in the trust that's
being sold, that the -- in the case of
premium-financed schemes, there was a
relinquishment or abandonment of the policy.

You know, they didn't even involve a life
settlement transaction, I can tell you that,
whatever those were. That's why there's a
difference between life settlements and
stranger-originated life insurance.

MS. MILLER: So we have 17 licensed -- 17 or
18 -- 17 --

MS. DAVIS: 17 in Florida.

MS. MILLER: -- licensed life settlement
providers, companies. And those entities are not the entities that were involved in STOLI transactions. Is that correct?

MR. FREEDMAN: That would be my assertion. And I think, you know, I would ask you the same question.

MS. MILLER: And so I think what we've been presented with from time to time is the question of, "If I do this transaction and I'm making a loan, at the time I make the loan, I'm telling people that in two years, you have a choice. You can keep the policy and repay my loan, or you can sell me the policy."

The people who are proposing to do that come to us and say, "Do we have to be licensed as a -- as a viatical settlement company or a life settlement company?"

And we say "Oh, yes, you do," because the law requiring a life settlement provider license is specific enough to cover that situation.

And they say "Okay. Never mind. Forget we ever asked." They go off. They don't come through us again and get licensed. They just go to these trusts and buy a beneficial interest in the trust, and they don't actually buy the policy.
Is that what they're doing?

MR. FREEDMAN: From the STOLI schemes that we've seen --

MS. MILLER: That's what it is?

MR. FREEDMAN: -- that's what it is.

MS. MILLER: So when you say it's two separate markets, it's separate players. It's not even --

MR. FREEDMAN: You made the case for me. I mean, when -- you know, if they thought that they were going to get away with something and you said it doesn't look like it's a life settlement to us -- or it would be a life settlement, they don't want to be regulated.

Again, when the scrutiny, when the lights are on and the -- and the regulation requires the level of scrutiny and diligence that we have to provide, that's good for investors. But it's good for the consumer and makes sure that there is a healthy market.

MS. DAVIS: I have another question about your verification of coverages. How many verification of coverages are requested as compared to how many policies are actually bought?

You're suggesting that the insurer should
reevaluate every policy they get a verification of
coverage on, but not every policy that they would
get a verification of coverage on would be a
policy that would be sold.

MR. FREEDMAN: Right. I'm sure that -- I
don't know the statistic. I don't know a number
that tells -- that answers your question as to how
many verification of coverages are received versus
how many are purchased.

But, again, the point is that the carrier is
notified of a potential sale of the policy. They
also are notified at the time of the assignment of
the policy, the transfer to the new owner. So
there's, again -- they do know at that time which
policies are actually sold.

MS. DAVIS: Does is specifically say this
policy is being viaticated or this policy is being
sold?

MR. FREEDMAN: Every carrier knows which ones
are being sold. It's not just a simple -- I mean,
this is part of what Darwin's testimony was, that
carriers are treating changes of ownership
differently for life settlements they change --
than they do for change of ownership for placing
it into a trust, a family trust, or from a
business, you know, to business. So carriers
track life settlements. They know which policies
are sold. They treat them differently at every
stage of the -- every stage.

Again, you know, we're just saying where we
know there is that additional level of attention,
additional level of scrutiny -- these are
regulated transactions. There's no one trying to
hide who owns it; and, again, the requirement of
the law that we have to notify the insured who
owns it if it changes ownership -- is that that's
a secure transaction for both the consumer and the
investor.

MR. BAYSTON: I would just make one comment
that I look at this as the simple part of this
transaction is that on one end of the spectrum, we
have seniors who have insurance policies they no
longer need, want or can afford. And they have
the right to sell them, and they're looking to
sell those in the marketplace.

And on the other end, you have an investor
who is making a decision on buying those policies
and providing that capital for those seniors. And
I think I -- one view that one could take is that
investors are pretty good at measuring the amount
of risk they have involved in the investment.

So anything that would be perceived as
increasing the risk that those investors have is
going to result in them paying, you know, a lesser
price to the consumer, to the senior who is trying
to sell that.

So actions that could be taken that will
reduce perception or the reality of risks that
those investors have, then the benefit of that
flows back to the seniors who are selling
policies.

MS. MILLER: Thank you for making that
connection. Is there anything else that you
wanted to add? No? Anybody else have questions?

Okay. We have -- thank you very much for
your testimony.

We have three more -- I think we have three
more speaker cards. So if everybody is on board,
hopefully, let's just push through instead of
breaking for lunch. It's 1:00 o'clock, and
hopefully, we can finish up pretty soon.

Thomas Weinberger is the next speaker card on
behalf of the Institutional Longevity Markets
Association.

MR. WEINBERGER: Good afternoon. My name is
Tom Weinberger. I'm a partner at Stroock, Stroock & Lavan. We are a full-service law firm with offices in Miami, New York, D.C. and Los Angeles, and we serve as general counsel for the Institutional Longevity Markets Association. I am appearing today on their behalf.

