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# VIATICAL SETTLEMENTS AND THE ELDERLY: POTENTIAL ADVANTAGES AND HIDDEN DANGERS

*Anna D. Halechko**

## Introduction

A viatical settlement is a process by which a terminally ill individual can sell his or her life insurance policy to an investor who pays the insured a discounted face value and then collects the policy benefit upon the insured's death.[1] The term "viatical" comes from the Latin word "viaticum," which in Roman times was a purse containing money and provisions for a journey.[2] Later, the term was used to refer to the communion given to the dying in the last rites of the Catholic Church.[3] In its purest form, therefore, a viatical settlement is a way in which dying people can acquire access to resources to benefit the last days of their lives. This noble-sounding purpose, however, has been complicated and often corrupted by the actions of overzealous entrepreneurs who are willing to take advantage of the most vulnerable in society in order to increase profits. Viatical settlements are often marketed to the chronically and terminally ill. The elderly in particular have been targeted as a major market for this financial vehicle.[4] This article will first explore the basic workings of a viatical settlement, along with its benefits and disadvantages for elderly consumers. The second section reviews the problem of fraud, which has permeated the viatical market, together with the developing case law related to the viatical industry. The concluding section addresses the potential for regulation of the industry.

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1 Liza M. Ray, *The Viatical Settlement Industry: Betting on People's Lives Is Certainly No "Exacta,"* 17 J. Contemp. Health L. & Pol'y 321, 322 (2000).

2 *Id.* at 325.

3 *Id.*

4 *See generally* Lawrence A. Frolik, *Insurance Fraud on the Elderly*, 37 Trial 48 (2001).

## I. The Mechanism of a Viatical Settlement

The key parties in a viatical settlement are the insured, known as the *viator*, the *insurance company* that issued the policy, and the *viatical settlement provider* who purchases the policy from the insured. In some cases, the viatical settlement provider is a broker who merely matches the viator with an investor, the person who will actually purchase the policy. As the investment market in viaticals has grown, the roles of provider and broker have become blurred: many providers purchase policies only to resell them to investors or merge them into large investment pools which are then sold in shares. These mutual funds of viaticated policies or so-called "death futures" have become both popular investment vehicles and the subject of numerous fraudulent schemes.[5]

The first step in the viatication process is a meeting between the terminally ill insured and the viatical provider. The provider typically requires access to the insured's medical records and often contacts the insured's physician directly. In addition, the provider reviews the insurance policy to determine that change of beneficiary is permitted and that no unusual restrictions apply. The provider also ascertains that the insurer is a reputable company with a strong record of paying beneficiaries promptly. Essentially, the provider investigates the factors that determine the degree of risk in the investment. From this determination, the provider will calculate an offer price for the viator.

If the viator accepts the offer, the policy is sold to the provider who then lists himself or herself as the beneficiary on the policy. The provider is now responsible for paying any remaining premiums. Typically, the provider will stay in touch with the viator, and upon the viator's death, will collect the entire face value of the policy. The provider's profit is the face value minus the amount paid to the viator, minus any premiums or other administrative expenses.

In the simplified version of the process described above, the viator and provider work with one another directly. In reality, there are likely to be many intervening parties involved in the transaction. As noted, a broker often makes the initial contact with

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5 *See generally* Miriam R. Albert, *The Future of Death Futures: Why Viatical Settlements Must be Classified as Securities*, 19 PACE L. REV. 345 (1999); Andrew Spurrier, Commentary, *The Death of Death Futures?: The Effects of the Health Insurance Portability and Accountability Act of 1996 on the Insurance and Viatical Settlement Industries*, 4 CONN. INS. L.J. 807 n.1 (1998) (explaining that the term "death futures" was originally used in this context in a SPY magazine article in 1993).

the viator, who may not even know the true purchaser of his or her policy. Often, the funds are not passed directly, but are held in escrow until the beneficiary change is finalized. Afterward, there may be others involved in administering the policy: paying the premiums, checking on the viator, obtaining a death certificate, and applying to the insurer for the death benefit.

