

AMERICAN COUNCIL OF LIFE INSURERS  
TESTIMONY IN SUPPORT OF HB 94, RELATING TO INSURANCE

February 22, 2008

Via E Mail: [fintestimony@capitol.hawaii.gov](mailto:fintestimony@capitol.hawaii.gov)  
Representative Marcus R. Oshiro, Chair  
House Committee on Finance  
Hawaii State Capital, Conference Room 308  
415 S. Beretania Street  
Honolulu, HI 96813

Dear Chair Oshiro and Committee Members:

Thank you for the opportunity to testify in support of HB 94, relating to Insurance.

Our firm represents the American Council of Life Insurers ("ACLI"), a national trade association whose three hundred fifty-three (353) member company's account for 93% of the life insurance premiums and 94% of the annuity considerations in the United States among legal reserve life insurance companies. ACLI member company assets account for 93% of legal reserve company total assets. Two hundred sixty-one (261) ACLI member companies currently do business in the State of Hawaii.

HB 94 enacts the National Conference of Insurance Legislators ("NCOIL") Life Settlement Model Act. The NAIC Viatical Settlement Model Act, as recently amended, has been introduced this session in the House as HB 3099 and in the Senate as SB 3021. Both Model Acts require the licensing of brokers who negotiate life settlement contracts and providers who effectuate the life settlement contracts with the owner.

While the NCOIL Life Settlement Act and the NAIC Viatical Settlement Model Act each approach the regulation of stranger-originated life insurance or "STOLI" differently, both provide needed and effective regulation of this growing predatory practice.

ACLI strongly supports legislation which protects consumers, particularly elderly consumers, from "STOLI".

What Is Stranger Originated Life Insurance?

An investor, usually a hedge fund or other institutional investor, arranges for the purchase of a policy insuring the life of a person over 70 years of age, who is insurable for at least \$5M. The investor funds the policy with the expectation that policy benefits will ultimately flow to the investor. This is usually done by the insured individual's transferring the ownership of the policy to the investor after 2 years but it can also be effected by the insured's irrevocably assigning a large percentage of the policy benefits after this 2 year period to the investor.

The investor funds the cost of the insurance by making a non-recourse loan to the insured; that is, the insured is not personally liable on the loan – instead, the investor's only recourse is against the policy which secures the loan. The interest rate on the loan is comparable to a credit card. If the insured dies during the two year period, the policy benefits must first be used to pay off the loan and fees owed to the investor, but the remainder is paid to the insured's designated beneficiary. If the insured survives the 2 year period, the insured can either repay the loan and keep the policy or transfer the policy to the lender in full satisfaction of the debt. Due to the high interest rate and fees, the insured will almost invariably choose to transfer the policy to satisfy the debt.

If the offer of free insurance is not enough, the insured may be paid some sort of signing bonus in exchange for his participation in the deal.

ACLI believes that STOLI is wrong.

1. STOLI is morally wrong and wrong for the life insurance industry and consumers.

Wagering on the lives of people is wrong.

- STOLI violates the intended purpose of life insurance. Life insurance is designed to protect an individual's family and estate in the case of a death – not to financially benefit a group of strangers gambling on a person's life.
  - STOLI benefits investment groups and hedge funds, not families. It circumvents insurable interest laws and does not protect consumers.
2. STOLI invites wrong-doing.
- STOLI investors are betting on the early deaths of consumers, not on their continuing good health. This gaming scheme simply invites wrong-doing that targets elderly seniors.
  - With STOLI, consumers do not have control over their own life insurance policies. Their life insurance is owned by or sold to strangers who do not have their health and welfare at heart.
  - Under STOLI transactions, consumers do not know who owns their life insurance policy and what that person or persons intend to do with it.
3. Preying on the elderly is wrong.
- STOLI takes advantage of the elderly – inducing them to buy something they would not normally buy and do not need.
  - There may be hidden tax consequences for elderly consumers that investors do not warn them about.

- If people enter into a STOLI arrangement, they may not be able to obtain more life insurance at a time they really need it.
  - STOLI is an unregulated business that preys on the elderly.
4. STOLI is unfair to consumers.

While the cost of life insurance continues to fall, enabling more Americans to obtain good coverage, STOLI could reverse this positive trend at the expense of all consumers.

5. STOLI is detrimental to the life insurance industry.

STOLI will likely alter the way life insurance companies do business. Insurance companies have been consistently able to raise the age at which they are able to provide affordable life insurance. STOLI may eventually result in fewer choices for insurance consumers.

HB 94 prohibits STOLI transactions by prohibiting “life settlement contracts” at any time prior to policy issuance or within a 2 year period thereafter, unless otherwise exempted.

HB 94 makes engaging in “STOLI” schemes a fraudulent life settlement act subject to regulatory and civil penalties. Further, any person damaged by the STOLI scheme may bring a civil suit for damages against the person committing the violation.