ILMA was formed by institutional investors, leading investment banks that were focused on longevity and mortality markets and in life settlements. Today, the members comprise Wells Fargo, Wilmington Trust, Credit Suisse, Fortress, Neo Partners and other investor groups, some of whom are investors on behalf of pension funds, and they are all institutional investors.

I appreciated and enjoyed Mr. McDowell's remarks. I thought they were very passionate and dramatic. I would submit that, as far as accuracy goes, perhaps not as much. I don't think we're talking today about STOLI. What we're talking about is whether a true secondary market will exist in the state of Florida.

The institutional investors that make up ILMA participate in primarily what is called the tertiary market. When you look at the life settlement industry, you have the primary market,
which is the initial issuance of the policy by the
insurance company to the original policy owner;
the secondary market is when that policy first
gets settled to a life settlement company; and the
tertiary market is all the subsequent trading that
goes on in that policy.

This tertiary market is crucial for the life settle -- the secondary market. Without the
tertiary market, the secondary market does not
exist because there needs to be liquidity. It's
the pension plans who can buy large blocks of
policies that provide the capital that ultimately
feeds this market.

And while Mr. McDowell was very passionate, I
also want to express a certain passion, because I
truly believe in the life settlement industry. It
is a product that provides a great service to
seniors. It's a product that provides a
reasonable return to institutional investors. And
if the insurance companies were honest about it, I
think it provides a lot of opportunities for them
as well in terms of product design and how they
work with their customers.

And I know Mr. McDowell went on and
constantly referred to the institutional investors
as hedge funds. I assume it was meant in a pejorative way. The reality is we're really talking about long-term investors with long-time horizons for whom this type of product makes sense because it matches their cash flow needs.

For pension plans that know that they have to make payouts in the next 10, 20, 30 years, these are perfect products, because they can invest today in products that will provide cash flow downstream. It's not people looking for outsized returns.

And if you ask investors, I think they'll tell you that the returns -- some of them have lost money, some have made money, but I think overall, the returns are respectable. It's not someone trying to grab and make a ridiculous return. That's not what the market is about. But if all the participants act in the market together, you can have a true and active secondary market.

Now, the question is, why do the institutional investors seek the protections that they're asking for today? And the reason is when we're buying blocks of policies, we actually have limited access to information. We're provided
with some sale documentation that was provided at
the time of the life settlement. Typically, the
due diligence is limited to a review of the policy
at the application, the life settlement contract
and some supporting documents.

We, at Strook, are actively involved in
helping the companies do diligence on these
policies, and I can tell you we do not have access
to the insureds. It's true that when you buy a
policy, you get updated medical information, but
that's not the same thing as being able to sit
done and talk to the insured and ask them, why did
you take out this policy? Why did you sell it?
That doesn't happen.

You certainly can't do it when you buy a
block of 100 policies or so, which is really what
happens in the tertiary market. And it's not the
practice and there are, in fact, due to privacy
laws, significant limitations on who can actually
contact the insured and when. So to say that
there's access to the insured is not entirely
accurate.

Also, the concept that the law is well
settled and there are legal certainties is also
not true, and I think that's what's driving the
interest in seeking the reforms and the
legislation that the institutional investors want.

The concept of a -- being able to challenge a
policy after the end of the contestability is
something that's actually very much in flux. In
Florida itself, you have two courts that came out
with different decisions on the issue. So it's
not -- it's far from a legal certainty. It's
unknown.

There have been only a few courts that have
actually addressed the issue. And the concept
that if there were no ability to challenge for
lack of insurable interest after the end of the
contestability period, that you are now going to
open the door to fraud, I don't think that's going
to prove to be the case.

And I think it's not going to be the case for
several reasons: One, in New York, there was a
case many years ago, the Caruso decision by the
New York Court of Appeals, where they said that
you can not challenge a policy on any basis after
the end of the contestability period. That has
not led to a rampant increase in fraud in the
state of New York.

I think investors do a very good job of
identifying policies that were fraudulently
originated, and they don't -- and they don't buy
them when they can identify them. But the reality
is there's just the lack of information.

And when you couple the lack of information
and the limits on the diligence that can be done
at the time you're originating policies with the
legal uncertainties in this area, it makes it much
less attractive for investors to come in. And
without the investors in the market, you're not
going to have the liquidity that you need for a
secondary market.

And, you know, if you look at what's going on
in the United States today, the current economic
environment, you have many Baby Boomers who are
entering their retirement years. Following the
Great Recession, there has been significant
reduction in asset values.

A lot of them have needs for long-term care
that are far more expensive than anyone ever
imagined be the case, and there's a real need
today for people to be able to settle their
policies to either fund a comfortable retirement
or perhaps pay for long-term care needs.

