REGULATING THE SECONDARY MARKET FOR LIFE INSURANCE: PROMOTING CONSISTENCY TO MAXIMIZE UTILITY

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INTRODUCTION

> "A contract of insurance upon a life in which the insured has no interest is a pure wager that gives the insured a sinister counter interest in having the life come to an end."[1]

The secondary market for life insurance policies, more commonly known as the viatical settlement or life settlement industry, involves the transaction of a life insurance policy from the policyholder or beneficiary to an investor, typically for monetary consideration.[2] This industry originated to meet the demands of policyholders wishing to liquidate their policies for a variety of reasons.[3] As the market developed, industry regulation played a vital role in protecting the policyholders, the array of players involved on the

* Managing Editor, *Rutgers Law Review*. J.D. candidate, Rutgers University School of Law–Newark, 2010; B.A., Economics, Vanderbilt University, 2004. The author wishes to thank his family and friends for their unending support, the *Rutgers Law Review* Editors and Staff for their incredible diligence, and the faculty at Rutgers School of Law–Newark for creating an environment in which thinking is the greatest commodity.

1. Grigsby v. Russell, 222 U.S. 149, 154 (1911). In writing the opinion for the Supreme Court, Justice Holmes declared that while the sale of a valid life insurance policy to a purchaser with no insurable interest in the policyholder's life conforms with the public policy of giving "life policies the ordinary characteristics of property," it is against the public policy of wagering on life to allow a party to name oneself as the beneficiary of a life insurance policy *initiated* on behalf of the life of a person in whom the beneficiary has no insurable interest. *Id.* at 156.

2. Individual Benefits, Inc., Viatical Settlements and Life Settlements, http://www.viatical.com/index.htm (last visited Mar. 26, 2010).

3. *See* New York State Ins. Dep't, Life Insurance – Top Ten Questions: Life Settlements, http://www.ins.state.ny.us/que_top10/que_life_set.htm (last visited Mar. 26, 2010) (listing seven potential reasons why one might consider selling his life insurance policy); *see also* Steven Arenson & Robert G. Miller, *Consider Life Settlements as an Option for Divesting Life Policies*, NAT'L UNDERWRITER LIFE & HEALTH-FIN. SERVS. EDITION, July 1, 2003, at 8. Policyholders have decided to liquidate their policies for a number of reasons including: (1) to meet financial constraints, (2) because they outlived individuals whom they named as the policy's beneficiaries, and (3) to simply obtain some financial benefit from property that would otherwise not appreciate during their lifetime.

acquiring end of transactions, and the insurance companies which issued the policies.[4]

In recent years, as the secondary market for life insurance has become more inhabited by parties seeking to purchase policies, investors have turned to the practice of stranger-originated life insurance to broaden the market.[5] In this practice, individuals initiate life insurance policies with the intention of selling the beneficiary rights to a third party investor.[6] Interpreting stranger-originated life insurance policies as wagers on life, the two leading organizations in favor of insurance regulation, the National Conference of Insurance Legislators (NCOIL) and the National Association of Insurance Commissioners (NAIC), have deemed the practice illegal and recommended new regulation to the states to prohibit such policies.[7]

This Note takes a journey through the secondary market for life insurance, examining its foundation and hashing out the true policy behind its proposed regulation to identify the ideal set of standards and conformities that should be adopted by the states in order to ensure a fair market for every player involved in transactions of life insurance policies. The first part of this Note provides information regarding the history of the secondary market for life insurance, as well as a comprehensive explanation of the industry. The second part of this Note assesses regulation in the secondary market for life insurance, analyzing the policy and reasoning behind specific regulatory requirements throughout the states. Finally, the third part of this Note identifies the ideal regulatory blend that would most effectively address public policy concerns and the interests of all parties involved in the secondary market for life insurance.

I. HISTORY AND BACKGROUND OF THE SECONDARY MARKET FOR LIFE INSURANCE

A. History

Documented as early as the eighteenth century, the secondary market for life insurance began as a natural consequence of the life insurance industry itself.[8] In England, the Royal Exchange was a

4. *See* MATTHEW BENDER & CO., THE LAW OF LIFE AND HEALTH INSURANCE § 5.06A[3][c][iv] (2008) [hereinafter LIFE AND HEALTH INSURANCE].

5. *See id.* § 2.07[9]. These policies are also known as "Investor Initiated Life Insurance ('IILI'), Investor Owned Life Insurance ('IOLI') or Stranger Owned Life Insurance ('SOLI')." *Id.*

6. *Id.*

7. *See* LIFE SETTLEMENTS MODEL ACT § 11 (Nat'l Conf. of Ins. Legislators 2007); VIATICAL SETTLEMENTS MODEL ACT 697-1 § 11 (Nat'l Ass'n of Ins. Comm'rs 2007).

8. *See generally* BURTON J. HENDRICK, THE STORY OF LIFE INSURANCE (1907)

venue for life insurance policyholders to auction their policies to speculators when they "found themselves unable to continue their payments."[9] Since life insurance companies had universally decided to refuse buying back issued policies, policyholders who could not afford to continue paying premiums were left with the option to either default, and subsequently let their policy lapse, or seek liquidation at an auction.[10] Seeing injustice in these limited options, Elizur Wright,[11] known to many as "the father of life insurance," endeavored to attach a cash-surrender value to life insurance policies, an amount reflective of the market value for the policy that the issuing life insurance company would be required to pay if policyholders default or seek to liquidate their policy.[12] As a result, Wright influenced the adoption of nonforfeiture laws in the United States that mandated this process, substantially diminishing the utility of a free secondary market for life insurance in America.[13]

Consequently, the secondary market for life insurance was essentially nonexistent in the United States for nearly a century and a half before it re-emerged in the form of viatical settlements.[14] In the 1980s and 1990s, the AIDS epidemic generated a number of life insurance policyholders who were overwhelmed by medical expenses

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(compiling articles from *McClure's Magazine* and exploring some early practices in the American life insurance industry, some of which were influenced by English customs).

9. *Id.* at 52.

10. *See* PHILIP G. WRIGHT & ELIZABETH Q. WRIGHT, ELIZUR WRIGHT: THE FATHER OF LIFE INSURANCE 221-23 (1937).

11. *Id.*

12. *See* HENDRICK, *supra* note 8, at 59.

13. *See* Erich W. Sippel & Alan H. Buerger, *A Free Market for Life Insurance*, CONTINGENCIES, Mar./Apr. 2002, at 17, 19, http://www.contingencies.org/marapr02/cover.pdf (arguing that Wright's reforms eliminated the "free market for the sale and purchase of life insurance policies"); William C. Koenig & Stephen H. Frankel, *Don't Forfeit Nonforfeiture*, 101 BEST'S REV. 119 (2000) (characterizing "the standard nonforfeiture law, [as] a pillar of life insurance practice since the 19th century, [that] remains a foundation of consumer protection [in the industry]"). Nonforfeiture laws effectively lulled the secondary market for life insurance because they created an alternative option for insured individuals to liquidate their life insurance policies "at rational, regulated prices." Sippel & Buerger, *supra*, at 18. Purchasing policies, as a result, became more speculative for investors because the nonforfeiture laws created a floor for the amount of capital that would be an attractive selling price for policyholders.

14. *See* Sippel & Buerger, *supra* note 13, at 1 (noting that while the secondary market had "dried up, . . . the potential was always present for the market to reappear if the regulated price (i.e., the cash surrender value) was below what others were willing to pay"); *see also* Allison Bell, *Life Settlement Firms Face Jumbled Regulatory Picture*, NAT'L UNDERWRITER LIFE & HEALTH-FIN. SERVS. EDITION, Sept. 20, 2004, at 40; Teresa R. Winer, *How Life Settlements Fit into the Impaired Risk Picture*, NAT'L UNDERWRITER LIFE & HEALTH-FIN. SERVS. EDITION, Oct. 28, 2003, at 16 (each describing the emergence of viatical settlements in the late 1980s).

and diagnosed with quite accurately predictable, short-term life expectancies.[15] Identifying opportunity amidst the gloomy circumstance, savvy investors began offering cash settlements to AIDS-stricken policyholders that were much greater than the amount available from a cash-surrender through the insurance company, but remained a sizeable discount from the plan's coverage.[16] Accordingly, the terminally ill were financially enabled to secure medical treatment while investors reaped monumental returns.[17] The viatical settlement industry boomed through most of the 1990s until advances in the medical treatment of HIV and AIDS lengthened life expectancies, therefore increasing the speculative nature of the market.[18]

Viatical settlements became even more of a risky venture for investors as a trend of fraudulent practices flooded the industry in the late 1990s.[19] In search of a more secure investment, players in the viatical settlement market began to shift their focus away from the terminally ill and toward healthy policyholders,[20] forming the life settlement industry.[21] Observing success and opportunity in this new market, financiers invested in life settlement companies causing the industry to surge across America.[22]

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15. *See* Sippel & Buerger, *supra* note 13, at 18 (describing the affect of the AIDS epidemic on life insurance markets); *see also* SEC v. Life Partners, Inc. & Pardo, 898 F. Supp. 14, 17 n.1 (D.D.C. 1995) (asserting that the "viatical settlement industry emerged during" the AIDS crisis).

16. *See* Sippel & Buerger, *supra* note 13, at 18 (recognizing that "the free market was reestablished when the market price for life insurance policies exceeded the regulated price"); *see also* Neil A. Doherty & Hal J. Singer, *The Benefits of a Secondary Market for Life Insurance Policies* 22 (The Wharton Financial Institutions Center, Working Paper No. 02-41, Oct. 14, 2002).

17. *See* Sippel & Buerger, *supra* note 13, at 18; Doherty & Singer, *supra* note 16, at 22.