The complexity of this process is significant, and poses some dangers to viators who initially may not realize they are dealing with a conglomerate of businesses rather than with an individual. The major power imbalance between the viators and the viatical settlement providers and their associates creates a strong potential for abuse.[6] Because of illness, a viator may not have the energy or motivation to "comparison shop" for the best payment.[7] A viator may not realize that he or she is giving up all rights to the policy for himself or herself and for his or her former beneficiaries. Time is precious — what should a viator do if the payment is delayed or some other problem arises and the viator is unable to contact the viatical provider? Finally, there is the major issue of confidentiality, because each additional party to a viatical transaction may gain access to the viator's medical records and may even intrude upon the viator's privacy directly by phoning or visiting the viator at home (ostensibly to see how the viator is doing; actually to determine if he or she is still alive).

## II. Growth of the Viatical Industry

The viatical industry was born in the 1980s in response to the Acquired Immune Deficiency Syndrome (AIDS) crisis.[8] In the early years of the pandemic, AIDS was a rapidly fatal disease whose victims usually died within a few months of their diagnosis. Many AIDS sufferers were single gay men who had little need to leave

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6 Joy D. Kosiewicz, *Death for Sale: A Call to Regulate the Viatical Settlement Industry*, 48 Case W. Res. L. Rev. 701, 703 (1998) ("On one side of the transaction is a large company with numerous resources, lots of money, and enormous bargaining power. On the other side is a terminally or chronically ill patient or elderly person with little money, big expenses, and few resources.").

7 The viatical provider may essentially have a monopoly in a local area:

> [e]ach geographical area has a small number of firms providing a service with no close substitutes, some barriers to entry, and the potential for excess profits. . . . Thus, viatical settlement companies may have functional monopolies which allow them, in effect, to hold potential viators who may be too sick to travel, or even to investigate other alternatives, essentially as geographic hostages.

Miriam R. Albert, Article, *Selling Death Short: The Regulatory and Policy Implications of Viatical Settlements*, 61 Alb. L. Rev. 1013, 1023 (1998).

8 Kosiewicz, *supra* note 6, at 704.

their insurance proceeds to beneficiaries, but were in great need of an infusion of income to pay for their care after they became debilitated by the disease. Their life expectancies were short and relatively predictable; thus, they were attractive subjects for viatication.

The industry grew dramatically from the approximate sale of $500 million in policy values in 1989 to well over $1 billion by 2000.[9] But along the way, the essential characteristics of the viator population changed. Advances in medicine made AIDS a treatable, if not curable, disease. Instead of dying within a few months, AIDS patients' lives could be continued for years on a regimen of antiviral "cocktails." They no longer were the sure bet for rapid demise that had been so attractive to the early viatical settlement companies. Nevertheless, the viatical providers found new markets for their product in the growing population of chronically ill and elderly persons.[10] People suffering from cancer, Alzheimer's disease, and other progressive illnesses, as well as frail elderly men and women in need of funds for assisted living, found that viatical settlements could provide a new source of income.[11] In addition, a rather surprising new viator population emerged: affluent older people who had purchased life insurance when their children were young but no longer felt the need to provide for them and wanted to enjoy at least a partial return from their policies.[12]

A major impetus to the growth of the viatical settlement industry occurred with the passage of the Health Insurance Portability and Accountability Act (HIPAA) in 1996.[13] Under the IRS regulations in existence prior to HIPAA, payments received under a life insurance contract by reason of the death of the insured were excluded only from the taxable income of the beneficiary.[14] In contrast, payment received by the insured for the sale of his policy was considered ordinary taxable income. HIPAA expanded the exclusion to benefit the terminally ill by providing that viatical settlements and accelerated death benefits would not be taxable.[15] The Act also provided a relatively flexible definition of "terminal ill-

9 Albert, *supra* note 5, at 353.

10 *Id.* at 357.

