

SESSION OF 2008

**SUPPLEMENTAL NOTE ON SENATE
SUBSTITUTE FOR HOUSE BILL NO. 2110**

As Recommended by Senate Committee on
Financial Institutions and Insurance

Brief*

Senate Sub. for HB 2110 would amend the provisions of the Viatical Settlement Act of 2002 and enact new requirements governing viatical settlements. Among the amendments, the bill would establish a definition of and make a stranger-originated life insurance, commonly referred to as STOLI, a fraudulent viatical settlement act and would include owner and provider disclosures to be made to an insurer about these transactions.

Definitions

The Viatical Settlements Act of 2002 (The Act), as amended by this bill, would include the following definition:

- *Stranger-originated life insurance* would mean “an act, practice or arrangement to initiate a life insurance policy for the benefit of a third party investor who, at the time of policy origination, has no insurable interest in the insured under KSA 40-450 and amendments thereto. Stranger-originated life insurance practices include, but are not limited to, cases in which life insurance is purchased with resources or guarantees from or through a person or entity who, at the time of the policy inception, could not lawfully initiate the policy, and where, at the time of the policy inception, there is an arrangement or agreement to directly or indirectly transfer the ownership of the policy or the policy benefits, or both, to a third party. Any trust that is created to give the appearance of insurable interest, and is used to initiate one or more policies for investors,

*Supplemental notes are prepared by the Legislative Research Department and do not express legislative intent. The supplemental note and fiscal note for this bill may be accessed on the Internet at <http://www.kslegislature.org>

violates KSA 40-450, and amendments thereto, and the prohibition against wagering on human life.” (Exclusions are listed below, with additional definitions created in the bill).

Under existing law, a *viator* is defined as an owner of a life insurance policy or a certificate holder under a group policy who enters or seeks to enter into a viatical settlement contract. A *viatical settlement contract* is the agreement between the viator and the viatical settlement provider (person who enters into or effectuates a viatical settlement contract) establishing the terms under which compensation will be paid to the viator in return for the viator’s assignment of the death benefit or ownership of the insurance policy or certificate of insurance. Other amendments to definitions amended by the bill are discussed below.

**New sections 1, 2, and 3 of the bill enact the provisions of KSA 2007 Supp. 40-5007, 40-5009, and 40-5012. The sections, which contained provisions that were subject to the Kansas Open Records Act, expired on July 1, 2007 and were redrafted. New sections 1 and 2 are unchanged, with the exception of the update of the expiration date; amendments were made in New Section 3 to the former provisions of KSA 40-5012 and have been noted.*

Examination (New Section 1)*

The bill would reinstate prior law (KSA 2007 Supp. 40-5007) to allow the Insurance Commissioner to conduct an examination under the Act as often as the Commissioner deems appropriate. The Commissioner also would be permitted to examine or investigate the business of any person as is necessary or material to the examination of the license. The bill also would provide examination requirements for foreign licensees. Additionally, all persons licensed by the Act would be required to retain and maintain copies of specified documents for five year.

The bill also would require the Commissioner to issue an

examination warrant when it is determined that an examination should be conducted. The Commissioner also could employ other guidelines and procedures as deemed appropriate. The Commissioner also would be granted the power to issue subpoenas and those individual failing to comply with examination requirements would be subject to suspension, revocation or refusal of any license.

Additionally, the bill would create requirements for examination reports, including the content, filing and receipt, and if determined to be appropriate, the regulatory actions the Commissioner may take. The reports and all materials associated with the course of examination would be considered confidential by law and not subject to the provisions of the Kansas Open Records Act, or of subpoena, and could not be used as evidence in any private civil action. The bill also includes similar confidentiality provisions for documents and other information in the possession or control of the National Association of Insurance Commissioners (NAIC). The Commissioner would be permitted to share and receive documents or other materials with other state, federal and international regulatory agencies, with the NAIC and its affiliates, and with law enforcement authorities provided the recipient agrees to maintain the confidentiality and privileged status of the document or other communication. The confidentiality provisions of the Act would expire on July 1, 2013, unless the Legislature acts to reenact those provisions.