And what we're talking about today is, will
there be a secondary market to provide that
service to them, to provide that option? And I do
think that if you look at the policy origination,
it's really the carriers who are in the best
position, at the time a policy is originated, to
do the proper diligence.

Yes, it's true that they ask questions and
you have to fill out a form. But should the
obligation of the carrier stop there? It's simple
enough in the two-year contestability period for
them to figure out what's going on with the
policy.

And we're not talking about doing this with
every policy. The issues are going to arise with
a certain block of policies. It's going to be
large face policies with older age issuances. All
they need to do is, six months down the road, call
up the insured and say, "Thank you for taking out
the policy. How is -- you know, is everything
okay? Do you need more information?"

You quickly find out if the insured sold the
policy. It's happened time and time again, but
the carriers didn't take that step and weren't
interested, quite frankly, weren't interested in
taking that step.
It's not something institutional investors can do four or five years down the road. It's certainly something that the companies can do during the contestability period without too much difficulty.

So I think just to quickly summarize --

MS. MILLER: Let me interrupt you. Do you think that the reason they don't, or to the extent that they don't, is just because that would be an expensive thing to do?

MR. WEINBERGER: I don't think it's an expensive thing to do. I think there have been cases where it's been done. Again, we're talking probably about a relatively small group of policies. We're not talking about doing it with someone who's 25 years old and took out a term policy.

We're talking about sales of universal life policies to people who are over the age of 65 and face amounts over a million dollars. It's not -- it's not a big group. It's something that they certainly can do during the contestability period. I don't think there's a lot of cost or a lot of effort involved in doing so.

MR. TRONCOSCO: You lose me on the fraud

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issue, and that's just because, you know, their testimony was quick to point out that 98 percent of, you know, the companies are not having this issue, and it seems like most of their problems came with one company.

And so, you know, if you make that issue -- I understand it alleviates your client's issues, but doesn't that perpetuate a fraud problem to just push the fraud to another sector of the market? I mean --

MR. WEINBERGER: No. I appreciate that. I think that's a very good observation. I think the answer is it will likely not, and here it comes out to a question of balancing what's most important here.

I think it would likely not lead to an increase in fraud for several reasons: One, the carriers that don't have the problems today already take the steps and identify, at the time of origination, the policies that are likely fraudulent because there are steps you can take.

I do diligence on these policies, and even with the limited information I have, I can find fraudulently-originated policies from time to time. There are certain red flags and the
carriers know what they are.

So I think it's possible to do it at the time of origination; need to ask a few more questions, need to add questions to the application. All of this is being done, and it's easy to follow up and easy to see inconsistencies in these policy applications if you care to look for it.

I think what's going on is they would get in information, which sometimes was fraudulent, but they'd merely check the box and say, okay, we got this, we got this, we got this. No one would bother to look.

And, in fact, there's been quite a bit of testimony that companies even realize after the fact that there were red flags, and there are memos to this, that they ignored the issues or they didn't act on the red flags.

All we're saying is that the companies should take a look and should act on it. And, again, we're talking probably about a segment of the market that is highly profitable for everyone involved that probably deserves a little more attention. And because other companies have been able to handle the issue, I think the insurance companies can handle the issue.
And the institutional investors don't want to buy these policies either. I get paid to help them find the fraudulent policies. But, again, because of where we are in the chain, it's not always possible to do so.

MR. TRONCOSCO: What concerns me, I guess, is, you know, how many lawyers -- not the fact of how many lawyers we have in the room, but I know we have a lot of lawyers in the room. And what concerns me is what we're talking about is handcuffing the law of equity.

And, you know, for everyone that went to law school, we understand that's the judge's power to make sure that things are fair and balanced, to put it in layman's terms. So that's the only thing that concerns me. You know, every time you do that, you do open the door to fraud, so that's just my point.

MR. WEINBERGER: Again, fair point. But I do think there is a significant value to making sure that the institutional investors can act in this space, and that you have to look at what the legal uncertainty does to the ability of the investors to be in this space, and whether you want the investors in the space and you want a secondary
market. So there is some balancing of equities that has to go on on a more global scale than just on the individual policy issuances.

MS. MILLER: Do you know how big the secondary and the tertiary markets are? We haven't been able to figure that one out, to be quite honest.

MR. WEINBERGER: There have been some reports. I think there's some studies, and I believe that in the submission that you received from Fortress, they had some studies in there that provided figures. Those are probably the most accurate figures that you'll find. I don't have independent information.

MS. MILLER: So is it in the billions, the tertiary market?

MR. WEINBERGER: Probably, yeah. And it's something that could grow. I mean, one thing that a number of states, including Florida, has been considering is whether, in order to fund Medicaid long-term care costs, whether the states themselves want to get into the business of life settlements.

So it's a market that's poised to grow. It's meeting a significant need. But in order to grow,
there does need to be a greater amount of legal
certainty around some of these issues.