11 *Id.*

12 Joseph B. Treaster, *Death Benefits, Now for the Living*, N.Y. TIMES, Sept. 27, 1998, § 3, at 1.

13 Health Insurance Portability and Accountability Act of 1996, 26 U.S.C. § 101(g) (1997); I.R.C. § 101(g) (1997).

14 Spurrier, *supra* note 5, at 813.

15 *Id.* at 814. In contrast to viatical settlements, accelerated death benefits are paid by the insurance company to the insured under the terms of some policies. Typically, these benefits represent a lower percent of the policy face value than a viatical pay-

ness" as an illness or physical condition of an individual such that death can "reasonably be expected" to occur within 24 months, as estimated by the individual's physician.[16]

In addition, HIPAA extended tax benefits to the chronically as well as the terminally ill, if the proceeds of the viatical settlement were used to pay for long-term care services.[17] A chronically ill individual was defined as someone who is unable to perform at least two activities of daily living without assistance for a period of at least 90 days or who requires substantial supervision to protect his health and safety because of severe cognitive impairment.[18] By the late 1990s, viatical marketers focused heavily on these new target populations of terminally and chronically ill elderly, and AIDS sufferers comprised only a small percentage of viators.

## III. Fraud in the Viatical Industry

The elderly are particularly susceptible to becoming victims of fraudulent investment schemes.[19] Diminished acuity in sight and hearing causes difficulty in reading the fine print of contracts or listening to an oral explanation of risks and benefits.[20] Poor health and lack of energy may prevent an elderly individual from conducting a thorough investigation before signing an agreement.[21] Cognitive deficits such as mild dementia or simple short-term memory loss may interfere with understanding the transaction.[22] Even social isolation can contribute to an elderly person's vulnerability when approached by a seemingly friendly salesperson.[23]

The prospect of selling a policy to a viatical settlement company may seem like an easy method to acquire extra funds for the chronically ill elderly person living on a fixed income. However, the extra money may actually interfere with the person's eligibility for current sources of income, such as means-tested benefits like

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ment, but the remaining value of the policy is paid to the beneficiary after the insured's death. Ownership of the policy remains with the insured. *Id.* at 809-10.

16 *Id.* at 816.

17 *Id.* at 818.

18 *Id.*; *see also* Gary J. Gasper, *Viatical Settlements – Cashing Out Life Insurance*, 11 Prob. & Prop. 20, 21-22 (1997) (explaining HIPAA changes).

19 Lawrence A. Frolik, Ass'n of Trial Lawyers of Am. Annual Convention, *Why the Elderly Are Vulnerable to Insurance Fraud*, 1 Ann. 2001 ATLA-CLE 597 (2001).

20 *Id.*

21 *Id.*

22 *Id.*

23 *Id.*; *see also* Frolik, *supra* note 4.

Medicaid and SSI.[24] Nursing homes may even encourage elderly residents to become viators because the resulting self-payment from the resident would be higher than the home's reimbursement from Medicaid.[25] At the other end of the economic spectrum, an affluent elderly person who has funds to invest may be drawn by promises of high returns and low risk, or may even view the viatical market as a humanitarian endeavor.[26]

Unfortunately, the viatical industry has been plagued with many forms of fraud and unethical practices, as will be discussed. Because of the complex relationships among the viator, the insurance company, the viatical provider, the investor, and various agents and brokers, the possibilities for deception are numerous. In general, fraudulent practices in the viatical industry can be classified into four major categories: (1) insurance agents defrauding insurance companies by hiding the viators' health status; (2) viators defrauding insurance companies on their own; (3) viators defrauding viatical settlement companies; and (4) viatical settlement companies defrauding viators and investors alike.[27]

*Davis v. Texas* provides an example of the first type of fraud.[28] There, an insurance agent worked with a viatical provider to induce AIDS viators to apply for additional policies; soon after they sold their existing policies to the viatical company, the AIDS sufferers were contacted by the insurance agent who assisted them in applying for several new policies.[29] The agent filled out the insurance applications with false information about the applicants' health status, a process known as "clean sheeting."[30] The viators were reimbursed for the policy premiums and were paid directly for each new policy issued.[31]