18. David W. Dunlap, *AIDS Drugs Alter an Industry's Math*, N.Y. TIMES, July 30, 1996, at D1.

19. Anna D. Halechko, *Viatical Settlements: The Need for Regulation to Preserve the Benefit While Protecting the Ill and Elderly from Fraud*, 42 DUQ. L. REV. 803, 804-13 (2004); *see also* United States v. Jamieson, 427 F.3d 394, 400 (6th Cir. 2005) (providing an example of a fraudulent scheme); Daniel W. Gerber & Jeffrey L. Kingsley, *The Rapid Growth of the Life Insurance Industry*, 2008 EMERGING ISSUES 2955 (describing the "variety of fraudulent practices that arose" after life insurance policies were held not to be securities).

20. *See* LIFE AND HEALTH INSURANCE, *supra* note 4, § 5.06A(3)(a). Typically, life settlement investors would seek "wealthy, elderly persons with policies of a half-million dollars or more who no longer need their existing life insurance policies because of a change in family or financial circumstances." *Id.*

21. *See id.*; *see also* Sippel & Buerger, *supra* note 13, at 1-2.

22. *See* Miles Weiss, *Hedge Funds Buy Life Insurance Policies to Ply New Profit Path*, BLOOMBERG, Dec. 1, 2005, http://www.bloomberg.com/apps/news?pid=10000103&sid=aJRAaRvAH3KA&refer=us (providing one analyst's opinion that the

As the life settlement industry became saturated with institutional financiers willing to acquire existing life insurance policies, some investors looked for creative ways to extract benefit from the fruitful market.[23] Dodging centuries-old public policy against wagering on life,[24] these investors embarked on a mission to increase the supply of purchasable policies by offering monetary consideration[25] to uninsured individuals who would agree to initiate a life insurance policy with a commitment to subsequently sell it to the investors.[26] This practice, known as stranger-originated life insurance,[27] has come under heavy scrutiny because of its tendency to jeopardize the integrity of the life insurance industry, and resemble a blatant wager by the investor on the life of the insured.[28]

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industry "will be worth $160 billion sometime in the next several years"); *see also* Sippel & Buerger, *supra* note 13, at 2 (noting that "[d]uring the 1990s – a decade of sluggish growth in the life insurance industry – viatical and life settlements were among the few bright spots").

23. *See* LIFE AND HEALTH INSURANCE, *supra* note 4, § 2.07[9][a] (identifying these investors as being mainly hedge funds).

24. *See* Life Assurance Act, 1774, 14 Geo. 3, c. 48 (Eng.) (declaring that "no insurance shall be made by any person or persons . . . on the life of any person or persons . . . wherein the person or persons for whose use, benefit, or on whose account such policy or policies shall be made, shall have no interest"); *see also* Warnock v. Davis, 104 U.S. 775, 780 (1881) (recognizing "the general policy of the law respecting insurance, [which prohibits] gambling or speculative contracts upon the chances of human life").

25. *See* STEPHAN R. LEIMBERG, FLA. OFFICE OF INS. REG., STRANGER-OWNED LIFE INSURANCE (SOLI): WHAT (SMART) COUNSEL NEEDS TO KNOW 6 (2008), http://www.floir.com/pdf/NYU2008STOLIPAPERLeimberg.pdf. Consideration, in these cases, typically comes in the form of non-recourse loans, secured by the value of the policy, which "are structured in such a way that the insured is almost invariably forced to transfer the policy to the lender-investors or sell it to a life settlement company to pay off the debt." *Id.*

26. *Id.* at 5-6. When non-recourse loans are offered to individuals to initiate a life insurance policy, the terms also usually require the loan to be repaid only after two years have elapsed, in order to evade the timeframe in which insurance companies may contest the transfer of the policy. Many times, the terms of the loan will include above market interest rates to ensure that its default, and subsequently the policy's transfer, is essentially inevitable. *See id.* at 6-7.

27. *See* LIFE AND HEALTH INSURANCE, *supra* note 4, § 2.07[9] (providing alternative labels for the practice of initiating life insurance for the benefit of a third party).

28. *See* Liam Pleven & Rachel Emma Silverman, *Investors Seek Profit in Strangers' Deaths*, WALL ST. J., May 2, 2006, at C1 (quoting one insurance executive who considered the practice of stranger-originated life insurance as "a perversion of what life insurance is about"). Insurance providers, concerned that the nature of life insurance is changing, are being faced with a peculiar financial dilemma. *Id.* "When they write policies, they often assume some will lapse and they won't have to pay claims against them. When investors buy these policies, that becomes less likely to happen, potentially putting insurers on the hook for bigger payouts." *Id.*; *see also* Liam Pleven & Rachel Emma Silverman, *Cashing In: An Insurance Man Builds a*

Currently, both states and federal regulators[29] across America continue to be challenged with the task of ensuring fairness in the secondary market for life insurance.[30] Many states have adopted legislation resembling model regulations proposed by the NCOIL and NAIC to achieve this goal, while others have elected to remain uninvolved in the industry, confident that a free market approach will less intrusively legitimize the industry.[31] The vast differences in approach to regulation today epitomize the long and lively history of the secondary market for life insurance, which has been the source of polarized debate since its inception.[32]

B. Background

To characterize the secondary market for life insurance as being complex would be an understatement. Thus, it is important to become familiar with the types of transactions, actors involved, procedures engaged, utility associated, and concerns surrounding the industry. Additionally, some industry information will provide a contextual understanding of the secondary market for life insurance.

1. Types of Secondary Transactions of Life Insurance

Three types of transactions for life insurance on the secondary market have emerged over the years, each possessing specific characteristics that play a vital role in their valuation.

a. Viatical Settlements

Rooted in the Latin term "viaticum," which means "a supply of money or other necessaries for a journey,"[33] viaticals or viatical settlements refer to written agreements between the owner of a life

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Lively Business in Death – As Life Settlements Boom, Banks, Regulators Circle, WALL ST. J., Nov. 26, 2007, at A1 [hereinafter *Cashing In*] (asserting that insurers are among the biggest critics of the market in life insurance policies).

29. *See* Michele Meyer McCarthy, Annotation, *Federal Regulation of Viatical Life Insurance Programs, Viatical Settlements, and Viatical Investments*, 1 A.L.R. FED. 2d 269 (2005) (detailing the status of federal regulations in the viatical market).

30. *See id.* (describing the approaches taken by federal regulators and the various federal circuits).

31. *See* Michele Meyer McCarthy, Annotation, *State Regulation of Viatical Life Insurance Programs, Viatical Settlements, and Viatical Investments*, 28 A.L.R. 6th 281 (2007); Thomson Reuters/West, *Viatical Settlements (Statutes)*, 0110 SURVEYS 40, Dec. 2009 (Westlaw) (illustrating the approach taken by states in regulating viatical settlements).

32. Brief and Argument for Plaintiff in Error at 7, Grigsby v. Russell, 222 U.S. 149 (No. 53) (1911) (identifying conflicting decisions regarding the sale of life insurance on a secondary market that gave "rise to two general rules, termed respectively by judges and text-writers: (a) [t]he 'prevailing' or 'majority' rule, holding such assignments valid, and (b) the 'minority' rule holding them void").

33. 12 OXFORD ENGLISH DICTIONARY 170 (1933).

insurance policy and a settlement provider where compensation, in an amount less than the policy's death benefits but greater than the policy's cash-surrender value or accelerated death benefit, is paid to the policy owner by the settlement provider in return for the "present or future assignment, transfer, sale, devise or bequest of the death benefit or ownership of any portion of the insurance policy or certificate of insurance."[34] Associated with the AIDS epidemic, the term "viatical" is commonly linked to settlements involving life insurance policies held by the terminally ill, individuals who have "an illness or sickness that can reasonably be expected to result in death in twenty-four (24) months or less."[35] As a result of the more immediate proximity of expected death, these policies typically result in higher settlements than those obtained from healthy individuals.[36]

b. Life Settlements

Life settlements, also known as "senior settlements" and "high net worth transactions," involve the same basic transaction as viatical settlements; existing life insurance policies are assigned, transferred, sold, devised or bequeathed from their owners to settlement providers for some form of compensation.[37] Customarily, life settlements represent transactions that involve life insurance policies held by healthy individuals who, for a number of reasons,[38] wish to liquidate the interest in their policy.[39] Since the life expectancies of healthy policy owners are more speculative and usually longer, these policies tend to yield lower settlement amounts than those offered to the terminally ill.[40]

c. Stranger-Originated Life Insurance

Also labeled "'investor initiated insurance' or 'IILI', 'stranger owned life insurance' or 'SOLI,' and 'investor owned life insurance' or 'IOLI'," the practice of stranger-originated life insurance, or STOLI, closely resembles its title.[41] It is "a practice or plan to initiate a life insurance policy for the benefit of a third party investor who, at the

34. VIATICAL SETTLEMENTS MODEL ACT 697-1 § 2N(1) (Nat'l Ass'n of Ins. Comm'rs 2007).

35. *Id.* § 2L; *see also* Doherty & Singer, *supra* note 16, at 3.

36. *See* Doherty & Singer, *supra* note 16, at 20-22 (describing the calculations made by investors in life settlements depending on the age and health of the policyholder).

37. LIFE SETTLEMENTS MODEL ACT § 2L (Nat'l Conf. of Ins. Legislators 2007).

38. *See supra* note 3 and accompanying text.

39. *See* Doherty & Singer, *supra* note 16, at 21; LIFE AND HEALTH INSURANCE, *supra* note 4, § 5.06A[3][a]; Sippel & Buerger, *supra* note 13, at 1-2.

40. *See* Doherty & Singer, *supra note* 16, at 21.