MS. MILLER: I'm going to tell you it's been
a really long road, from my perspective. But
we don't have to digress into it, but we've had
quite a number of fraud cases and officers of
licensed viatical companies that we've had to go
through the process of, A, proving what was going
on, and then B, working with prosecutors to take
those cases and stop those people from
masquerading as legitimate viatical or life
settlement companies. And I'm not sure that we
got them all.

I mean, the -- what I'm hearing is that there
are a whole other group of people out here who, to
stay off the radar now, are buying -- or were
buying policies by buying the -- or by trading a
beneficiary interest.

I don't know what the next iteration is going
to be, but this group of issues is so convoluted,
I'm not sure that it isn't ripe for the courts
whether rather than trying to get involved in
these transactions, you know, with hard-and-fast
rules from the legislature.

MR. WEINBERGER: Well, I think actually,
there was a lot of time spent discussing beneficial interest. Most states that have adopted updated life settlement laws actually expressly prohibit the sale of beneficial interest in a trust during the contestability period.

That practice, as a result, has largely disappeared from the market, if not entirely. I'm not aware of any institutional investors that are active in doing anything like that today.

MS. MILLER: So the STOLI issue is pretty much an issue of the past, 2007/2008, other than the fact that there's still policies out there that were procured that way?

MR. WEINBERGER: I think a lot of the most egregious practices probably are from that period. And both the insurance companies have become much better at identifying them and preventing them; the institution investors are better at identifying people that participate in those types of activities and not purchase those policies.

But that doesn't obviate the need for more legal certainty in the space, because there are a lot of issues that are floating around, especially in the courts in Florida. And I know for a fact that -- I have a number of clients that, when we
review policies for them, they also ask us -- you know, we look at policy design issues and other factors and help them evaluate the policies.

Right now, they are actually handicapping any policy that's issued in Florida because of the legal uncertainty, which means that the prices they're -- that they're willing to pay for Florida policies are much lower than the rest of the country.

MS. MILLER: Okay. Thank you.

MR. WEINBERGER: Thank you.

MS. MILLER: James Tollerton, Professional Benefits, Inc. Thank you for sticking around and not being first.

MR. TOLLERTON: Thank you for letting me get up and circulate my blood. And for the record, I am Jim Tollerton of CLU and CHFC, Professional Benefits in Sarasota, Florida.

I was invited by representatives at the National Association of Insurance and Financial Advisors, Florida Chapter, to come and speak as a typical Florida insurance agent today about my experiences in this area.

It's actually been very instructive and I appreciate the information that's been provided.
I'm intrigued by the questions you've asked. I do not have a great deal of experience personally in the settlement industry, except peripherally.

I do, in the interest of disclosure, want to tell you that I did settle a policy, actually with a friend and a client, about 15 years ago who had developed cancer and was offered a settlement. He accepted it and it was my only experience with it.

I became very uncomfortable with the process. I would get calls every three to six months, "How's he doing? What's going on," and so forth. And as I sit here and listen to the colloquy we've been going through, I -- it occurs to me that this is that slippery slope.

The farther we get away from the essential underpinnings of the insurance -- life insurance industry of insurable interest, I think the slippier the slope is going to be. When you have somebody else owning a life insurance policy on you, you don't know who it is, you don't know where it is, you don't know what's going to happen, that is very uncomfortable.

This came to light to me -- an attorney -- a couple attorneys have asked me to review these sorts of policies because they didn't understand
what in the world is going on here. And I remember one instance last year, a gentleman in his, I believe, early 70s had a $2 million-dollar policy by a legitimate company, a name you'd all know, not one we'd characterize ill in the industry.

And he said, "Geez," to his attorney, "I'm afraid I don't know who owns my policy anymore. This agent came to me and offered me a loan so I said sure. It wouldn't cost me anything really. They bought me a nice dinner at a fancy steak restaurant and so forth."

And now, at the end of two years, they say, "Well, you don't really have to pay that loan back."

And I -- of course, I interject parenthetically, most of these seniors that deal with this have no idea of the tax implications of a loan forgiveness or boot or anything like that, have no idea where this policy is going and what's happening. All that's dangled out there is that nice attractive dollar amount, and gee whiz and it's painless and so forth.

And all of a sudden it dawned on this guy, he's got $2 million on his head. He has no idea
who owns it. That's not been disclosed at all.
It's long gone in tertiary four, five, six times.
Who knows where it's been sold to.

So I think the bottom line from an insurance
agent's perspective is that we're in the business
of, where there is insurable interest, insuring
lives for families, for businesses, for charities
in some instances.

And 99.9 percent of our agents in NAIFA and
the agents, legitimate agents in Florida, have no
interest in this market because of the ongoing
problems that just naturally happen if you can
sell it.