The bill also contains provisions for conflict of interest of the examiners, retaining actuaries, fees and procedures for examination, liability, and civil cause of action and libel or other tort. Finally, the Commissioner would be permitted under the bill to investigate suspected fraudulent viatical settlement acts and persons engaged in the business of viatical settlements. The provisions of this section are to be part of the Viatical Settlements Act of 2002.

Viatical Settlement Contracts (New Section 2)*

Submission of documents. The bill would reinstate prior law (KSA 2007 Supp. 40-5009) to require that a viatical settlement provider entering into a viatical settlement is to first obtain:

- If the viator is insured, a written statement from a licensed attending physician that the viator is of sound mind and under no constraint or undue influence to enter into the contract; and
- A document in which the insured (policyholder) consents to the release of his or her medical records to a viatical settlement provider, viatical settlement broker and the insurance company that issued the individual's life insurance policy.

Other document requirements are contained in the Act and would expire July 1, 2013, unless the Legislature acts to reenact such provisions. Among the requirements, the viatical settlement provider (within 20 days after the viator executes documents to transfer any rights under an insurance policy or within 20 days of entering any agreement to viaticate the policy) would be required to give written notice to the insurer that issued the policy that the policy has or will become a viaticated policy. The documents to be submitted with the notice would include the medical release for the insured's medical records, a copy of the viator's application for the viatical settlement contract, the written notice, and a request for verification of coverage to the insurers that issued the life policy that is the subject of the viatical transaction. The time frame for the response of the insurer is outlined in the Act.

Additionally, prior to or at the time of execution of the contract, the viatical settlement provider would be required to obtain a witnessed document in which the viator consents to the contract, represents that the viator has a full and complete understanding of the viatical settlement contract, that the viator has a full and complete understanding of the benefits of the life insurance policy, acknowledges that the viator is entering into

the contract freely and voluntarily and, for persons with a terminal or chronic illness, acknowledges that the policyholder has a terminal or chronic illness or condition and that the illness or condition was diagnosed after the life insurance policy was issued.

The medical information solicited or obtained by a licensee would be subject to the applicable provisions of state law relating to the confidentiality of medical information. These document provisions would expire July 1, 2013, unless the Legislature acts to reenact such provisions.

Right to Rescind. The bill also would require that all viatical settlement contracts entered into in Kansas provide the viator with an unconditional right to rescind the contract for at least 15 calendar days from the receipt of the viatical settlement proceeds.

Change of Ownership. The viatical settlement provider would be required to instruct the viator to send the executed documents necessary to effect the change in ownership, assignment, or change in beneficiary directly to the independent escrow agent. Upon payment of the settlement proceeds into the escrow account, the agent is to deliver the forms to the provider or related provider trust. Upon receipt of a properly completed transfer of ownership or similar arrangement, the escrow agent is to pay the settlement proceeds to the viator. If the contract is not considered within the time outlined in law, then the contract could be rendered voidable by the viator.

The bill also addresses contacts made with the insured for the purpose of determining the health status of the insured. The contacts would be required to be made only by the viatical settlement provider or the viatical settlement broker and would be limited to once every three months for insureds with a life expectancy of more than one year and to no more than once per month for insureds with a life expectancy of one year or less. The provisions of this section are to be part of the Viatical Settlements Act of 2002.

Fraudulent Viatical Settlement Acts (New Section 3)

The bill would reinstate prior law (KSA 2007 Supp. 40-5007), with some amendments, and also would prohibit persons from:

- Committing a fraudulent viatical settlement act; knowingly or intentionally interfering with the enforcement of this Act or any investigation of suspected or actual violations of this Act;
- Knowingly or intentionally permitting any person convicted of a felony involving dishonesty or breach of trust from participating in the business of viatical settlements;
- Issuing, soliciting, marketing or otherwise promoting the purchase of an insurance policy for the sole purpose of or with the primary emphasis on settling the policy (the terms, “sole” and primary emphasis” amend the reinstated language);
- Employing any device, scheme or artifice in violation of KSA 40-450 (insurable interest, life insurance) in the solicitation, application or issuance of a life insurance policy; and
- Receiving any proceeds, fees or other consideration from the policy or owner of the policy that are in addition to the amounts required to pay the principal, interest and costs or expenses incurred by the lender or borrower related to policy premiums paid under the premium financing agreement (new language).