41. *See* LIFE AND HEALTH INSURANCE, *supra* note 4, § 5.06A[3][a] (2008).

time of policy origination, has no insurable interest in the insured."[42] Typically, investors will create a trust for individuals who initiate a life insurance policy, under the agreement to later transfer the policy to investors.[43] Stranger-originated life insurance involves varying forms of complex transferring techniques that are developed and implemented to avoid "insurable interest laws and the prohibition against wagering on life."[44]

2. Actors

The secondary market for life insurance involves a number of actors who play distinctive roles throughout junctures before, during, and after the transaction.[45] As the industry has become more widespread, greater complexity in the form of investment has led to increased functions and new roles.[46] Major players in the life settlement, viatical settlement, and stranger-originated life insurance markets include the insured,[47] owner,[48] broker,[49] provider,[50] investment agent,[51] purchaser,[52] financing entity,[53]

42. LIFE SETTLEMENTS MODEL ACT § 2Y (Nat'l Conf. of Ins. Legislators 2007).

43. *Id.*; *see supra* note 25 and accompanying text.

44. LIFE SETTLEMENTS MODEL ACT § 2Y (Nat'l Conf. of Ins. Legislators 2007).

45. *See* Eileen Shovlin, *Clearing Up Common Misconceptions About Life Settlements*, NAT'L UNDERWRITER LIFE & HEALTH-FIN. SERVS. ED., Dec. 10, 2001, at 22 (distinguishing the "front end" from the "back end" of a life settlement transaction); *see also* Sachin Kohli, *Pricing Death: Analyzing the Secondary Market for Life Insurance Policies and its Regulatory Environment*, 54 BUFF. L. REV. 279, 287-90 (2006) (describing how the typical life settlement transaction works).

46. *See* LIFE AND HEALTH INSURANCE, *supra* note 4, § 5.06A[3][c][ii] (listing the actors involved in a typical life settlement transaction).

47. "[T]he person covered under the policy being considered for sale in [the secondary market for life insurance]," is generally referred to as the 'insured.' LIFE SETTLEMENTS MODEL ACT § 2I (Nat'l Conf. of Ins. Legislators 2007).

48. Also known as the 'viator,' "the owner of a life insurance policy or a certificate holder under a group policy, with or without terminal illness, who enters or seeks to enter into [a settlement on the secondary market for the benefits of their life insurance policy]" is the 'owner.' *Id.* § 2N; *See* VIATICAL SETTLEMENTS MODEL ACT § 2T (Nat'l Ass'n of Ins. Comm'rs 2007).

49. The 'broker' of a transaction on the secondary market for life insurance is "a Person who, on behalf of an Owner [or viator] and for a fee, commission or other valuable consideration, offers or attempts to negotiate [the settlement] between an Owner [or viator] and [settlement] Providers." LIFE SETTLEMENTS MODEL ACT § 2B (Nat'l Conf. of Ins. Legislators 2007); *see* VIATICAL SETTLEMENTS MODEL ACT § 2M (Nat'l Ass'n of Ins. Comm'rs 2007).

50. The 'provider' is "a person, other than an Owner [or viator], who enters into or effectuates a [settlement on the secondary market for life insurance] with an Owner [or viator]." LIFE SETTLEMENTS MODEL ACT § 2S (Nat'l Conf. of Ins. Legislators 2007); *see* VIATICAL SETTLEMENTS MODEL ACT § 2P (Nat'l Ass'n of Ins. Comm'rs 2007).

51. The 'investment agent' is "a person who is an appointed or contracted agent of a licensed . . . provider who solicits or arranges the funding for the purchase of a viatical settlement [or life settlement] by a viatical settlement [or life settlement]

special purpose entity,[54] and life insurance producer.[55]

3. Procedure

The procedures employed in settlements for life insurance policies on the secondary market differ based on the type of settlement. Viatical and life settlements have tended to take the form of practices used in other secondary markets in financial service industries.[56] On the other hand, the processes engaged in stranger-originated life insurance have adapted to evade contestability for

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purchaser and who is acting on behalf of a viatical settlement [or life settlement] provider." VIATICAL SETTLEMENTS MODEL ACT § 2O (Nat'l Ass'n of Ins. Comm'rs 2007).

52. "A Person who pays compensation or anything of value as consideration for a beneficial interest in a trust which is vested with, or for the assignment, transfer or sale of, an ownership or other interest in a life insurance policy or a certificate issued pursuant to a group life insurance policy which has been the subject of a [settlement on the secondary market for life insurance]," is known as the 'purchaser.' LIFE SETTLEMENTS MODEL ACT § 2U (Nat'l Conf. of Ins. Legislators 2007); *see* VIATICAL SETTLEMENTS MODEL ACT § 2R(1) (Nat'l Ass'n of Ins. Comm'rs 2007).

53. "[A]n underwriter, placement agent, lender, purchaser of securities, purchaser of a policy or certificate from a Provider, credit enhancer, or any entity that has a direct ownership in a policy or certificate that is the subject of a [settlement on the secondary market for life insurance] . . . whose principal activity related to the transaction is providing funds to effect the [settlement] or purchase one or more of the policies; and . . . who has an agreement in writing with one or more Providers to finance the acquisition of [settlements for life insurance on the secondary market]," is deemed the 'financing entity.' LIFE SETTLEMENTS MODEL ACT § 2F (Nat'l Conf. of Ins. Legislators 2007); *see* VIATICAL SETTLEMENTS MODEL ACT § 2E(1) (Nat'l Ass'n of Ins. Comm'rs 2007). Investors or purchasers who are non-accredited are not considered financing entities. VIATICAL SETTLEMENTS MODEL ACT § 2E(2) (Nat'l Ass'n of Ins. Comm'rs 2007); LIFE SETTLEMENTS MODEL ACT § 2F (Nat'l Conf. of Ins. Legislators 2007).

54. "A corporation, partnership, trust, limited liability company, or other legal entity formed solely to provide either directly or indirectly access to institutional capital markets . . . for a financing entity or provider; or . . . in connection with a transaction in which the securities in the special purpose entity are acquired by the owner or by a 'qualified institutional buyer'"; or "the securities pay a fixed rate of return commensurate with established asset-backed institutional capital markets," is defined a 'special purpose entity.' LIFE SETTLEMENTS MODEL ACT § 2X (Nat'l Conf. of Ins. Legislators 2007).

55. "Any person licensed . . . as a resident or nonresident insurance producer who has received qualification or authority for life insurance coverage or a life line of coverage pursuant" to the applicable statutes in each state in which they operate is considered a 'life insurance producer.' LIFE SETTLEMENTS MODEL ACT § 2K (Nat'l Conf. of Ins. Legislators 2007); *see* VIATICAL SETTLEMENTS MODEL ACT § 2G (Nat'l Ass'n of Ins. Comm'rs 2007).

56. *See* Doherty & Singer, *supra* note 16, at 15 (analogizing the secondary market for life insurance to the secondary markets for home mortgages, catastrophic risk insurance and NASDAQ-listed securities).

non-conformity with legislation and public policy.[57]

a. Viatical Settlements and Life Settlements

There are two sides to every viatical settlement and life settlement: (1) the financing and (2) the transaction.[58] The settlement hinges on work performed by the settlement provider who is active in both acquiring funds and fulfilling the transaction.[59]

The financing stage primarily involves seeking capital from independent or institutional investors.[60] As settlement providers have become more institutionalized, the investment opportunities offered to financiers more closely resemble investments available in other secondary markets for securities.[61] Thus, settlement providers have begun to pool acquired life insurance policies into structured securities, in which investors may subsequently acquire a stake.[62] The result: a more predictable and steady return for the investors, and greater availability of funds for the settlement providers.[63]

The actual transaction takes place when the settlement provider utilizes the financing provided by investors to acquire policies.[64] Typically, a life settlement or viatical settlement is initiated by the policy's owner through a broker.[65] When the ultimate decision to pursue a settlement is made by the policy's owner, his broker then submits the policy details, complete with information about the insured, to a number of settlement providers to solicit quotes.[66] If offers are made, subject to due diligence requirements and conformity to regulations, the policy's owner, with assistance from

57. *See, e.g.*, N.J. STAT. ANN. § 17B:30B-10 (West 2008) (requiring a "[t]wo-year period . . . between issuance of policy and viatical settlement"); *see also supra* notes 24-26 and accompanying text.

58. *See* Shovlin, *supra* note 45, at 22; *see also* Kohli, *supra* note 45, at 287-90.

59. *See* Kohli, *supra* note 45, at 284-85.

60. *See id.* at 287-88 (identifying the financing stage as the "back end" of the transaction).

61. *See* Doherty & Singer, *supra* note 16, at 15.

62. *See* EMMANUEL MODU, A.M. BEST CO., LIFE SETTLEMENT SECURITIZATION 3-5 (2009), http://www.ambest.com/debt/lifesettlement.pdf.

63. *See* Kohli, *supra* note 45, at 287-88. Investors purchasing a stake in securitized life settlements experience less volatility because their investment relies on a number of policies that, as an aggregate, vest at a more predictable rate. Securitization also allows for more funding in the life settlement industry because a larger range of investors are capable of purchasing, as well as willing to purchase, stakes, or fractions of the whole. Purchasing a single policy requires a hefty investment, and inevitably poses a high level of risk for the investor. *See id.*

64. *See id.* at 287-90; Shovlin, *supra* note 45, at 22-23.

65. Kohli, *supra* note 45, at 288.

66. *Id.* at 289.

his broker, will select the most favorable.[67] The amount of the accepted offer will then be provided to the policy's owner by the settlement provider as consideration for assignment of the policy's benefits to the provider.[68] As a result, the original policy owner, no longer holding an interest in the policy's benefits, becomes relieved of the duty to maintain premium payments on the policy, and the settlement provider becomes responsible for the premiums.[69]

b. Stranger-Originated Life Insurance

Criticized for its tendency to breach public policy against wagering on life and legislation requiring insurable interest in life insurance, the practice of stranger-originated life insurance is characteristically elusive in its many forms.[70]

4. Utility

The secondary market for life insurance delivers four essential benefits to a policyholder and society as a whole.[71] First, the industry provides an essential option to policyholders seeking to liquidate life insurance policies, abolishing the "monopsony" status historically held by insurance providers and establishing a fair market value for the policies.[72] Second, the existence of a secondary market for life insurance gives the trait of liquidity to an asset that has historically been viewed as being primarily illiquid, subsequently

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67. *See id.*

68. *See id.*

69. *Id.* at 289-90.