I think the analogy of the mortgage industry
where the mortgages were packaged together and
sold in the secondary, tertiary and down-the-road
market, and look at the trouble we got into. And
that's dealing with homes and objects. It's not
dealing with human lives, which is what we all
are, fortunately, by the grace of God, living
today.

So I summarize my remarks that way. I would
be glad to answer questions as a practical matter
from an insurance agent's point of view from a
small town in the back waters of Florida.
MS. MILLER: Well, I suppose one thing that we had identified from the assignment from the legislature is that it assumed that we want to ensure that the tertiary market continues to exist for Florida consumers and for Florida seniors. And from what I'm hearing, it may be that that market needs to exist for investors but not necessarily for seniors. Is that your perspective on it?

MR. TOLLERTON: Speaking only for myself, I'm uncomfortable with the industry generally, to be honest with you.

MS. MILLER: Thank you very much.

MR. TOLLERTON: Thank you.

MS. MILLER: Oh, my goodness, I can't believe I gave Paul Sanford the last word unless there's somebody else here that I don't have a speaker card for.

MR. TRONCOSCO: Do you waive your time?

MS. MILLER: No. Mr. Sanford is not going to waive his time in support.

MR. SANFORD: Thank you. Paul Sanford representing the Florida Insurance Council. I just want to comment on a couple of things that were said without taking too long, because
everybody is ready to go.

The issue of these verification of coverages has come up two or three times. Basically, when an insurer gets a verification of coverage, it's a question of, is the policy in force, and are premiums paid?

It's very unlikely that any substantial re-underwriting of the contract is going to take place at that time. And to try to use that as a vehicle to cut off any questions about insurable interest just seems to be way far afield from our perspective.

I think the other issue that was brought up, again, about the return of premiums, insurable interest and that sort of thing, and I think if there's one thing that you can really count on today is every case, the facts are different.

If you're going to find equity in these cases, which is what the courts are trying to do, you must look at each case individually in order to arrive at the right conclusion and see that the parties who participated in the wrongdoing are punished to some extent, and those who did not are not punished.

And the only way that can happen is to go
through the courts. Anything that we may do to
guarantee that a return of premiums in every one
of these circumstances may well be guaranteeing a
large return on a risky investment that was bought
with knowledge of what they were buying. So from
our perspective, we don't really think any
legislation is necessary.

But if you wanted to consider some
legislation, it might be to look at the NAIC model
act on these STOLI transactions, especially the
five-year provision on nonrecourse premium
financing and the limitations on transferring
those policies, and combine that with the trust
provisions from the NCOIL Act that would get to
these issues where they're able to deceive the
insurers on what the contract really is.

Those two things might well forever remove
STOLI from the -- from this planet, and that
appears to be the only real hazard that this
secondary market is having.

MS. MILLER: I disagree that it's the only
hazard.

MR. SANFORD: Well, true. Perhaps a larger
one we discussed today.

MS. MILLER: That might be the hazard du jour
or maybe the hazard of 2007/2008; and there will be a new hazard du jour in 2014.

And I would ask just a couple things. One is, what have the life insurance companies done to strengthen their underwriting and their ability to identify policies that have been sold? And can they, in fact, tell if there is a policy that is owned by a trust that the beneficial ownership of it has changed?

MR. SANFORD: Quite frankly, I think the underwriting policies are about as strong as they can get. I think we've seen situations where we get an application. It's attached -- it's -- the application may or may not be fraudulent, which some of those things you can find.

We've received financial statements from CPAs that didn't exist. The policy is purchased by a trust that appears to be for the benefit of a person who does have an insurable interest in the applicant.

And other than having to go back and look every day after that to see what happened, we can't keep up with what that trust does. And unless we want to expend huge sums of money and large amounts of time, which will increase the
cost of insurance for everyone to try to ferret this out, I don't really know what else they can do.

MS. MILLER: Well, they can pick up the phone and call the insured.

MR. SANFORD: Call who?

MS. MILLER: The insured.

MR. SANFORD: Yes.

MS. MILLER: They can call them and they can say, you know, "Mr. Smith, I see that Joey Smith is your beneficiary. Is Joey your son?"

"Yes."

"How old is Joey? Where did he grow up? Where does he live now?" And those things, they could verify on the internet.

So I'm not sure that there aren't things that life insurance companies could do to kind of check some of this out, and I think that they do do some of that and maybe more now than they have done in the past.

MR. SANFORD: And I think the larger the policy, the more checking that goes on.

MS. MILLER: Probably so.

Anybody else have any questions?

MR. SANFORD: Thank you.
MS. MILLER: Thank you.

Okay. Does anybody else wish to testify? Well, see, we got through this without any bloodshed. Today, we have heard testimony from interested parties on the secondary, or as it may now be known, the tertiary life insurance market in the state of Florida.

The Office will carefully review and consider the testimony offered here today, as well as all materials submitted to the Office before making our report to the legislature. If anyone in the audience wants to provide additional comments or materials, please e-mail them to secondarylife@flior.com no later than October 30th, 2013.

