

2009 SHAPING UP AS ACTIVE YEAR IN BATTLE TO DETER ABUSE OF SENIORS BY STOLI PROMOTERS

States across the nation are expected to consider legislation next year to protect senior citizens from the scam known as stranger-originated life insurance (STOLI).

Following a successful campaign in 2008 which saw 11 states enact legislation to deter this inappropriate use of life insurance, 2009 could prove to be even more eventful amid growing concerns over a transaction that benefits speculators and hedge funds at the expense of seniors.

"We are gratified that more and more states are taking a hard look at STOLI and recognizing the potential risks to seniors. Unexpected taxes, liability concerns, loss of privacy, loss of eligibility for government entitlements; the list goes on and on. Doing nothing is not an option. Every senior in every state deserves the highest level of protection from STOLI promoters," said Frank Keating, president and CEO of the American Council of Life Insurers (ACLI).

"Even though the nation is focused on the current financial crisis, the effort to deter STOLI should not be sidetracked. The abuses will continue to grow unless state legislatures act, and seniors in the states that fail to act will be the primary targets," said Cliff F. Wilson, CLU, ChFC, CLF, LUTCF, president of the National Association of Insurance and Financial Advisors (NAIFA).

States where STOLI bills likely will be considered next year include Illinois, New York, Georgia, Minnesota, Washington state and Wyoming. Most of the states are considering legislation based on the models developed by the National Association of Insurance Commissioners and the National Conference of Insurance Legislators.

The NCOIL model addresses all forms of STOLI, including schemes involving trusts, by establishing a statutory definition of STOLI and classifying it as a fraudulent act. It also contains reasonable restrictions against STOLI-related premium finance schemes.

The NAIC model targets the most prevalent form of STOLI, manufactured life settlements, by establishing a limited five-year moratorium on the settlement of STOLI policies. The moratorium does not apply to policies purchased with the policy owner's own money. Similarly, the moratorium does not apply to situations where the policy owner wants to settle the policy due to a change in life circumstances, such as illness, loss of job, divorce or death of the beneficiary.

New York is likely to follow the NCOIL approach in part, but also will emphasize consumer protections such as licensing of settlement brokers, clear disclosure of producer compensation and terms, annual reporting requirements, privacy protection and application of the state's Unfair Trade Practices Act to life settlements.

"Whichever approach the different states follow during 2009, the legislation must be substantive and effective. During the legislative battles of 2008, we saw instance-after-instance of STOLI promoters publicly claiming to support strong bills, while at the same time working behind the scenes to undermine the very same legislation by demanding 'tweaks' or amendments that would allow STOLI transactions to proceed unhindered," Keating said.

"STOLI threatens to undermine the life insurance marketplace for seniors with genuine family protection and estate planning needs. In these difficult economic times, state lawmakers cannot just sit by and allow the STOLI promoters to profit at the expense of our senior citizens. 2009 should be the year when lawmakers across the nation put an end to STOLI once and for all," Wilson said.

STOLI LITIGATION INCREASING ACROSS THE UNITED STATES

Litigation involving stranger-originated life insurance is increasing dramatically across the nation.

Currently, some 105 STOLI-related cases are pending in both state and federal courts, compared with only one case in the fourth quarter of 2005, according to an analysis by James A. Hoffman II, vice president and associate general counsel with Lincoln Financial Group. Hoffman presented his data at the recent annual meeting of the American Council of Life Insurers in Boston.

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According to the analysis, New York leads the way in STOLI litigation with 27 cases pending in trial or appellate courts. Second is California with 18 cases, followed by Minnesota with eight cases and Florida with seven.

While much of this litigation is still in the trial phase, some key questions are emerging from the early opinions handed down by trial courts.

These questions include:

- What evidence must an insurer present to prove that, at the time the policy is procured, a scheme existed to engage in STOLI?
- What are an insurer's rights if it is alleged that the insurer's agent participated in or knew about the STOLI scheme?
- What are an insurer's rights if a STOLI provider declares bankruptcy?

The analysis says that the questions raised by the STOLI cases highlight the importance of financial underwriting in fraud detection. Proper due diligence improves an insurer's ability to prove fraud claims. It is important to establish and then follow internal guidelines, verify financial representations, conduct credit checks and insist on complete applications.

However, insurers will face new challenges in the battle against STOLI, according to the analysis. These include facing increasingly complex trust arrangements, identifying premium financing programs and determining schemes where there may be multiple layers of intermediaries.

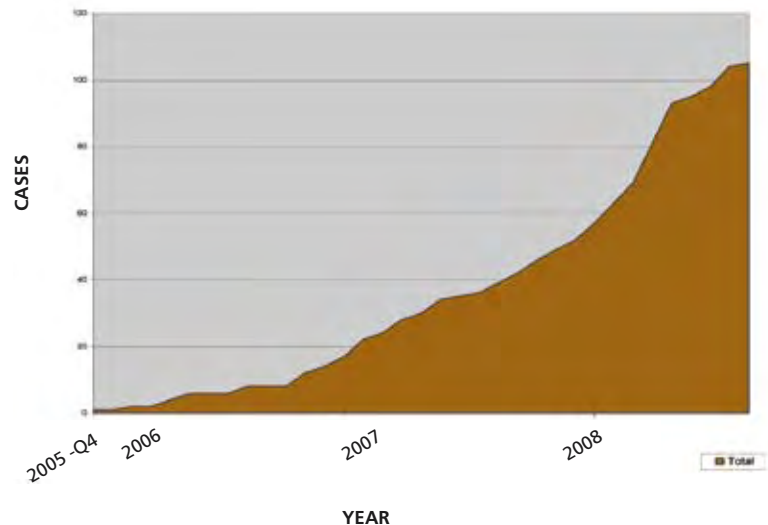
Michael Lovendusky, vice president and associate general counsel with ACLI, who moderated the session where Hoffman spoke, noted that regulation in this area is characteristically in reaction to market abuses.

"Today, the abuse is of insurable interest laws by means of stranger-originated policies attempting to evade detection and enforcement within contestable time periods. The courts are increasingly the battlegrounds where the fundamental integrity of the insurance system is being tried," he said.

105 STOLI CASES NATIONWIDE



STOLI CASES 2005 - PRESENT



STOLI Alert is published by the American Council of Life Insurers and the National Association of Insurance and Financial Advisors.

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For further information about *STOLI Alert* and the issue of stranger-originated life insurance, please contact us.

American Council of Life Insurers

101 Constitution Ave., NW, Suite 700, Washington, DC 20001
Bruce Ferguson & Michael Lovendusky, 202-624-2000 www.acli.com

National Association of Insurance and Financial Advisors

2901 Telestar Court, P.O. Box 12012, Falls Church, VA 22042
Gary Sanders & Roland Panneton, 703-770-8100 www.naifa.org