The second type of fraud is illustrated in *Amex Life Assurance v. Superior Court of Los Angeles County*.[32] There, an applicant for an insurance policy, who knew he was HIV positive, sent an imposter to take the required physical exam.[33] Later, the insured individual sold the policy to a viatical company. After the viator's death and

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24 Gregory C. Larson & Melissa Hauer, *Planning for Nursing Home Care in North Dakota*, 74 N.D. L. REV. 191, 198 (1998).
25 Albert, *supra* note 5, at 364.
26 *See* Treaster, *supra* note 12.
27 Albert, *supra* note 5, at 368.
28 68 S.W.3d 273 (Tex. Ct. App. 2002).
29 *Id.* at 278.
30 *Id.* at 279.
31 *Id.*
32 930 P.2d 1264 (Cal. 1997).
33 *Id.* at 1266.

the discovery of the deception, the insurance company attempted to withhold payment to the viatical provider.[34] The court ruled against the insurer, however, because the two-year contestability period on the policy had expired.

The third type of fraud occurs if a viator presents his or her health status *worse* than it actually is, deceiving the viatical provider into offering a higher payment for his or her policy.[35] For example, an AIDS patient could postpone starting a course of treatment until after the viatical settlement was complete.[36] If he then underwent a successful course of treatment that had the effect of prolonging his life, the profit margin of the viatical provider would be reduced.[37]

Another potentially fraudulent activity perpetrated by a viator could occur if an insured person sold his or her policy to more than one viatical company, although this type of fraud has become less likely as viatical providers have become increasingly sophisticated and require direct confirmation from the insurance company of any policy changes undertaken by the insured.[38] Nevertheless, a viator may attempt to sell a policy over which he or she has no legal control. In *Gander v. Gander*, a father was required as part of a divorce settlement to maintain a life insurance policy on himself as the insured and his ex-wife as the beneficiary, with all proceeds of the policy to be held in trust for the couple's two children. However, he sold the policy to a viatical settlement company.[39] The children sued the viatical provider, and the court found that they were the legal beneficiaries of the policy.[40] Although the viatical company argued unsuccessfully that it was a bona fide purchaser of the policy, the court held that the company had notice of the conflicting claim.[41]

The most prevalent form of fraud is the final type, in which unscrupulous providers and brokers deceive unsuspecting viators and investors. The viator is defrauded by receiving payment far below the present value of his or her policy. The National Association of Insurance Commissioners (NAIC) has issued guidelines for payments based on the life expectancy of the insured; however,

34 *Id.*
35 Albert, *supra* note 5, at 377.
36 *Id.*
37 *Id.*
38 *Id.* at 378.
39 250 F.3d 606 (8th Cir. 2001).
40 *Id.* at 613.
41 *Id.*

these have not been adopted in all states.[42]

Many schemes have been perpetrated by viatical providers to solicit investors fraudulently, often from among the vulnerable elderly population. In *SEC v. Tyler*,[43] the defendant was accused of enticing more than 480 elderly investors into purchasing viatical shares with false guarantees of liquidity, high interest rates, and fixed maturity dates. In reality, viaticals are generally not liquid, do not have fixed maturity dates (because the date of the insured's death is uncertain), and their rate of return is a variable dependent upon how long the insured survives after his or her policy is sold.[44] Tyler lured investors through an elaborate campaign of newspaper ads, investment seminars, telemarketing calls, and mass mailings.[45]

In a Pennsylvania case, *Srein v. Frankford Trust Co.*, a broker sold the same viatical policy to two investors.[46] Although both investors had accounts with Frankford Trust, the viaticals were not registered investments and no one at the trust company noticed the duplication.[47] After several years, Srein began to investigate why his viatical investments were not paying off and discovered that the policy benefits had been paid out to the other investor.[48] At the district court level, his suit against the trust company was unsuccessful because of his contributory negligence in failing to monitor his investments more closely.[49]