Materials received on this matter will be available to the public and posted on the Office's website. Therefore, if any interested parties believe they have comments or information that has not already been expressed today, feel free to add those.

Thank you for your participation. If there's nothing further, this hearing is adjourned.

(Whereupon, the proceedings concluded at 1:35 p.m.)
CERTIFICATE OF REPORTER

I, LISA A. BABCOCK, do hereby certify that I was authorized to and did report the foregoing proceedings, and that the transcript, pages 3 through 148, is a true and correct record of my stenographic notes.

Dated this 12th day of November, 2013 at Tallahassee, Leon County, Florida.

LISA A. BABCOCK

Court Reporter

FOR THE RECORD REPORTING TALLAHASSEE, FLORIDA 850.222.5491
APPENDIX B

SURVEY AND RESULTS
SECONDARY LIFE MARKET SURVEY QUESTIONS

* 1. What is the total count of Florida in-force life policies as of June 30, 2013?

* 2. What is the total sum of the face amount of Florida in-force life policies as of June 30, 2013?

* 3. What is the count of Florida in-force life policies that were owned by a trust as of June 30, 2013?

* 4. What is the sum of the face amount of Florida in-force life policies that were owned by a trust as of June 30, 2013?

* 5. For the previous two responses, are your answers based on known or estimated information?

* 6. What is the count of Florida in-force life policies that were owned by a bank or financial institution as of June 30, 2013?

* 7. What is the sum of the face amount of Florida in-force life policies that were owned by a bank or financial institution as of June 30, 2013?

* 8. For the previous two responses, are your answers based on known or estimated information?

* 9. What is the count of Florida in-force life policies that were financed through a premium finance company or other structured loan program as of June 30, 2013 (do not include insurer-financed policies)?

* 10. What is the sum of the face amount of Florida in-force life policies that were financed through a premium finance company or other structured loan program as of June 30, 2013 (do not include insurer-financed policies)?

* 11. For the previous two responses, are your answers based on known or estimated information?

* 12. What is the count of Florida in-force life policies that have been viated as of June 30, 2013?
13. What is the sum of the face amount of Florida in-force life policies that have been viaticated as of June 30, 2013?

14. For the previous two responses, are your answers based on known or estimated information?

15. Please provide any comments you have regarding the data that has been provided.

16. Does your company have procedures in place to evaluate the impact of viaticated policies on the net-present-value of the life insurance book of business?

17. If you responded 'Yes' to the previous question, please provide an explanation of the procedures or include them in the Supporting Documentation component and respond 'Supporting Documentation' here. DO NOT INCLUDE 'TRADE SECRET' INFORMATION IN YOUR RESPONSE.

18. Provide the name and title of the officer of the company who has reviewed the submission of this data and who would attest that the above information is true and accurate to the best of his or her knowledge.

* Required field
SUMMARY OF SURVEY RESULTS

393 of 425 companies completed the survey (92.4%).

The companies responding represent 92.3% of the face amount of Florida life insurance policies in-force as of December 31, 2012.

63 companies had no in-force policies in Florida as of June 30, 2013.

Three companies reported data solely related to credit life and term policies.

327 companies responding to the survey appear to have in-force Florida policies that could be subject to viatication.

319 companies did not have procedures in place to evaluate the impact of viaticated policies on the net-present-value of the life insurance book of business.

Trust-Owned, Bank-Owned, and Premium-Financed Policies:

186 companies (57%) relied on estimates to respond as they were not able to readily identify all trust owned, bank-owned, and premium financed policies

Based on either known or estimated data:

- **Trust-owned Policies:**
  - 175 companies identified 52,725 in-force life policies owned by a trust for $72.348 billion.
    - 86 (49%) of these companies identified 11,476 trust-owned policies based on known data.
    - 89 (51%) of these companies identified 41,249 (78%) trust-owned policies based on estimates.
    - 85 (49%) of these companies identified $14,044,453,841 (19%) trust-owned policies based on known data.
    - 90 (51%) of these companies identified $58,303,266,059 (81%) trust-owned policies based on estimates.
  - 157 companies reported no policies on their books as trust-owned.
    - 95 (62.5%) of these companies responded based on known data.
    - 57 (37.5%) of these companies responded based on estimates.

- **Bank or Financial Institution Owned Policies:**
  - 89 companies identified 9,647 policies owned by a bank or financial institution, with a face value of $6.280 billion.
    - 33 (37%) of these companies identified 4,500 bank-owned policies based on known data.
    - 56 (63%) of these companies identified 5,147 bank-owned policies based on estimates.
• 33 (37%) of these companies identified $2,137,438,295 in bank-owned policies based on known data.
• 56 (63%) of these companies identified $4,142,757,582 in bank-owned policies based on estimates.

  o 238 companies reported no policies bank-owned policies on their books
    • 138 (58%) of these companies responded based on known data.
    • 100 (42%) of these companies responded based on estimates.