70. *See* LIFE AND HEALTH INSURANCE, *supra* note 4, § 5.06A(3)(a)-(c); Life Insurance Transactions, Op. Off. General Counsel No. 05-12-15 (N.Y. Ins. Dep't Dec. 19, 2005), http://www.ins.state.ny.us/ogco2005/rg051215.htm; *see also* LIFE SETTLEMENTS MODEL ACT, Drafting Note (Nat'l Conf of Ins. Legislators 2007) (targeting criticism at stranger-originated life insurance, declaring that a person with insurable interest cannot lend that insurable interest). The Court in *Grigsby v. Russell* held that "cases in which a person having an interest lends himself to one without any, as a cloak to what is, in its inception, a wager, have no similarity to those where an honest contract is sold in good faith." 222 U.S. 149, 156 (1911).

71. *See* DELOITTE CONSULTING LLP & UNIV. OF CONN., THE LIFE SETTLEMENTS MARKET: AN ACTUARIAL PERSPECTIVE ON CONSUMER ECONOMIC VALUE 3 (2005) [hereinafter DELOITTE & UCONN]; *see also* Doherty & Singer, *supra* note 16, at 15-30.

72. *See* Sippel & Buerger, *supra* note 13, at 1; WRIGHT & WRIGHT, *supra* note 10; DELOITTE & UCONN, *supra* note 71, at 3; Doherty & Singer, *supra* note 16, at 17, 24-25. Insurance providers, before the emergence of life settlement and viatical settlement providers, were the only buyers in the secondary market for life insurance. As a result, policyholders were at the mercy of surrendering unwanted or unaffordable policies to the insurers for amounts well below their market value. With the help of nonforfeiture laws, the materialization of an active secondary market for life insurance drove the purchase price for unwanted or unneeded life insurance policies up closer to a reasonable market value.

increasing the value of the primary market for life insurance.[73] Third, policyholders who experience a decline in health are provided the opportunity to sell their policy at fair market value, above the policy's cash-surrender value offered by the insurer.[74] Finally, an efficiently operating secondary market for life insurance provides lucrative investment opportunities to financiers, the prospect of higher commissions for insurance agents, and long-term value for insurance carriers.[75] Considered together, the benefits provided by the secondary market for life insurance reveal utility for "players" on every side of a settlement.

5. Concerns

A number of concerns, many of which are held by the incumbent insurance carriers, inhabit the secondary market for life insurance. Ranging from issues surrounding consumer protection,[76] to the industry's impact on the traditional role of life insurance in society,[77] to the potential for outright fraud,[78] these concerns have many critics passing negative judgment on the market.[79] As a result, many

73. Life insurance, becoming more easily and reasonably liquidable, is more valuable to consumers seeking to initiate a policy. *See* DELOITTE & UCONN, *supra* note 71, at 3; Doherty & Singer, *supra* note 16, at 27. Consequently, the existence of life and viatical settlements increases the demand for policies, subsequently raising "the value of a life insurance contract in the primary market as well." DELOITTE & UCONN, *supra* note 71, at 3.

74. *See* DELOITTE & UCONN, *supra* note 71, at 3; Doherty & Singer, *supra* note 16, at 17-19. Since the cash-surrender value of a policy is set at the time it is initiated, it does not account for sudden declines in health, which elevate the policy's market value by effectively shortening the span of time expected before the policy vests (not only will the policy vest sooner, but the amount of funds required by way of premiums are also reduced). Doherty & Singer, *supra* note 16, at 17-19. Thus, suddenly ill policyholders are granted the capability to receive fair market settlement funding for necessary medical treatment or other expenses.

75. *See* DELOITTE & UCONN, *supra* note 71, at 3; Doherty & Singer, *supra* note 16, at 29-30. The expansion of the secondary market for life insurance has created a niche for a number of investment institutions, an array of investment tools for many investors, and a span of employment positions for those entering the industry on the transacting end. While insurance carriers may experience short term cost increases, as the occurrence of lapsed policies decreases, the added value associated with insurance policies as a result of their increased liquidity will produce greater demand and higher premiums in the long term. Doherty & Singer, *supra* note 16, at 30.

76. *See* LIFE AND HEALTH INSURANCE, *supra* note 4, § 5.06A(3)(c)(iv)(A); *see also* Grigsby v. Russell, 222 U.S. 149, 154 (1911); Geoffrey Tomb, *Insurance Industry Rushes to Regulate Sale of Death Benefits*, MIAMI HERALD, Aug. 22, 1992, at 1B; Greg Steinmetz, *New Firms Buy Policies of AIDS Patients – Offering Cash for Insurance Is a Growing Business*, WALL ST. J., July 31, 1992, at A4C.

77. *See* LEIMBERG, *supra* note 25, at 11-12.

78. *See* GLORIA GRENING WOLK, VIATICAL & LIFE SETTLEMENTS: AN INVESTOR'S GUIDE 83 (2005).

79. *See, e.g.*, Miriam R. Albert, *Selling Death Short: The Regulatory and Policy*

opponents of the industry have urged legislators to adopt regulations to limit certain practices in the secondary market for life insurance.[80]

Concerns regarding the welfare of consumers have come from an array of interested parties; the insurance companies, public policy advocates, and financial advisors have all expressed an interest in protecting individuals wishing to fulfill a transaction in the secondary market for life insurance.[81] Insurers noted their concern that the entry of life settlements, viatical settlements, and stranger-originated life insurance transactions have increased and will continue to severely increase their costs, which will eventually be neutralized by higher premiums for consumers.[82] Other critics have identified the negative psychological effects that liquidating a policy will have on the relationship between the policyholder and the former beneficiaries of the policy from which they were divested.[83] Some financial advisors and attorneys have directed their concerns at the tax implications that result from policyholders settling their life insurance policies.[84] Finally, other opponents have indicated worries about the industry's potential for manipulation of elderly, ill, and misinformed policyholders,[85] as well as the general public policy concern of giving investors a "sinister counter interest in having the life [of the insured individual] come to an end."[86] Given the vulnerable position of many policyholders, in terms of their level of knowledge as it relates to their life insurance, consumer protection concerns weigh quite heavily on lawmakers contemplating whether to regulate or legitimize the secondary market for life insurance.[87]

Another string of concerns with the industry focuses on its tendency to tarnish the traditional role of life insurance that has

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Implications of Viatical Settlements, 61 ALB. L. REV. 1013, 1050-52 (1998).

80. *See id.*

81. *See infra* Part II.

82. *See* Doherty & Singer, *supra* note 16, at 22-23.

83. *See* LIFE AND HEALTH INSURANCE, *supra* note 4, § 5.06A(3)(a) (noting the possible psychological effects on both beneficiaries and purchasers of life insurance policies).

84. *See* Steinmetz, *supra* note 76, at A4C (pointing out that there is "potential for abuse" and that all consumers should not only be advised that their settlement will be taxed, but also that it may "disqualify them from Medicaid and other programs"); *see also* Jennifer Cody, *Insurance Regulators May Move to Curb Firms that Buy Policies from the Dying*, WALL ST. J., Dec. 3, 1993 (noting that viatical companies "may fail to warn policyholders that selling their policies could result in tax consequences").

85. *See Cashing In*, *supra* note 28 (discussing a lawsuit initiated by television host, Larry King, for his broker's failure to disclose certain information).

86. Grigsby v. Russell, 222 U.S. 149, 154 (1911).

87. *See* Constance M. Buerger, *The Secondary Market for Life Insurance Is Poised To Go Mainstream – Are You Ready?*, CAL. BROKER, Feb. 2004, at 22.

historically served many consumers.[88] Insurance providers are worried that the essence of a life insurance policy is changing from being a form of security, in the sense that it acts as a financial safety net for beneficiaries relying on the policyholder's support,[89] to a different form of security, in the sense that the policy takes the form of a liquidable and transferable asset or investment.[90] These critics fear that the primary life insurance industry's image will suffer, and its value to society will consequently be diminished by the secondary market.[91]

The final set of concerns about life settlements, viatical settlements and stranger-originated life insurance policies orbits around its vulnerability to fraudulent practices. Since the transaction for a life insurance policy involves protected information about the policyholders, the industry has been targeted by elaborate Ponzi schemes by criminals manipulating the minimal information available to share with potential investors.[92] Challengers to the secondary market have also associated increased occurrences of fraud by consumers, when initiating life insurance policies, to the rise of this industry.[93] Most critics consider the practice of stranger-originated life insurance policies to be fraudulent, in itself, and accordingly seek to eliminate the practice altogether by promoting legislation that stacks obstacles against it.[94] In sum, the existing concerns about the secondary market for life insurance present challenges for lawmakers seeking to protect consumers and promote a healthy environment for business in the undivided life insurance industry.

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88. *See* HOWARD M. ZARITSKY & STEPHAN R. LEIMBERG, TAX PLANNING WITH LIFE INSURANCE ¶ 1.01 (2d ed. 2008) (explaining that life insurance has been a source of funding for college expenses, mortgages, debts, and other financial needs).

89. *See id.*

90. *See* Albert, *supra* note 79, at 1018-20.

91. *See id.* at 1039.

92. *See* WOLK, *supra* note 78, at 83.

93. *See* Jacques Chambers, *Crackdown on Fraud Under Way in Viatical-Settlement Industry?*, POSITIVE LIVING (AIDS Project L.A., Los Angeles, Cal.), Dec. 1999, *available at* http://www.thebody.com/content/money/art32791.html (referencing AIDS victims providing false medical information in order to procure policies for settlements); Bradley K. Feldman & Robert M. Heinrich, *Legislation Designed to Eliminate Stranger-Originated Life Insurance Has Its Positives, Negatives*, MICH. LAW. WKLY., May 12, 2008, http://www.schechterwealth.com/pdfs/lawyerWeekly.pdf (referencing individuals providing false information regarding their contact, or intentions to settle, with life settlement providers at the time of their policy initiation, necessary to complete a stranger-originated life insurance policy).