The viatical settlements would be required to contain the following statement (or a substantially similar statement): “Any person who knowingly presents false information in an application for insurance or viatical settlement contract is guilty of a crime and may be subject to fines and confinement in prison.”

Persons in the viatical settlement business and any other person having any knowledge or reasonable belief that a fraudulent act is being, will be or has been committed, would be required to provide such information to the Commissioner. No civil liability could be imposed on, nor a cause of action arise from, a person's furnishing of information to the Commissioner; employees of the Commissioner; federal, state or local law enforcement or regulatory officials; any person involved in the prevention and detection of fraudulent viatical settlement acts; the NAIC; the National Association of Securities Dealers; the North American Securities Administrators Association or their employees or other representatives, and the life insurer that issued the policy covering the life of the insured. Further provisions would address statements made with actual malice and the awarding of attorney fees and costs in a civil cause of action.

Under the Act, the Commissioner would be allowed to release documents and evidence obtained in an investigation of suspected or actual fraudulent viatical settlement acts in specified circumstances. These document provisions would expire July 1, 2013, unless the Legislature acts to reenact the provisions.

Antifraud initiatives. The bill also would specify that the Act would not preempt the authority or relieve the duty of other law enforcement or regulatory agencies to investigate, examine and prosecute suspected violations of law. Viatical settlement providers and brokers would be required to have antifraud initiatives in place that are reasonably calculated to detect, prosecute, and prevent fraudulent viatical settlement acts. The Act details the requirements for the initiatives, which the Commissioner is permitted to order modifications to, including fraud investigators and an antifraud plan. Antifraud plans submitted to the Commissioner would be privileged and confidential and would not be a public record, nor subject to discovery or subpoena in a civil or criminal action.

Naming of the Act (Section 4)

The bill would make the first three sections of the bill part of the Act.

Definitions (Section 5)

In addition to adding the definition for stranger-originated life insurance described above, the bill would amend certain definitions under the Act.

“Fraudulent Viatical Settlement Act.” Amendments to this the definition for this term would add two activities or acts:

- Stranger-originated life insurance, and
- Failing to disclose, when requested by an insurer, that the person to be insured has undergone a life expectancy evaluation by any party other than the insurer in connection with the policy’s issuance.

“Viatical Settlement Contract.” The bill would significantly amend the definition in current law. The new definition would include three types of arrangements:

- A written agreement between a viator and a viatical settlement provider that includes the following provisions:
 - The agreement would establish the terms under which compensation or anything of value is being paid or will be paid;
 - The amount to be paid would be less than the expected death benefits of the policy and more than the cash surrender value at the time of application for such a contract; and
 - The viator would be paid in return for the viator’s present or future assignment of the death benefit or

ownership of any portion of the insurance policy or certificate of insurance.

- The transfer of compensation or value of ownership into a trust or other entity, if that entity was formed or used for the principal purpose of acquiring one or more life insurance contracts.
- A written agreement for a loan or other lending transaction, secured primarily by an individual or group life insurance policy, or a loan made on or before the date of issuance to finance the premium of a life insurance policy if there is any agreement as of the date of issuance that the viator will later receive a viatical settlement value for or sell the policy.

Exceptions to the definition of "Viatical Settlement Contract". The bill further would include exceptions that would apply to both the definition of "stranger-originated life insurance" and "viatical settlement contract," so that neither definition would include the following:

- A policy loan by a life insurance company pursuant to the terms of the policy or accelerated death provisions contained in the policy, whether issued with the original policy or as a rider.
- Loan proceeds that are used solely to pay either premiums for the policy or any costs or expenses incurred by the lender or borrower in connection with the financing.
- A premium finance loan or any loan made by a bank or other licensed financial institution.
- A collateral assignment of a life insurance policy by a viator.
- A loan made by a lender that does not violate the Kansas Insurance Premium Finance Company Act, unless the premium finance loan meets the criteria described for a loan under a viatical settlement contract.
- An agreement where all parties are:
 - closely related to the insured by blood or law; or

- have a lawful substantial economic interest in the continued life, health and bodily safety of the person insured, or are trusts established primarily for the benefit of such parties.
- Any designation, consent or agreement by an insured who is an employee in connection with the purchase by the employer, or trust established by the employer, of life insurance on the life of the employee.
- A *bona fide* business succession planning arrangement.
- An agreement entered into by a service recipient, or a trust established by the service provider who performs significant services for the service recipient's trade or business.
- Any other contract, transaction, or arrangement exempted from the definition by the Commissioner.