In prior written testimony the Life Settlement Institute (“LSI”) has suggested that the definition of “STOLI” be amended as follows:

~~“Stranger-originated life insurance” or “STOLI” means a practice or plan to initiate a policy for the benefit of a third party investor who, at the time of policy origination, has no insurable interest in the insured, and includes: Arrangements in which life insurance is purchased with resources or guarantees from or through a person or entity who at the time of policy inception, could not lawfully initiate the policy himself or itself, and where, at the time of inception, there is an arrangement or agreement, whether verbal or written, to directly or indirectly transfer the ownership of the policy, the policy benefits, or both, to a third party; and~~  
(2) the procurement of new life insurance by persons or entities that lack insurable interests on the insured and, at policy inception, such person or entity owns or controls the policy or the majority of the death benefit in the policy and the insured or insured’s beneficiaries receive little or none of the proceeds of the death benefits of the policy. Trusts created to give the appearance of insurable interest and used to initiate policies for investors.

The suggested change is objectionable as it limits the definition of STOLI to situations where the third party without an insurable interest owns or controls the policy

at inception. This is already a violation of the insurable interest under current law. Accordingly, the suggested amendment adds no new provision to prevent STOLI.

The NCOIL definition picks up much more. Included within its definition are “practices or plans” to secure a policy for an investor; cases where the policy is paid for or guaranteed by the investor; and where there is an “arrangement” or an “agreement” to transfer the policy to the investor.

In support of the amendment LSI states that the STOLI definition in the Model Act was presented to the NCOIL Executive Committee at the last minute, suggesting that it was hastily drafted without careful thought and analysis. It was not. It was carefully crafted with the input of all stakeholders.

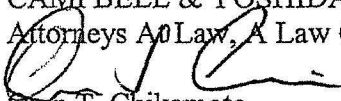
Further, LSI suggests that Kentucky Representative Damron’s decision to revise the STOLI definition as described above is reflective of the NCOIL executive committee as a whole. It does not.

Indeed, others in the life settlement industry support the NCOIL STOLI definition.

In a recent press release the executive director of the Life Insurance Settlement Association has characterized the NCOIL definition as a pioneering consumer protection measure. In commenting on the STOLI transaction which was the subject of a lawsuit filed in the U.S. District Court case of Life Product Clearing LLC, vs. Angel, \_\_\_ F. Supp.2d \_\_\_, 2008 WL170193 (Jan. 22, 2008, S.D.N.Y.) LISA observed:

The Angel order repeatedly demonstrates the wisdom of the NCOIL Model . . . The NCOIL Model provides a legislative definition of STOLI as “a practice or plan to initiate a life insurance policy for the benefit of a third party investor.” This is virtually identical language to the court’s holding in Angel. And NCOIL’s pioneering consumer affirmations – including written certifications stating “I have not entered into any agreement or arrangement providing for the future sale of this life insurance policy” and “I have not entered into any agreement by which I am to receive consideration in exchange for procuring this policy” – would likely have stopped issuance of this policy.

ACLI strongly supports legislation which effectively deters STOLI transactions. HB 94 does so. ACLI, therefore, respectfully requests that this Committee pass HB 94, **UNAMENDED**.

CHAR HAMILTON  
CAMPBELL & YOSHIDA  
Attorneys At Law, A Law Corporation  
  
Oren T. Chikamoto  
737 Bishop Street, Suite 2100  
Honolulu, Hawaii 96813  
Telephone: (808) 524-3800

GOODSILL ANDERSON QUINN & STIFEL

A LIMITED LIABILITY LAW PARTNERSHIP LLP

GOVERNMENT RELATIONS TEAM:

GARY M. SLOVIN, ESQ.  
CHRISTOPHER G. PABLO, ESQ.  
ANNE T. HORIUCHI, ESQ.  
MIHOKO E. ITO, ESQ.  
JOANNA J. H. MARKLE\*  
LISA K. KAKAZU\*\*

\* Government Relations Specialist  
\*\* Legal Assistant

ALII PLACE, SUITE 1800 • 1099 ALAKEA STREET  
HONOLULU, HAWAII 96813

MAIL ADDRESS: P.O. BOX 3196  
HONOLULU, HAWAII 96801

TELEPHONE (808) 547-5600 • FAX (808) 547-5880

info@goodsill.com • www.goodsill.com

INTERNET:

gslovin@goodsill.com  
cpablo@goodsill.com  
ahoriuchi@goodsill.com  
meito@goodsill.com  
jmarkle@goodsill.com  
lkakazu@goodsill.com

February 21, 2008

TO: Representative Marcus Oshiro  
Chair, Finance Committee  
Hawaii State Capitol, Room 306

Via Email: [FINtestimony@Capitol.hawaii.gov](mailto:FINtestimony@Capitol.hawaii.gov)

FROM: Gary M. Slovin

RE: **H.B. 94, HD1 – Relating to Insurance**  
**Hearing Date: Friday, February 22, 2008 at 12:00 pm**

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Dear Chair Oshiro and Members of the Committee on Finance:

I am Gary Slovin, submitting testimony on behalf of the Life Settlements Institute (“LSI”). LSI membership consists of the world’s leading institutional investors and intermediaries in the mortality and longevity marketplace.

HB 94, HD 1, Relating to Insurance establishes the Life Settlements Model Act (“Act”) adopted by the National Conference of Insurance Legislators (NCOIL). LSI supports the intent of HB 94, HD1 and offers a few clarifying amendments.