94. *See* LEIMBERG, *supra* note 25, at 12.

6. Industry Information

Growth in the secondary market for life insurance has been consistent and substantial since it re-emerged onto the financial scene in the 1990s.[95] In the most recent study, analysts have estimated that "$12 billion of U.S. life insurance face values [were] settled in 2007."[96] This annual number nearly eclipses the entire industry's valuation of about $13 billion in March of 2005.[97] The rapid advancements in the market have been attributed to more widespread knowledge and acceptance of these transactions, as well as the surge of policies qualifying for a settlement that have resulted from the maturation of baby boomers.[98] Analysts expect this growth to continue through 2010,[99] and have projected that the industry will reach a valuation of $160 billion in the next several years.[100]

II. REGULATION IN THE SECONDARY MARKET FOR LIFE INSURANCE

The vast array of concerns[101] attributed to the secondary market for life insurance, along with "the widespread abuses which characterized the early years of the . . . industry," prompted efforts to regulate the various forms of life insurance settlements.[102] Early judicial holdings represented the initial step toward limiting certain practices in accordance with public policy.[103] As the secondary market for life insurance expanded across America, extensive lobbying efforts were directed at encouraging the implementation of statutory regulation in the industry.[104] Individual states, responsible for drafting independent insurance legislation, have taken different approaches to regulating the market.[105] The array of legislative

95. *See* Doherty & Singer, *supra* note 16, at 31-33.

96. *See* Press Release, Conning & Co., Strong Growth for Life Settlements in 2007 and Favorable Forecast Through 2010 (Oct. 8, 2008), http://www.prnewswire.com/cgi-bin/stories.pl?ACCT=PEFIN.story&STORY=/www/story/10-08-2008/0004900270.

97. *See* Weiss, *supra* note 22.

98. *See id.*

99. *See* Conning & Co., *supra* note 96.

100. Weiss, *supra* note 22; *see also* Heather Morton, *Money for Your Life (Insurance): Selling a Policy for Cash is Not as Unusual as You Might Think*, NAT'L CONF. OF STATE LEGISLATURES, Jan. 2009, http://www.thefreelibrary.com/-a0191765575 ("The life settlements industry has grown from $2 billion in 2001 to $16 billion in 2008.").

101. *See supra* Part I.B.5.

102. *See* LIFE AND HEALTH INSURANCE, *supra* note 4, § 5.06A(3)(c).

103. *See* Grigsby v. Russell, 222 U.S. 149, 155 (1911); Warnock v. Davis, 104 U.S. 775, 779 (1882); *see also* Life Assurance Act, 1774, 14 Geo. 3, c. 48 (Eng.) (regulating insurance upon lives).

104. *See* Halechko, *supra* note 19, at 819-23; Doherty & Singer, *supra* note 16, at 36-37 (discussing the self-interest of insurance firms in lobbying for regulation).

105. *See infra* Part II.C.

schemes across America not only exemplifies the mixed feelings about the industry, but also highlights the opportunity for a consistent legislative scheme that will most effectively promote fairness, efficiency and prosperity in the secondary market for life insurance.[106]

A. Judgments in Reaction to Early Public Policy Concerns

Since the eighteenth century, lawmakers have acknowledged the public policy concern against "wagering" on life.[107] While all life insurance policies may arguably be characterized as gambles that entail speculation around the length of an individual's life, legislators and judges alike have been more fearful of transferring a "sinister counter interest" in the life of the insured to a third party who does not have "an insurable interest . . . in having the life continue and so one that is opposed to crime."[108] Today, policymakers continue to respect this age old concern, and while the secondary market for life insurance has been widely accepted, recent pushback has been targeted at stranger-originated life insurance policies because they are "initiated" by individuals who do not have an insurable interest in the insured's life.[109]

B. NCOIL and NAIC Model Acts

Similar in their approach, the National Conference of Insurance Legislators (NCOIL) and the National Association of Insurance Commissioners (NAIC), the two leading organizations advocating regulation of the secondary market for life insurance in the United States, have over the years compiled model laws which they suggest and encourage states to consult and adopt in drafting their legislation.[110] These model acts target five general objectives: (1) to

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106. *See infra* Part II.C.

107. *See, e.g.*, Life Assurance Act, 1774, 14 Geo. 3, c.48, § 6 (Eng.).

108. Grigsby v. Russell, 222 U.S. 149, 154-55 (1911). *See generally* JONATHAN CURLING, JANUS WEATHERCOCK 229-65 (1938) (chronicling the criminal actions of Thomas Griffiths Wainewright, who encouraged Helen Abercromby, a woman in her twenties, to obtain excessive amounts of short-term life insurance and subsequently poisoned her in order to collect the proceeds); *see also* FREDERIC G. KITTON, THE MINOR WRITINGS OF CHARLES DICKENS 89-90 (1900); THOMAS DEQUINCEY, WORKS 250 (1890); Bell, *supra* note 14, at 40 (each providing examples of the social impact of Wainewright). *But see Grigsby*, 222 U.S. at 156 (1911) (noting that "the ground of the objection to life insurance without interest in the earlier English cases was *not the temptation to murder* but the fact that such wagers came to be regarded as a mischievous kind of gaming") (emphasis added).

109. *See* LIFE SETTLEMENTS MODEL ACT, Drafting Note (Nat'l Conf. of Ins. Legislators 2007) (claiming that stranger-originated life insurance arrangements "violate insurable interest laws and the prohibition against wagering on life").

110. *See, e.g.*, LIFE SETTLEMENTS MODEL ACT (Nat'l Conf. of Ins. Legislators 2007); VIATICAL SETTLEMENTS MODEL ACT (Nat'l Ass'n of Ins. Comm'rs 2007).

establish licensing requirements for 'brokers' or 'providers' in the secondary market for life insurance;[111] (2) to set procedural standards for transactions occurring in the industry;[112] (3) to prevent fraud from occurring against consumers, insurers and investors;[113] (4) to arrange penalties for actions not in compliance with the regulations;[114] and (5) to absolutely abolish stranger-originated life insurance arrangements from the market.[115] Adopted in 1993, and

111. *See* LIFE SETTLEMENTS MODEL ACT §§ 3-4 (Nat'l Conf. of Ins. Legislators 2007). Licensing requirements recommended by the NCOIL and NAIC are targeted at ensuring integrity in the industry and protection for consumers. The model acts compel potential providers and brokers to submit applications, along with a fee, to the state's Insurance Commissioner. *See id.* § 3(B). Licensed providers and brokers would be required to renew their licenses on a timeframe set by the state. *See id.* § 3(G). A number of additional provisions oblige providers and brokers to be subordinate to orders for information and other judgments by the Commissioner. *See id.* §§ 3-4.

112. *See id.* §§ 5-11. Procedural standards for transactions in the secondary market for life insurance dominate the majority of measures proposed by the NCOIL and NAIC. The model acts set specific contractual requirements, mandated by the Commissioner, as prerequisites to completing a settlement. *See id.* § 5. Advertising and solicitation techniques are also proposed to be regulated by the NCOIL and NAIC. *See id.* § 8. Finally, the model laws recommend that states mandate specific disclosures be made by providers and brokers to policyholders and insurers. *See id.* §§ 9-10.

113. *See id.* § 14. A specific set of standards, proposed in the NCOIL and NAIC's model acts, are designed to eliminate the existence of fraud in the secondary market for life insurance. These suggested requirements would compel "[a]ny person engaged in the business of life settlements" to report any knowledge of fraud in the industry to the Insurance Commissioner, providing "[i]mmunity from [l]iability" for those reporting the fraudulent behavior. *Id.* § 14(C), (D). The model acts suggest that strict confidentiality be granted to any reports, and subsequent investigation, of fraud. *Id.* § 14(E). Finally, the NCOIL and NAIC propose that states require providers and brokers to "have in place antifraud initiatives reasonably calculated to detect, prosecute and prevent" fraudulent settlements. *Id.* § 14(G).

114. *See id.* §§ 15-16. Penalties for actions not in conformity with the proposed regulations are included in the model acts to deter fraud and other unfair practices in the industry. *See id.* The NCOIL and NAIC propose that the Commissioner have the ability to issue injunctions, as well as cease and desist orders. *Id.* § 15. Willful violations of orders from the Commissioner would be subject to statutory damages. *See id.* § 15(C). Civil remedies for persons damaged by violations of the model acts, as well as civil penalties against violators are proposed by the NCOIL and NAIC. *See id.* § 15(B). The model acts also suggest imposing criminal liability for fraud in the secondary market for life insurance. *See id.* § 16.

115. *See id.* § 13. The most recent proposals, added to the model acts in 2007, highlight stranger-originated life insurance transactions as a matter of preventing violations of public policy against wagering on life. *See id.* The NCOIL and NAIC propose that states allow insurance companies to contest transactions of life insurance policies occurring within the first five years of the policy's inception. *See* LIFE SETTLEMENTS MODEL ACT 36 n.8 (Nat'l Conf. of Ins. Legislators, Proposed Official Draft 2007). This contestability period, increased from the previously recommended two years, would permit insurance companies to investigate transacted policies for the time at which providers and brokers became interested in the policy. *See id.* The

amended extensively in 1998, 2001 and 2007 "to address fraud, advertising and civil remedies . . . [as well as] the issue of Stranger Originated Life Insurance," the model laws have received varied responses and adoptions from the states.[116]

C. State Adoptions

A number of factors have influenced state legislators to enact regulations in the secondary market for life insurance. First, heightened criticism surrounding the industry, in response to predatory practices and the market's clear susceptibility to fraud, pressured many lawmakers to seek ways to protect consumers and investors.[117] Second, the industry's inherent complexity, resulting from the market's intimate ties with investment and insurance, exposed potential for confusion and a utility for certain mandates to streamline the practice.[118] Third, the commonplace imbalance of information and resources amongst players in the market has also created potential vulnerability amidst the practice of these transactions. [119] As a result, states have been confronted with a broad range of concerns that orbit the secondary market for life insurance, and many have decided to draft intricate statutory plans to specifically address these matters. [120]

Given the industry's expansive set of characteristics that reveal a potential need for regulation, along with simply a difference in approach to regulating, states have enacted legislation at quite a varying degree.[121] Twenty-seven states and Puerto Rico have enacted legislation to extensively regulate viatical settlements, life settlements and stranger-originated life insurance.[122] Fourteen

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model acts broadly define stranger-originated life insurance transactions, and specifically propose that they be outlawed by the states. *See* LIFE SETTLEMENTS MODEL ACT § 2(Y) (Nat'l Conf. of Ins. Legislators 2007).