The bill also would clarify that a "viator" would not include a qualified institutional buyer as such term is defined in rule 144A of the Federal Securities Act of 1933.

Filing of Annual Statement – Requirements for Certain Policies (Section 6)

The bill would create a new requirement under the Act governing the filing of annual statements with the Insurance Commissioner. For policies settled within five years of the policy's date of issue, the annual statement would be required to specify the total number, aggregate face amount and life settlement proceeds of policies settled during the immediately preceding calendar year, together with a break down of the information by policy issue year. The information would be limited to transactions where the insured is a Kansas resident and would not include individual transaction data that could be used to identify the policy owner or the insured.

Viatical Settlement Applications; Broker Disclosures (Section 7)

The bill would amend the information to be disclosed to the viator to include a viatical settlement broker that represents exclusively the viator and not the insurer or the viatical settlement provider. Furthermore the viatical settlement broker owes a fiduciary duty to the viator including the duty to act according to the viator's instructions and in the best interest of the viator.

Insurance Carrier Inquiry. In addition to other questions an insurance carrier may lawfully pose to a life insurance applicant, the carrier would be permitted to inquire in the insurance application whether the proposed owner intends to pay premiums with the assistance of financing from a lender that will use the policy as collateral. If the loan provides funds which can be used for a purpose other than paying for the premiums, costs, and expenses associated with obtaining and maintaining the life insurance policy and loan, the application would be rejected as a violation of the Act.

If the financing is not in violation of the Act, the insurance carrier would be allowed to make certain disclosures on either the application or any amendment, including:

- “If you have entered into a loan agreement where the policy is used as collateral, and the policy does change ownership at some point in the future in satisfaction of the loan, the following may be true:
 - A change of ownership could lead to a stranger owning an interest in the insured's life.”

The disclosures also would include the effect a change of ownership could have on an individual's future life insurance and coverage limitations, the effects of changes in health status, and tax consequences.

Among the certifications that could be made by the applicant or the insured would be “I have not entered into any agreement or arrangement providing for the future sale of this life insurance policy...and the borrower has an insurable interest in the insured.”

**Viatical Settlement Contracts; Two-Year Prohibition
(Section 8)**

The bill also would clarify the two-year prohibition in existing law for the settling of viatical settlement contracts to specify that no person at any time prior to, at the time of, the application for or issuance of policy, or during a two-year period (begins with the date of issuance) shall enter into a viatical settlement regardless of the date compensation is to be provided and regardless of the date of the assignment, transfer, sale, devise, bequest or surrender of the policy is to occur. Amendments also would be made to existing criteria for when the prohibition would not apply and “the beneficiary of the policy is a family member of the viator and the beneficiary dies” would be added to this list. The ability for an insurer to contest the validity of any policy is stated in the provision applying to the independent evidence submitted when an insurer seeks to verify coverage.

Background

The substitute bill was recommended by the Senate Committee on Financial Institutions and Insurance. The substitute bill incorporates provisions of SB 601, as introduced, and SB 624, a bill requested by the Kansas Insurance Department, and further amendments proposed by the parties involved, including additional language from the National Conference of Insurance Legislators’ Life Settlements Model Act. A subcommittee was appointed to study some of the proposed amendments. SB 601 was requested for Committee introduction by Coventry. Proponents of SB 601, as introduced, included representatives of the Life Settlement Institute. Proponents of SB 624 included the American Council of Life Insurers.

The original bill, HB 2110, would have amended current law to allow Health Maintenance Organizations (HMOs) to unite, merge, or consolidate with any other company or companies engaged in like business, provided certain conditions are met. These provisions were enacted in 2007 HB 2112.

No fiscal note was available for the substitute bill.