Clarify STOLI Definition

HB 94, HD1 contains a definition of Stranger Originated Life Insurance (“STOLI”) that reflects the definition used in the NCOIL Model Act. It should be noted that this definition was presented to the NCOIL Executive Committee literally at the very last minute, only one half hour before the final vote on approval of the Act, after more than a year of intense deliberations on its provisions.

A primary mover on the NCOIL Executive Committee for the inclusion of a STOLI definition in the Act was Representative Robert R. Damron of Kentucky, who, upon reflection, has decided that the definition in the Act should be revised. LSI strongly supports the revised definition of STOLI that Rep. Damron has introduced in Kentucky

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and has passed the Kentucky House as HB 348/HCS, Kentucky Regular Session of 2008 (see attached). Kentucky's proposed definition is below and LSI suggests that it replace the STOLI definition in HB 94, HD 1 on page 13, line 16 through page 14, line 10:

“Stranger-oriented life insurance” or “STOLI” means the procurement of new life insurance by persons or entities that lack insurable interest on the insured and, at policy inception, such person or entity owns or controls the policy or the majority of the death benefit in the policy and the insured or insured's beneficiaries receive little or none of the proceeds of the death benefits of the policy. Trusts that are created to give the appearance of insurable interest and are used to initiate policies for investors violate insurable interest laws and the prohibition against wagering on life. STOLI arrangements do not include those practices set forth in subsection (b) of the definition of “Life Settlement Contract.”

#### Disclosure of Common Control

Additionally, LSI believes that the prohibition of common control between a broker and a provider, as called for in Part V, § -41 subsections (6) and (7) of HB 94, HD 1 should be modified. Transparency is critical to consumer protection and we propose an amendment that would provide such transparency. A broker who is under common control with a provider might make the best offer to an owner for the sale of the policy. Common control of an entity should not preclude an owner from obtaining the maximum amount in disposing the policy so long as full disclosure has been made. As long as a life settlement broker has established policies and procedures that require the full disclosure of its affiliation to any life settlement provider, and as long as these parties are required to disclose this relationship to the consumer, in order to prevent any conflict of interest, a life settlement broker should be able to procure a sale of a policy to the highest bidder, regardless of the relationship among parties. Prohibiting a broker from selling a policy to an entity under common control (even where the entities are separately managed) is inconsistent with a broker's fiduciary duty to his or her client where the sale is in the consumer's best interest, e.g. where the affiliate is the highest bidder. In order to ensure that the consumer obtain the maximum value for a policy, LSI proposes the following amendments:

On page 52, subsection (6) should read as follows:

“(6) With respect to any policy or life settlement contract and a broker, knowingly solicit an offer from, effectuate a life settlement contract with, or make a sale to any

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provider, financing entity, or related provider trust that is controlling, controlled by, or under common control with such broker, unless such relationship is disclosed to the owner.”

On page 52, subsection (7) should read as follows:

“(5) With respect to any policy or life settlement contract and a provider, knowingly enter into a life settlement contract with an owner, if, in connection with such life settlement contract, anything of value will be paid to a broker that is controlling, controlled by, or under common control with such provider or the financing entity or related provider trust that is involved in such settlement contract, unless such relationship is disclosed to the owner.”

LSI strongly believes that there should be no tolerance for unscrupulous players in this market who take advantage of consumers who are probably at the most vulnerable stage of their lives. We look forward to working with you and other interested parties in developing legislation that will prevent such players from doing business in Hawaii while allowing consumers the opportunity to obtain needed financial assistance free from harm.

Thank you for the opportunity to submit testimony.

holding the ownership or beneficial interest in policies. The trust shall have a written agreement with the licensed life settlement provider under which the licensed life settlement provider is responsible for ensuring compliance with all statutory and regulatory requirements and under which the trust agrees to make all records and files related to life settlement transactions available to the executive director as if those records and files were maintained directly by the licensed life settlement provider.

(13) "Settled policy" means a life insurance policy or certificate that has been acquired by a life settlement provider pursuant to a life settlement contract.

(14) "Special purpose entity" means a corporation, partnership, trust, limited liability company, or other similar entity formed solely to provide, either directly or indirectly, access to institutional capital markets for a financing entity or licensed life settlement provider.

(15) "Stranger-originated life insurance" or "STOLI" means the procurement of new life insurance by persons or entities that lack insurable interest on the insured and, at policy inception, such person or entity owns or controls the policy or the majority of the death benefit in the policy and the insured or insured's beneficiaries receive little or none of the proceeds of the death benefits of the policy. Trusts that are created to give the appearance of insurable interest and are used to initiate policies for investors violate insurable interest laws and the prohibition against wagering on life. STOLI arrangements do not include those practices set forth in paragraph (b) of subsection (17) of this section.

~~(16)(6) — "Wholesale life insurance" is that plan of life insurance, other than salary savings life insurance or pension trust insurance and annuities, under which individual policies are issued to the employees of any employer and where policies are issued on the lives of not less than four (4) employees at date of issue. Premiums for the policies shall be paid either wholly from the employer's funds, or~~