*Premium Financed Policies:*
  o 16 companies identified 8,134 policies financed through a premium finance company or via another structured loan program in the amount of $1.340 billion in face value.
    • 9 (56%) of these companies identified 8,022 premium finance policies based on known data.
    • 7 (44%) of these companies identified 112 premium finance policies based on estimates.
    • 9 (56%) of these companies identified $903,861,925 in premium financed policies based on known data.
    • 7 (44%) of these companies identified $436,154,886 in premium financed policies based on estimates.

  o 311 companies reported no premium finance policies on their books
    • 150 (48%) of these companies responded based on known data.
    • 161 (52%) companies responded based on estimates.

*Viaticated Policies:*

159 companies (49%) relied on estimates to respond as they were not able to readily identify all viaticated policies.

  o 64 companies have identified, based on either known or estimated data: 1931 viaticated policies at a face value of $1.500 billion in face value.
    • 24 (38%) of these companies identified 364 viaticated policies based on known data.
    • 40 (62%) of these companies identified 1567 viaticated policies based on estimates.
    • 24 (38%) of these companies identified $474,392,147 viaticated policies based on known data.
    • 40 (62%) of these companies identified $1,025,722,008 viaticated policies based on estimates.

263 companies (80%) have no knowledge of viaticated policies on their books. Of these 263 companies 257 have no procedures in place to evaluate the impact of viaticated policies on the net-present-value of the life insurance book of business.
## 2013 Life Policy Target Survey Results

### Question # Summary of Question

<table>
<thead>
<tr>
<th>Question #</th>
<th>Company Totals (includes estimated data)</th>
<th>&quot;Known&quot; Totals (excludes estimated data)</th>
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</thead>
<tbody>
<tr>
<td>1</td>
<td>Total Count of Florida in-force policies</td>
<td>6,628,892</td>
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<tr>
<td>2</td>
<td>Total Sum of Florida in-force policies</td>
<td>$987,404,181,004</td>
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<tr>
<td><strong>Number of companies with Florida in-force policies:</strong> 327</td>
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<td></td>
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<tr>
<td>3</td>
<td>Number of policies owned by a trust</td>
<td>52,725</td>
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<tr>
<td>4</td>
<td>Face value of policies owned by trust</td>
<td>$72,347,719,901</td>
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<tr>
<td><strong>Number of companies identifying trust-owned policies:</strong> 175</td>
<td></td>
<td></td>
</tr>
<tr>
<td>6</td>
<td>Number of policies owned by bank or financial institution</td>
<td>9,647</td>
</tr>
<tr>
<td>7</td>
<td>Face value of policies owned by bank or financial institution</td>
<td>$6,280,195,877</td>
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<td><strong>Number of companies identifying bank owned policies:</strong> 89</td>
<td></td>
<td></td>
</tr>
<tr>
<td>9</td>
<td>Number of premium-financed policies</td>
<td>8,134</td>
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<tr>
<td>10</td>
<td>Face value of premium-financed policies</td>
<td>$1,340,016,811</td>
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<td><strong>Number of companies identifying policies financed:</strong> 16</td>
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<tr>
<td>12</td>
<td>Number of policies viaticated</td>
<td>1,931</td>
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<tr>
<td>13</td>
<td>Face value of policies viaticated</td>
<td>$1,500,114,155</td>
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<tr>
<td><strong>Number of companies identifying viaticated policies:</strong> 64</td>
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<td></td>
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</tbody>
</table>

* Excludes companies that expressly indicated that they do not have life insurance business in Florida as of June 30, 2013, or write only the kinds of policies that would not be subject to viatication (e.g., credit life, group, term, or accidental death and dismemberment).
APPENDIX C

FLORIDA REGULATORY AND ENFORCEMENT ACTIONS PERTAINING TO VIATIONAL SETTLEMENT PROVIDERS
FLORIDA REGULATORY AND ENFORCEMENT ACTIONS
SINCE OCTOBER 1, 1996

The below information is current as of November 30, 2013

Administrative Complaints – (2)

- Accelerated Benefits Corporation
- Wm. Page & Associates, Inc. d/b/a the Lifeline Program

Orders to Show Cause – (3)
Includes Notice and Order to Show Cause

- Coventry First LLC
- Future First Financial Group, Inc.
- Mutual Benefits Corporation

Orders to Cease & Desist – (7)

- Findco, Inc.
- Future First Financial Group, Inc.
- GWG Life Settlements, LLC f/k/a Great West Growth, LLC
- Mutual Benefits Corporation
- Resource Funding Group, Inc. et al.
- Robin Hood International, Ltd et al.
- VESPERS, LLC

Orders – (10)