116. MODEL LAWS, REGULATIONS AND GUIDELINES 29 (Nat'l Ass'n of Ins. Comm'rs 2008).

117. *Cf.* Halechko, *supra* note 19, at 808-13 (explaining the potential for fraud in the industry).

118. The industry, given its hybrid foundation in insurance and investment, is also "subject to a variety of federal regulations, including those involving securities law, insurance law, [ERISA], and criminal law." McCarthy, *supra* note 29, at 269.

119. *See* Kohli, *supra* note 45, at 316-17 (detailing the potential for pricing fraud, conflicts of interest, and the lack of sufficient disclosure regulations).

120. *See id.* at 302-05.

121. *See infra* text accompanying note 128.

122. Along with Puerto Rico, P.R. LAWS ANN. tit. 26, §§ 4221-4235 (2008), the states that have enacted extensive regulation include: Alaska, ALASKA ADMIN. CODE tit. 3, §§ 31.025, 31.300-.449 (2010); Arkansas, ARK. CODE ANN. §§ 23-81-801 to -818 (West 2009); Colorado, COLO. REV. STAT. ANN. §§ 10-7-601 to -620 (2006); Connecticut, 2008 Conn. Acts 08-175 (Reg. Sess.); Florida, FLA. STAT. ANN. §§ 626.991-.993 (West 2009); Georgia, GA. CODE. ANN. §§ 33-59-1 to -18 (West 2009); Hawaii, HAW. REV. STAT. §§

states have passed laws that broadly control the secondary market for life insurance, placing significant constraints on practices that would impair fair-dealing, emphasizing consumer and investor protection.[123] Only one state, Arizona, has confined its regulation of the industry to exclusively prohibit the practice of stranger-originated life insurance schemes.[124] Five states explicitly consider settlement transactions of life insurance policies to be securities and, as such, govern transactions through their respective state securities regulations.[125] Three states remain silent in their approach, enacting no laws that specifically address regulation in the secondary market for life insurance.[126] Finally, the District of Columbia has merely defined and authorized viatical settlements in the context of government employment.[127] This broad discrepancy in approach among the jurisdictions to regulation, or withholding regulation, is a

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431E-1 to -53 (2009); Indiana, 760 IND. ADMIN. CODE 1-61-1 to -12 (2009); Iowa, IOWA ADMIN. CODE r. 191-48.1 to .14 (2009); Kansas, KAN. STAT. ANN. §§ 40-5001 to -5015 (2009); Kentucky, 2008 Ky. Acts 32; Louisiana, LA. ADMIN. CODE tit. 37, §§ 3901-3917 (2008); Maine, ME. REV. STAT. ANN. tit. 24-A, §§ 6801-6819 (2009); Maryland, MD. CODE ANN., INS. §§ 8-601 to -611 (West 2010); Montana, MONT. CODE ANN. §§ 33-20-1301 to -1317 (2009); Nebraska, NEB. REV. STAT. ANN. §§ 44-1101 to -1117 (LexisNexis 2009); Nevada, NEV. REV. STAT. ANN. §§ 688C.010-.510 (West 2009); New Jersey, N.J. STAT. ANN. §§ 17B:30B-1 to -17 (West 2010); North Carolina, N.C. GEN. STAT. §§ 58-58-200 to -310 (2009); North Dakota, N.D. CENT. CODE §§ 26.1-33.3-01 to -16 (2009); Ohio, OHIO REV. CODE ANN. §§ 3916.01-.99 (Lexis Nexis 2009); Oklahoma, OKLA. STAT. tit. 36, §§ 4041-4052 (2009); Pennsylvania, 40 PA. STAT. ANN. §§ 626.1-.17 (West 2008); Tennessee, TENN. CODE ANN. §§ 56-50-101 to -111 (2009); Utah, UTAH CODE ANN. §§ 31A-36-101 to -119 (2005); Virginia, VA. CODE ANN. §§ 38.2-6000 to -6016 (2008); and West Virginia, W. VA. CODE §§ 33-13C-1 to -18 (2008).

123. States taking a broad, consumer-protection focused, approach to regulating include: California, CAL. INS. CODE §§ 10113.1-.2 (West 2008); Delaware, DEL. CODE ANN. tit. 18 §§ 7501-10 (2009); Illinois, 215 ILL. COMP. STAT. 158/1-/99 (2009); Massachusetts, MASS. ANN. LAWS ch. 175 §§ 212-223 (Lexis Nexis 2008); Michigan, MICH. COMP. LAWS SERV. §§ 550.521-.528 (LexisNexis 2006); Mississippi, MISS. CODE ANN. §§ 83-7-201 to -223 (West 2009); New Mexico, N.M. STAT. ANN. §§ 59A-20A-1 to -11 (West 2009); New York, N.Y. INS. LAW §§ 7801-7810 (McKinney 2010); Oregon, OR. REV. STAT. ANN. §§ 744.319-.358 (West 2007); Texas, TEX. INS. CODE ANN. §§ 1111.001-.053 (Vernon 2009); Vermont, VT. STAT. ANN. tit. 8, §§ 3826-3834 (2009); Washington, WASH. REV. CODE ANN. §§ 48.102.005-.901 (West 2008); and Wisconsin, WIS. STAT. ANN. § 632.68 (West 2009).

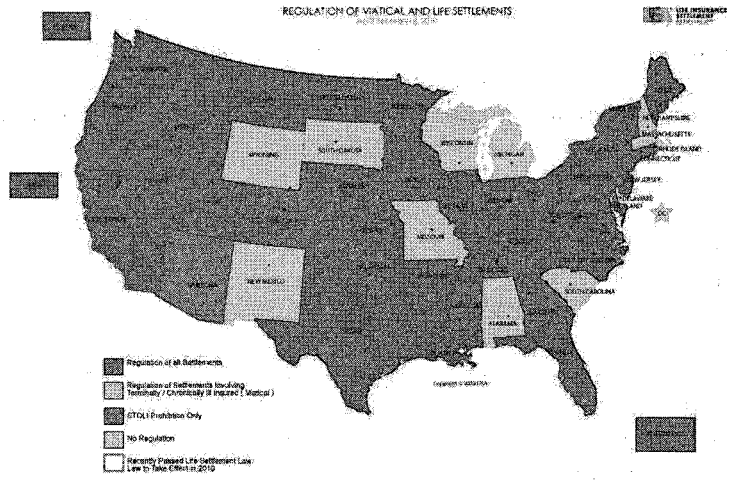
124. ARIZ. REV. STAT. ANN. § 20-443.02 (Supp. 2009).

125. States that defer regulation to their securities statutes include: Alabama, *see* ALABAMA SECS. COMM'N, POLICY STATEMENT ON VIATICAL SETTLEMENT CONTRACTS (May 27, 1999), *available at* http://www.thevoiceoftheindustry.com/files/alabama_admin_code_promulgated_securities_policy_posted_11_17_06.pdf; Idaho, IDAHO CODE ANN. § 30-14-102 (2008); Missouri, MO. REV. STAT. § 409.1-102 (2009); South Carolina, S.C. CODE ANN. § 35-1-102 (Supp. 2009); and South Dakota, S.D. CODIFIED LAWS § 47-31B-102 (2009).

126. States refraining from enacting legislation include: New Hampshire, Rhode Island and Wyoming.

127. D.C. CODE §§ 1-622.04 -.08 (2009).

testament to the varied societal impressions of, and the challenges faced by legislatures responsible for ensuring fairness in, the secondary market for life insurance.



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1. Extensive Regulation

The twenty-seven states[129] electing to extensively regulate life and viatical settlements have geared their legislative schemes closely to the model laws presented by the NAIC and NCOIL.[130] Consequently, these states have established licensing requirements and procedural standards, made targeted efforts to prevent fraud, set penalties for regulatory violations, and drafted laws to effectively prevent the practice of stranger-originated life insurance.[131]

These states have generally granted broad discretion to their respective Insurance Director or Commissioner for issuing licenses to settlement providers, brokers and representatives.[132] License applications must provide specific information about the individual applicant and be submitted with a fee before being reviewed by the Director or Commissioner.[133] Typically, the applicant must also provide a plan of operation, indicating the type of insurance plans he

128. Life Insurance Settlement Association, *Regulation of Viatical and Life Settlements*, Map, Feb. 12, 2010, http://www.lisassociation.org/vlsaamembers/legislative_maps/images/Reg-of-viatical-and-life-se.jpg.

129. *See supra* note 122.

130. Kohli, *supra* note 45, at 303-05.

131. *See* Albert, *supra* note 79, at 1026-27.

132. *See id.* at 1030.

