TESTIMONY SUPPORTING HB 404

BY

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AMERICAN COUNCIL OF LIFE INSURERS

BEFORE THE

STATE OF OHIO

HOUSE INSURANCE COMMITTEE

REPRESENATIVE BILL BATCHELDER, Chairman

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Good afternoon, Mr. Chairman and members of the Committee, my name is Bruce Ferguson. I am Senior Vice President of State Relations for the American Council of Life Insurers. Thank you for the opportunity to testify today in strong support of House Bill 404. We appreciate the leadership of Representative Hottinger, Representative Barrett and Insurance Director Hudson in developing this legislation.

The ACLI is a national trade comprised of 373 member life insurers. We are very proud to include within our membership several Ohio based companies, including Nationwide, Western and Southern, Ohio National, Union Central, Grange, Motorists Life, Anthem Life, Central Reserve, Great American Life and Western Reserve Life. Together, ACLI members account for 91 percent of the life insurance premiums and 94 percent of the annuity considerations in this state.

We have reviewed both H.B. 404 as introduced and the proposed substitute for H.B. 404, which includes amendments that were developed during the Subcommittee's deliberations on the bill. ACLI strongly supports the bill and those amendments. We are grateful to Director Hudson and her staff for their willingness to consider our concerns and the concerns of other stakeholders involved in this issue. The package of amendments that was developed as a result of those discussions make this bill a stronger tool to protect Ohio's consumers and ensure effective regulation of the viatical and life settlement marketplace.

We are particularly pleased that H.B. 404 effectively addresses stranger-originated life insurance, or STOLI, a practice where speculators aim to circumvent your state's insurable interest law and abuse the vital social purpose of life insurance. A fundamentally important principle of life insurance since the 17th century, insurable interest stands for the proposition that at the time the life insurance policy is issued, the person who procures the policy, or causes the policy to be procured, must have a lawful and substantial economic interest in having the life of the individual insured continue, as distinguished from an interest that would only arise by, or would be enhanced in value by, the death of the insured.

Unfortunately, Mr. Chairman, the insurable interest doctrine is being turned on its head by third party investors who procure the issuance of life insurance policies on elderly people in whom the investors have no insurable interest, for the sole purpose of acquiring those policies and profiting from them at a later date. These schemes are increasing in number and sophistication and require immediate action on the part of public policy makers to protect senior citizens from the real and hidden perils of such transactions. For example, seniors may face unexpected taxes and fees, loss of insurance capacity and loss of privacy. In addition, promoters of these schemes may induce seniors to mislead insurers on policy applications.

By way of example, one of the more prevalent forms of STOLI involves a life settlement company or broker approaching an elderly individual, pitching a program in which the individual could generate a profit from the sale of a life insurance policy insuring the individual's life without having to pay any premiums on the policy. The elderly individual obtains a non-recourse loan (secured only by the policy) arranged by the life settlement company that carries an exorbitant interest rate and is scheduled to mature 26 months after date of issuance of the policy. Following the expiration of the two-year settlement moratorium in state law, the life settlement company assists the individual in selling the policy to financial investors, who repay the loan in exchange for ownership of the policy.

One of the most important provisions of H.B. 404 is the strictly limited five year moratorium on settlements such as these that are initiated by investors ultimately for their own profit, not for the benefit of the insureds and their beneficiaries. The bill targets these transactions without adversely impacting consumers' ability to sell policies that were purchased for legitimate financial protection purposes but are no longer wanted or needed. For example, the bill allows policyholders to settle their policies *at any time* if they experience a change in life circumstances, such as illness, loss of employment, divorce or death of the intended beneficiary. Additionally, the two year settlement moratorium found in existing Ohio law would be preserved for most policy purchases (i.e., those where the policyholders use their own assets or traditional premium financing to purchase the policy, and where the policy has not been pre-evaluated for settlement).

The result: in transactions such as the one alluded to earlier, investors have to wait five years to get their hands on a policy that was initiated with the intent of settling it. This significantly reduces the economic incentives for STOLI transactions to occur, as investors will be far less likely to engage in these transactions if their investment dollars are tied up for five rather than two years, especially given that the target market for life settlements are seniors age 65 and older. An added benefit of this legislation is that it does not preclude any form of premium financing – it simply ensures that any such premium financing works primarily for the benefit of the insured, not the third-party investors. Ultimately, therefore, it is the elderly insurance consumer who stands to benefit from this legislation, which helps stop abusive transactions before they occur and before seniors are put in harm's way.

We are also heartened that committee substitute also includes language recommended by Director Hudson addressing the use of trusts and other vehicles by speculators as a means of cloaking the existence of insurable interest at policy inception. Developed and adopted by the National Conference of Insurance Legislators (NCOIL) after extensive discussion, this language is intended to address some of the more sophisticated schemes involving ownership of a life insurance policy by a trust that is controlled by and organized for the benefit of third party investors, not the insured or the insured's estate or beneficiaries.

Additionally, we support those provisions now in the committee substitute that would make certain practices that are characteristic of STOLI transactions fraudulent settlement acts. Derived from the NCOIL Life Settlements Model Act, one such provision would prohibit the issuance, solicitation, or marketing of a policy for the purpose of or with an emphasis on settling the policy. Another would prohibit persons from concealing from an insurer when requested the fact that the prospective insured has undergone a life expectancy evaluation by a party other than the insurer in connection with the application, underwriting or issuance of the policy. These provisions, in conjunction with the targeted five year settlement moratorium on suspicious transactions, provide an effective framework for addressing STOLI while preserving policyholders' ability to sell their policies in the secondary market.

As we sorted through the comments on the proposed legislation submitted by various interested parties, we were pleased to read that some within the life settlement community endorse the limited five-year settlement moratorium and the other anti-STOLI provisions contained in H.B. 404. In its comments, Life Settlement Insights, Ohio largest life settlements broker, states that the provisions for preventing STOLI transactions are both “timely and necessary”, another indication that the regulatory framework proposed by H.B. 404 is a responsible and reasonable approach.

Mr. Chairman, I again want to thank you for this opportunity to testify today, and express our appreciation to the sponsors and Director Hudson for their leadership on this issue. By enacting House Bill 404, Ohio will be among the first in the country to protect consumers from abusive STOLI transactions and provide for the effective regulation of the viatical and life settlements marketplace. I would be happy to answer any questions you or members of the committee may have.