- Accelerated Benefits Corporation
- Amerifirst Funding Group, Inc.
- Future First Financial Group, Inc.
- GWG Life Settlements, LLC f/k/a Great West Growth, LLC
- Justus Viatical Group, LLC et al.
- Kelco, Inc.
- Neuma, Inc.
- Resource Funding Group, Inc., et al.
- Robin Hood International, Ltd et al.
- Wm. Page & Associates, Inc. d/b/a The Lifeline Program

Consent Orders – (2)
Excludes application-related consent orders

- Life Partners, Inc.
- Mutual Benefits Corporation
Examination/Investigation Related Consent Orders – (14)

- CMG Surety, LLC - $23,000
- CMG Surety, LLC - $15,500
- Coventry First, LLC - $1,500,000
- GWG Life Settlements, LLC t/a Great West Growth, LLC - $162,000
- Life Settlement Corp d/b/a Peachtree Life Settlements - $50,000
- Life Equity LLC - $35,000
- Maple Life LLC - $28,000
- Magna Life Settlements, Inc. - $13,000
- Mutual Benefits Corporation - $10,000
- Q Capital Strategies, LLC - $15,500
- Q Capital Strategies, LLC - $18,000
- Proverian Capital, LLC - $28,000
- VESPERS, LLC – $85,000
- Wm. Page & Associates d/b/a The Lifeline Program - $25,000

Licenses Revoked – (4)

- Accelerated Benefits Corporation – February 5, 2001
- Future First Financial Group, Inc. – May 17, 2002
- Kelco, Inc. – March 21, 2003
- Mutual Benefits Corporation – March 29, 2005

Licenses Surrendered – (9)

- Viaticare Capital, L.P. – December 31, 2002
- Viaticus, Inc. – December 31, 2002
- Life Settlements International, LLC – September 10, 2004
  - Note: later reapplied for licensure with new owners and approved
- Wm. Page & Associates, Inc. – March 15, 2005
  - Note: continues to report on a quarterly basis under a Final Order and will do so for the foreseeable future
- Living Benefits Financial Services, LLC – March 26, 2008
- Dedicated Resources, Inc. - March 9, 2011
- Life Settlement Corporation – September 9, 2011
- Life Settlement Solutions – October 7, 2013

Licenses Denied – (8)

- AmeriFirst Funding Group, Inc.
- Future First Financial Group, Inc.
  - Note: later reversed, subsequently revoked
- Imperial Life Settlements, LLC
  - Note: later reversed
- Justus Viatical Group
ApplicationsFiledandWithdrawnwithoutfurtheractivity–(26)

- American Benefits Services, Inc.
- Axis Thought Capital, LLC
- Beneficial Assurance, Ltd.
- Cato Capital, LLC
- Centre Life Finance Ltd.
- Centre Life Finance Ltd. Trust
- Fairmarket Life Settlements Corp.
- Genesett Capital Corp., Jacksonville, FL
- Genesett Settlements Corp. (f/k/a Genesett Capital Corp.)
- Kelco Life, LLC
- Legacy Benefits Corporation
- Montage Financial Group, Inc.
- Natlis Capital, LLC
- Neuma, Inc.
- Neuma, Inc. d/b/a Neuma, Inc. of Illinois
- Portsmouth Settlement Co. Inc.
- Reliance Financial Group, Inc.
- Resource Funding Group, Inc.
- Spiritus Life, Inc.
- VESPERS, LLC
- Viatical & Elderly Settlement Providers, LLC
- Viatical Benefactors, LLC – Greensboro, NC
- Viatical Benefactors, LLC – Ft. Lauderdale, FL
- Abacus Settlements, LLC
- Spiritus Life, Inc.
- Viasource Funding Group, LLC
APPENDIX D

LICENSED VIATICAL SETTLEMENT PROVIDERS IN FLORIDA
**LICENSED VIATIONAL SETTLEMENT PROVIDERS IN FLORIDA**

*The below information is current as of November 30, 2013*

<table>
<thead>
<tr>
<th>Company Name</th>
<th>Date Licensed</th>
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<tbody>
<tr>
<td>CMG Surety, LLC</td>
<td>12/11/2003</td>
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<td>Coventry First, LLC</td>
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<td>Credit Suisse Life Settlements, LLC</td>
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<td>EaGIL Life Settlements, LLC</td>
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<td>Econotree Capital, Inc.</td>
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<td>GWG Life Settlements, LLC</td>
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<td>Imperial Life Settlements, LLC</td>
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<td>Institutional Life Services (Florida), LLC</td>
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<td>Life Equity, LLC</td>
<td>12/21/2001</td>
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<td>Lotus Life, LLC</td>
<td>5/18/2012</td>
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<tr>
<td>Magna Life Settlements, Inc.</td>
<td>2/12/2004</td>
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<td>Maple Life Financial, Inc.</td>
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<td>Proverian Capital, LLC</td>
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<td>Q Capital Strategies, LLC</td>
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<td>Vespera Life, LLC</td>
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