133. *See id.*

or she will seek to transact and an overview of his business model, as well as an anti-fraud plan.[134] The statutes also require licensees to maintain a bond, usually in the amount of at least $200,000, to cover potential liability.[135] In these states, licenses are required to be renewed biennially, accompanied with a renewal fee, and at the discretion of the Director or Commissioner.[136] The license regulation also typically includes a list of grounds for disqualification, including making misrepresentations on applications, felony convictions, participating in fraud, expressing untrustworthiness and breach of contract, among others.[137] Aggregately, these provisions tightly restrict the number of settlement providers, brokers and representatives, with the ultimate goal of ensuring accountability and candor in the secondary market for life insurance. [138]

The procedural standards that are in place throughout states with extensive regulation focus heavily on leveling the imbalance of information and bargaining power between the parties involved in settlement negotiations.[139] Again granting considerable discretion to the Director or Commissioner, these states require all settlement contracts to be submitted for, and subsequently receive approval by, the Director or Commissioner.[140] To be approved, the contracts must include specific disclosures, generally targeted at leveling any imbalance of information that may exist between parties.[141] Usually, these states also require all settlements to be paid in a lump sum and

134. *See* ALASKA ADMIN. CODE tit. 3, § 31.300 (2010).

135. *See id.* § 31.315: Surety Bond Requirement.

136. *See id.* § § 31.340: License Renewal.

137. *See* Albert, *supra* note 79, at 1030.

138. *See id.*

139. *See, e.g.*, N.J. STAT. ANN. § 17B:30B-5 (West 2008) (requiring settlement contract forms to be approved by the Commissioner to ensure that they are not "unreasonable, contrary to the interest of the public, or otherwise misleading or unfair to the viator").

140. *Id.*

141. Required contract content and disclosures usually include statements indicating: the viator's right to rescind the settlement within fifteen days of receiving settlement proceeds, the viator's liability for any fraudulent representations, the provider's responsibility to provide the viator with copies of correspondence between the provider and the insurance company, as well as other circumstantial information relating to the transaction. *See, e.g.*, COLO. REV. STAT. § 10-7-608 (West 2010). Regulation, usually designed for consumer protection, also typically requires providers to inform viators about: alternatives to settling their policy, the tax implications of settling, the potential impact on the viator's status with Medicaid or other federal programs, the name of the escrow agent or trustee through whom the settlement proceeds will be transferred, confirmation that medical records will remain confidential, contact information for parties involved, and the process utilized in calculating compensation for the parties involved. *See, e.g.*, ALASKA ADMIN. CODE tit. 3, §§ 31.380 (2010).

through an escrow account within three days of filing all requisite paperwork. [142] Included in their procedural regulation, states that heavily regulate life and viatical settlements have imposed limitations on advertising practices undertaken by players in the industry.[143] Finally, legislation targeting the settlement procedure usually indicates specific practices that should be avoided to maintain fair competition in the market.[144] The ultimate goal surrounding procedural mandates tends to focus on guaranteeing fairness in the secondary market for life insurance; primarily, the states seeking to attain this goal have aligned regulation to promote transparency throughout the settlement process. [145]

To combat fraud in the industry, extensively regulated states have continued their trend of regulating settlement transactions from beginning to end. As a proactive measure, lawmakers in these states have required life and viatical settlement providers to draft and submit comprehensive fraud-prevention plans.[146] During the settlement process, these states compel providers to include verbiage in contracts that promotes fraud awareness. [147] Even after settling, providers in these states continue to be regulated as legislators have imposed strict reporting mandates. [148] Pursuant to this legislation, settlement providers are typically required to submit extensive reports to the Director or Commissioner each year, revealing detailed

142. *See, e.g.*, MASS. ANN. LAWS ch. 175, § 219(a)(7) (2008).

143. Aside from Director or Commissioner approval, advertising limitations usually include a concrete ban on: misleading information or omissions that would lead to deception; statements contrary to public interest; implying that interest charged on accelerated death benefits or policy loans are incorrect or improper; using "the words 'free,' 'no cost,' 'without cost,' 'no additional cost,' or 'at no extra cost'" unless the statements are factually true; using statistics without clearly providing the source; disparaging information about other players in the industry; and using trade names without identifying the individual providers behind the advertisement. *See, e.g.*, ALASKA ADMIN. CODE tit. 3, §§ 31.375 (2006).

144. Fair marketing provisions include: restrictions on paying finder's or referral fees; limitations on soliciting a medical practitioner to finance the settlement of one of his or her patient's policies; requiring a physical assessment of the viator, confirming he or she is of sound mind; providing a written notification of the transaction to the insurance company within twenty days of the settlement. *See, e.g.*, ALASKA ADMIN. CODE tit. 3, §§ 31. 390 (2006).

145. *See* MASS. ANN. LAWS ch. 175 § 219 (2008) (outlining procedures to ensure transparency).

146. Anti-fraud plans are usually required to include: "a description of procedures for detecting and investigating [fraud] . . . and procedures for resolving [misrepresentations on] applications;" "antifraud education and training of personnel;" and an outline of personnel who are in charge of policing fraud in the business. *See, e.g.*, ALASKA ADMIN. CODE tit. 3, §§ 31.405 (2006).

147. *See, e.g., id.* § 31.370(d)(5) (requiring a fraud warranty in every contract, in size ten font, bolded type).

148. *See, e.g., id.* § 31.360(1).

information about every settlement they have transacted, as well as every settlement that has vested, over the prior twelve months.[149] In sum, this legislation effectively seeks to seal the vulnerable voids throughout the industry that had historically been susceptible to fraudulent practices by providers and consumers alike.

Extensive regulatory schemes also typically present penalties for non-compliance with the statutory provisions. In these states, penalties typically range from administrative fines, to injunctions, to possible first-degree felony imprisonment of up to thirty years.[150] Legislation in these states also usually permits parties who have been damaged as a result of the acts of a person in violation of the pertaining statutes to bring a civil suit, seeking damages and attorney's fees from the alleged violator.[151] With such a stern stance on imposing punishment for violations, these states have clearly set forth to deter any activity in the secondary market for life insurance that may be detrimental to the industry's integrity.

The final aspect of the market that states with extensive legislation consistently target is the practice of stranger-originated life insurance. Most states do not specifically define and prohibit the practice, but rather impose a provision that voids all settlements that occur within the two-year period following the insurance policy's initiation.[152] Some extensively regulated states have taken recommendations from NAIC and NCOIL, adopting or revising statutes to void settlements occurring within five years of a policy's inception.[153] Other states have chosen to attack the practice of stranger-originated life insurance by simply and straightforwardly defining and prohibiting the practice.[154] Legislators intend, by enacting terms of settlement ineligibility, to construct barriers that essentially destroy the practice's lucrative nature through increasing the risk assumed by investors.[155]

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149. The regulation requires information, such as: the insured's life expectancy, the policy's death benefit, the proceeds paid, the premiums to be paid, the parties involved in the transaction, the type of policy, the contestability period remaining on the policy, whether the insured has been diagnosed with AIDS/HIV or other disease or condition, the manner of funding the settlement, etcetera. *See, e.g., id.* §§ 31.025-.449.

150. FLA. STAT. §§ 626.991-.99275 (2005).

151. *Id.* § 626.9927(3).

152. *See, e.g., id.* § 626.99287.

153. *See, e.g.*, OHIO REV. CODE ANN. § 3916.16(B) (West 2008).

154. *See, e.g.*, ARIZ. REV. STAT. ANN. § 20-443.02 (2006).

155. Typically, stranger-originated life insurance policies are financed by investors who provide the insured with a loan to initiate the insurance policy and pay its premiums. By enacting laws that prohibit policy transfers within two or five years from its inception, the investors risk the possibility that the insured will die during that period, in which case their investment would provide them with no return, essentially providing the insured with free insurance for two or five years, depending

Together, the extensive legislation in states that have chosen to intricately regulate the secondary market for life insurance aims to leave no space for practices that would be contrary to the public interest. In doing so, these states have essentially defined the practice of pursuing, negotiating, and transacting life and viatical settlements.[156] However, is this an efficient way to maximize the utility of the industry, while protecting the parties involved? Are public policy concerns the true motivation for these laws?

2. Consumer-Protection-Based Regulation

The fourteen states[157] that have elected to broadly regulate the secondary market for life insurance predominantly direct their legislation toward protecting consumers and securing the public interest. Most of these states specifically tailor their laws to preside over viatical settlements, defined as policies held by insureds who have "catastrophic or life-threatening illness[es] or condition[s]."[158] Like the states with extensive regulations, these states also have licensing, reporting and disclosure requirements that are aimed at ensuring fairness and accountability.[159] However, in addressing prohibited acts, rather than enumerating actions that would constitute statutory violations, the states imposing broad regulations have granted wide, and general, discretion to their Insurance Director or Commissioner to adopt rules, impose penalties and make licensing decisions that "he or she deems . . . reasonably necessary to protect the interests of the public."[160] The ultimate impact of this broad approach to regulating the industry tends to establish a watchful eye over transactions that involve consumers with hindered bargaining power or vulnerable circumstances.[161] But does this leave the door open for abuse amidst life settlement transactions that involve healthy individuals? Is too much discretion bestowed upon the Commissioner or Director to define what is in the best interests of the public?

3. Solely STOLI Regulation

As the only state to enact regulation in the secondary market for life insurance that solely targets stranger-originated life insurance transactions, Arizona has been motivated by the "prohibition against

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on the state's legislation.

156. *See, e.g.*, N.J. STAT. ANN. § 17B:30B-5 (West 2008) (explaining the procedure for life insurance transactions from negotiation to settlement).

157. *See supra* note 123.

158. *See, e.g.*, 215 ILL. COMP. STAT. 158/5 (West 2009).

159. *See supra* note 123.

160. CAL. INS. CODE § 10113.2(1) (West Supp. 2010).

161. *See, e.g., id.* §§ 10113.1-2.

wagering on life" to place limitations on the industry.[162] The Arizona legislation comprehensively defines what constitutes a stranger-originated life insurance policy, and then broadly prohibits the practice.[163] To give an inclusive effect to the prohibition, the regulatory scheme subsequently enumerates eight instances that are *not* considered illegal stranger-originated life insurance transactions.[164] As a result, by avoiding placing limitations on these policies through two- or five-year no-transaction periods and affirming that "nothing in [its legislation] prohibits the assignment of a life insurance policy that is not part of a stranger originated life insurance practice," Arizona ensures its statutory adoption solely, but effectively, prohibits the stranger-originated life insurance practice.[165] As it stands, does this method of regulation have the net effect of positively addressing public policy concerns? Which parties receive the primary benefit from this statutory strategy?

