

# SENATE BILL REPORT

## SB 5195

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As Reported by Senate Committee On:  
Financial Institutions, Housing & Insurance, February 10, 2009

**Title:** An act relating to adopting the life settlements model act.

**Brief Description:** Adopting the life settlements model act.

**Sponsors:** Senators Berkey, Swecker, Kauffman, Hobbs, King, Marr, Haugen, Franklin, Parlette, Schoesler and Shin.

**Brief History:**

**Committee Activity:** Financial Institutions, Housing & Insurance: 1/28/09, 2/03/09, 2/10/09 [DPS].

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### SENATE COMMITTEE ON FINANCIAL INSTITUTIONS, HOUSING & INSURANCE

**Majority Report:** That Substitute Senate Bill No. 5195 be substituted therefor, and the substitute bill do pass.

Signed by Senators Berkey, Chair; Hobbs, Vice Chair; Benton, Ranking Minority Member; Franklin, McDermott, Parlette and Schoesler.

**Staff:** Diane Smith (786-7410)

**Background:** The term "life settlements" involves selling a life insurance policy that is no longer wanted or needed to a third party, other than the insurance company that issued the policy. Typically, the seller receives more than the policy's cash surrender value but less than its net death benefit.

Generally, the purchasers of life insurance policies are institutions called "life settlement companies" or "life settlement providers." They may hold the policies until maturity, when the insured person dies, and collect the net death benefits. They may also resell the policies, or they may sell interests in multiple policies to hedge funds or other investors. The person selling his or her policy receives a lump sum payment. The amount of the lump sum varies depending on a range of factors including the person's age, health, and terms and conditions of the life insurance policy. The purchaser agrees to pay any additional premiums required to keep the policy in effect and receives the death benefit when the insured person dies.

The Office of Insurance Commissioner (OIC) administers the Insurance Code. That code

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governs all insurance and insurance transactions; however, there is no specific regulatory authority for the OIC to regulate the business of life settlements.

**Summary of Bill (Recommended Substitute):** A life settlement contract is a written agreement between the policy owner and the third party, called the provider, that pays the owner less than the death benefit of the insurance policy in return for the policy owner's transfer of the death benefit to the provider. The minimum value of a life settlement contract must be greater than the cash surrender value of the policy or accelerated death benefit available at the time of application for the life settlement contract.

Initiating a life insurance policy for the benefit of an investor who has no insurable interest in the insured is called stranger-originated life insurance. This is a prohibited practice and unlawful.

A system of licensing providers and brokers of life settlement contracts is established under the authority of the OIC. The fee for and term of the license are established by the OIC. The OIC must investigate each applicant to determine that the applicant meets the requirements for licensure, including the provision of an anti-fraud plan to the OIC; that the applicant is competent and trustworthy and intends to transact its business in good faith; has a good business reputation; and has the education or experience to be qualified to transact the life settlements business. Life settlement brokers must complete continuing education in life settlements in the amount of 15 hours every two years, unless the broker is a life insurance producer.

The OIC conducts examination of licensees with the contents of the investigation being confidential by law and privileged. The costs of the examination are borne by the licensee.

The OIC may revoke, suspend, or refuse to renew a license if the provider has entered into any life settlement contract that the OIC has not approved, among other reasons. Before it takes any of these actions, the OIC must conduct an administrative hearing.

No life settlement contract or form, including the disclosure form, may be used unless it is approved by the OIC for compliance with general rules, advertising requirements, and disclosure requirements, among other requirements. The OIC must approve a document calculated to appraise the consumer of his or her rights as an owner of a life insurance policy. This disclosure must be included as part of the notice insurance companies must send to owners of its policies when owners become 60 years old, or older, and certain events critical to the continuation of the policy occur, such as the lapse of the policy.

Policies settled within five years of issuance must be reported to the OIC in an annual statement. Providers who willfully fail to file this annual statement are subject to penalties of up to \$250 per day of delay, not to exceed \$25,000 in the aggregate for each failure.

Provisions protect the insured's identity and financial and medical information.

With exceptions, entering into a life settlement contract within two years of the date of issuance of the life insurance policy is prohibited. Before executing a life settlement contract, those having a terminal illness must acknowledge that the illness was diagnosed after the life

insurance policy was issued. A terminal illness is one in which death is expected within two years.

Advertising about life settlement contracts must be filed with the OIC. No advertising may expressly reference that the insurance is "free" for any period of time. Promoting the purchase of an insurance policy for the purpose of settling the policy is unlawful. A loan, secured by an interest in the life insurance policy the premiums of which policy the loan is designed to finance, is unlawful if the proceeds are in addition to the amount required to pay the principal, interest, and service charges of the policy's premiums. If the loan provides funds which can be used for purposes other than paying the premiums of the life insurance policy and the loan itself, the application must be rejected.

A disclosure document from the provider or broker to the owner must contain specified language, be a separate page, be signed by both the owner and provider or broker, and be given to the owner no later than the date of application. Another disclosure from the broker to the owner and the provider, containing specified language, must be given to the owner and provider no later than the date the contract is signed by all parties.

The OIC has rulemaking authority. The laws of the state that apply to the owner take precedence if there is a conflict with the laws of the state of the purchaser.

**EFFECT OF CHANGES MADE BY FINANCIAL INSTITUTIONS, HOUSING & INSURANCE COMMITTEE (Recommended Substitute):** The proposed substitute bill includes technical amendments to conform the bill to the original negotiated understanding; clarify the application of the Washington Securities Act; and enable the seamless integration of the bill into the existing regulatory framework.

**Appropriation:** None.

**Fiscal Note:** Available.

[OFM requested ten-year cost projection pursuant to I-960.]

**Committee/Commission/Task Force Created:** No.

**Effective Date:** Ninety days after adjournment of session in which bill is passed.

**Staff Summary of Public Testimony on Original Bill:** PRO: The underpinning of life insurance is insurable interest. Investors waiting for the death of the insured is out of keeping with the purpose of life insurance. The definition of STOLI (Stranger Originated Life Insurance) in this bill is good. It is workable. It protects the interests of widows and orphans depending on the continued life of another for their support.

This is a very complicated, important, nuanced bill. The debate was vigorous. The Chair kept the sessions honest and fair. The core of the bill is the regulation of difficult, problematic practices. There is no cloak you can put over STOLI to make it right. The bill is a very strong curb on STOLI practices. Washington is in the forefront in preventing the Bear-Stearns, Lehman Brothers and Barney Madoff-like practices that arise from securitized debt based on fraud. Subject to making sure the language from the Insurance Commissioner

is in order, we support this bill. We are for this bill though section 11 gives us a bit of heartburn because of the potential expense. This is a solid bill. We would like to have seen some of it be different, but we committed to this process and as long as the Insurance Commissioner's amendments are only technical, we support this bill. This is important and valuable protection legislation.

The disclosures to consumers of the potential for unforeseen consequences of settling a life insurance policy are very important. The inclusion of documents pre-existing and independent of any fraud within the non-discoverable and confidential category established by section 15(4) and (5) could cause difficulties to claimants. Section 20(3) causes a concern because the public policy of this exception to the disclosure of public records is not evident. Any exceptions to the Public Records Act should be very carefully considered.

The Office of Insurance Commissioner has purely technical amendments so that the bill will integrate seamlessly with the existing regulatory structure.

**Persons Testifying:** PRO: Mel Sorensen, National Association of Insurance & Financial Advisors; John Mangan, American Council of Life Insurers; Jeffrey Laurence, Symetra; Carrie Tellefson, Coventry; Leroy Shannon, Washington State Association of Justice; Mary Clogston, Jim Tompkins, OIC.