4. Regulating as Securities

Five states[166] have decided not to enact new legislation, finding practicality in deferring regulation of the secondary market for life insurance to their already established securities laws. Four of the five states have effectuated this approach by simply including "viatical settlement[s] . . . or similar agreement[s]" in their definition of an "investment contract."[167] Alabama, however, has, through its securities commission, issued a policy statement that dissents from

162. ARIZ. REV. STAT. ANN. § 20-443.02(A) (West Supp. 2009).

163. *See id.* at § 20-443.02(B).

164. The eight exempted practices include: (1) policy loans made by life insurance companies; (2) loans made by banks for a life insurance policy, so long as, (a) a default on the loan that results in the policy's transfer was not agreed upon for purposes of evading regulation, (b) the funds are only used to pay policy premiums and lender costs, (c) the policyholder has not agreed to transfer any part of the policy in the future, or (d) "[t]he [policyholder] does not receive . . . a guarantee of the future value of the sale of the policy"; (3) collateral assignments of a policy; (4) premium finance loans; (5) agreements where all parties "[a]re closely related to the insured by blood or law," or "[h]ave a lawful substantial economic interest in the continued life, health and bodily safety of the person insured"; (6) agreements made between employees and employers, where the employee is the insured; (7) "bona fide business succession planning arrangement[s]" between (a) shareholders or a corporation and its shareholders, (b) "[p]artners in a partnership," or (c) "[m]embers in a limited liability company"; (8) agreements made between service recipients and service providers "that performs significant services for the . . . recipient's trade or business." *Id.*

165. *Id.*

166. *See supra* note 125.

167. Idaho, IDAHO CODE ANN. § 30-14-102 (2008); Missouri, MO. REV. STAT. § 409.1-102 (2009); South Carolina, S.C. CODE ANN. § 35-1-102 (2009); South Dakota, S.D. CODIFIED LAWS § 47-31B-102 (2009).

the D.C. Circuit Court's ruling in *SEC v. Life Partners, Inc.*[168] In that case, the court found that a viatical settlement fell *short* of meeting the four requisite elements, established in *SEC v. W.J. Howey Co.*,[169] and should not be determined an investment contract.[170] Along with expressly declaring that the transactions *are* investment contracts, and thus securities, Alabama's statement also affirmatively announces that the state "has no position and makes no representations on the social value of viatical settlements."[171] By refusing to carve out legislation that pertains specifically to transactions on the secondary market, these states have essentially decided to require that the same level of accountability and protection enforced on other securities is maintained throughout the practice of life and viatical settlements. But, what impact does this approach have on stranger-originated life insurance? Do securities laws provide enough protection for policyholders?

5. The Hands-Off Approach

Three states have entirely withheld from taking any position on how transactions in the secondary market for life insurance should be regulated.[172] Trusting that the industry will self-regulate, these states have placed more emphasis on promoting awareness and education than mandating the same.[173] As a result, players in the market have broad authority to engage in transactions so long as they do not violate existing legislation that pertains to their practice, such as statutes that prohibit life insurance fraud.[174] Yet, will the inherent imbalance of information between parties leave some individuals at the mercy of savvy investors who are not required to make certain disclosures? Does the hands-off approach leave the market vulnerable to damaging practices?

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168. SEC v. Life Partners, Inc. 87 F.3d 536, 547-48 (D.C. Cir. 1996) (finding a viatical settlement does not provide profits to investors through the effort of others, but rather by the death of the insured).

169. SEC v. W.J. Howey Co., 328 U.S. 293, 301 (1946) (establishing four elements of an investment contract: (1) investment of money; (2) in a common enterprise; (3) with an expectation of profits; (4) to be earned through the efforts of others).

170. *See* ALABAMA SECS. COMM'N, POLICY STATEMENT ON VIATICAL SETTLEMENT CONTRACTS 3-4 (1999).

171. *Id.* at 7.

172. *See supra* note 126.

173. *See, e.g.*, CONSUMER DIV., STATE OF NEW HAMPSHIRE INS. DEP'T, VIATICAL FRAUD INFORMATION (2006), http://www.nh.gov/insurance/consumers/documents/viaticalfraud.pdf.

174. *See id.* (explaining how viatical insurance fraud is perpetrated).

III. A SELECTIVE APPROACH TO REGULATION

The current status of regulation throughout the United States' secondary market for life insurance reveals widespread inconsistency among the states and their varying approaches to maximizing the industry's benefits, while minimizing its costs.[175] It seems the discrepancy is a result of differing levels of concern for certain public policy issues.[176] Many of these concerns, founded in candid rationale, have influenced states to enact effective legislation.[177] However, some concerns seem to serve as pretexts for alternative initiatives, resulting in legislation that overburdens aspects of the secondary market for life insurance that are otherwise governed by pre-existing laws. As a result, the states should take a selective approach to regulating the secondary market, understanding that many of its components are already policed by other statutes, and sift through critics' concerns to enact laws that will protect and promote *true* public policy.

Beginning with one prevalent concern surrounding the life and viatical settlement practice, states should be aware of, and proactive about, limiting the industry's vulnerability to manipulation. The market's complexity has exposed both investors and policyholders to potential exploitation by parties in a position of greater knowledge.[178] As a result, states that have adopted laws that require licensing, reporting and certain specific disclosures to be maintained by providers, brokers and representatives effectively promote transparency and awareness in the industry, while creating minimal impositions on life and viatical settlements.[179]

On the other hand, states should refrain from imposing most procedural standards, including advertisement regulations and minimum settlement values, on the market. While these regulations are imposed with mainly philanthropic concepts in the minds of legislators, many of them have the net effect of handcuffing the industry without effectively providing utility. Therefore, states should grant limited discretion to their respective Insurance Director or Commissioner to manage specific procedures and practices.

Fraud is another ubiquitous concern in the industry.[180] States, however, through their existing statutes, expressly prohibit fraud in

175. McCarthy, *supra* note 31, at 295-96.

176. *See supra* Part I.B.5.

177. *See supra* Part II.

178. Kohli, *supra* note 45, at 313, 316-17; *see supra* Part I.B.5.

179. *See, e.g.*, Albert, *supra* note 79, at 1030-32; *see supra* Part II.C.1.

180. Halechko, *supra* note 19, at 808-13.

the insurance industry, as well as in the practice of securities transactions and other contractual agreements.[181] Thus, states should find it generally unnecessary to draft legislation to specifically prevent fraud in the secondary market for life insurance.

Last, but certainly not least, states claim to be motivated by the public policy concern against "wagering on life" when they adopt laws that prohibit stranger-originated life insurance.[182] Concerns provided by some of the strongest lobbyists in each state, however, seem to reveal alternative motivations for regulation in this corner of the market. For example, insurance companies, threatened by deflated profits as a result of decreased policy lapse rates, have been some of the practice's most critical opponents.[183] So, while many states claim that prohibiting stranger-originated life insurance promotes "a public policy which protects citizens against the assumed dangers of insurance on their lives held by strangers,"[184] pressure from other directions has also played a part in their legislative adoptions. By permitting life and viatical settlements, the states have already heavily withdrawn their interest in eliminating "sinister counter interests in having the life [of the insured] come to an end"[185] via prohibitions in this industry. Additionally, criminal punishment and privacy requirements have historically been enough to deter and prevent individuals from acting in furtherance of these sinister counter interests." Fraud statutes also prevent material misstatements on insurance applications, so insurance companies seeking the truth behind a submission for a policy need only inquire in order to obtain protection.[186] Correspondingly, minimal, if any, true public policy concerns surround the practice of stranger-originated life insurance that are not directly covered by other applicable regulations.[187] Therefore, states should allow the free market to regulate these practices, and refrain from enacting statutes that present hurdles to investors in, or that boldly prohibit, stranger-originated life insurance schemes.

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181. MD. CODE ANN., INS. § 27-401-08 (2009); 40 PA. STAT. ANN. § 474 (West 2009); N.J. STAT. ANN. § 17B:27-75 (West 2008).

182. *See supra* note 115 and accompanying text.

183. *See* Pleven & Silverman, *supra* note 28, at A1. Since premiums for stranger-originated life insurance policies are paid by investors, the likelihood that the policy will lapse decreases substantially. As a result, insurance companies who factor the expectation of lapsed policies into their profit calculations experience a decrease in net earnings. *Id.*

184. Griffin v. McCoach, 313 U.S. 498, 507 (1941).

185. Grigsby v. Russell, 222 U.S. 149, 154 (1911).

186. *See*, e.g., ME. REV. STAT. ANN. tit. 24-A, § 2186 (2009).

187. *See, e.g., Griffin*, 313 U.S. at 503.

CONCLUSION

The secondary market for life insurance has evolved over two hundred years to become one of America's most complex and thriving markets.[188] Its vulnerability to certain practices that tainted the integrity of the industry, however, have led many states to seek regulatory schemes to promote fairness and protect their citizens who are engaged in transacting their life insurance policies.[189] Wide ranging statutory adoptions from state to state have revealed potential value in finding consistent regulation that would maximize the market's net benefit.[190] To protect policyholders and investors in positions of less knowledge, licensing, reporting and disclosure mandates should be enacted by the states. To promote flexibility and allow the industry to maximize its lucrative nature, states should defer to existing laws for regulating procedural standards, the potential for fraud in the market, and stranger-originated life insurance transactions. Altogether, this regulatory format would provide rigidity where public policy concerns warrant protection, while minimizing its effect on restricting the secondary market for life insurance's great economic potential.

188. *See generally* Sippel & Brueger, *supra* note 13.

189. *See supra* Part II.C.1.

190. *See supra* notes 122-23.

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