On appeal, the decision was reversed and the case remanded for a new trial.[50] The appeals court recognized that the trust company had a fiduciary duty to the plaintiff, established when Frankford solicited Srein's business and charged him fees for trust management.[51] In failing to establish an efficient tracking system which would have identified the duplications, Frankford neglected to notice that the proceeds of Srein's investments were being paid into another account.[52] However, even the appeals court chal-

42 VIATICAL SETTLEMENTS MODEL REGULATION (National Association of Insurance Commissioners, Draft 2003), *at* http://www.naic.org/models_papers/models/docs/viatic14.pdf (on file with the New York City Law Review).

43 No. 3:02-CV-0282-P, 2002 U.S. Dist. LEXIS 2952 (N.D. Tex. Feb. 21, 2002).

44 *Id.*

45 *Id.* at *3-4.

46 323 F.3d 214, 219 (3d Cir. 2003). Srein initially sued the broker and won a judgment of $2 million, but by then the broker was insolvent and the judgment could not be collected. *Id.*

47 *Id.* at 217.

48 *Id.* at 219.

49 *Id.*

50 *Id.* at 225.

51 *Id.* at 222-23.

52 *Id.* at 219.

lenged Srein for not monitoring his investments more closely, and reversed the lower court on the ground that it had failed to properly instruct the jury on the Pennsylvania Comparative Negligence Act.[53] Thus, it seems that "let the buyer beware" continues to be the appropriate motto for investors in viatical plans.

## IV. Viatical Settlements and Securities Regulation

Courts have struggled with the question of whether or not viatical arrangements should be considered "securities" and thus subject to the control of the Securities and Exchange Commission (SEC). If so, the purveyors of these arrangements would be required to reveal certain information regarding risks and performance of investments, so that potential buyers would have the capability of making informed decisions. Although the SEC has monitored the viatical industry closely, it has not been successful in obtaining a clear ruling at the federal level that viaticals must meet the legal requirements of securities.

The highest federal court to consider the question has been the United States Court of Appeals for the District of Columbia Circuit in *Securities and Exchange Commission v. Life Partners, Inc.*[54] Life Partners marketed fractions of viatical contracts which allowed small investors to pay as little as a few hundred dollars for a share of a policy.[55] Using financial planners as its agents, Life Partners grew to dominate the market, which attracted the attention of the SEC.[56] Although Life Partners modified its business practices several times, it essentially operated by identifying potential viators, evaluating their medical records to determine degree of risk, purchasing the insurance policies and naming itself as the beneficiary, and then reselling fractions or shares of the policies to investors.[57] When it came under scrutiny of the SEC, Life Partners changed its practice to either list the investors or an escrow agent as the policy owner instead of itself.[58] Under either plan, Life Partners made its profit through fees charged to the investors before the proceeds of the policies were paid out.[59]

The district court agreed with the SEC and held that Life Part-

[53] *Id.* at 224.
[54] 87 F.3d 536 (D.C. Cir. 1996).
[55] *Id.* at 539.
[56] *Id.*
[57] The medical risk evaluations of policy holders were conducted by a physician who was a part owner of Life Partners. *Id.*
[58] *Id.* at 540.
[59] *Id.*

ners was selling securities without a license. However, the court of appeals reversed, after applying the three-pronged test used by the U.S. Supreme Court in *Securities and Exchange Commission v. W.J. Howey Co.*[60] Under this test, an investment contract is deemed to be a security if the investors (1) expect profits from (2) a common enterprise that (3) depends on the efforts of others.[61] Clearly, the investors in the Life Partners viaticals expected profits, clearly theirs was a common enterprise in that their funds were pooled to buy the policies, and they shared any profits or losses after the policy benefits were paid out. However, the court ruled that the third prong of the test was not met, because Life Partners performed no essential entrepreneurial services after the purchase of the contracts.[62] The court reasoned that the profitability of the investment was directly determined by how long a viator lived, not by any actions of Life Partners itself. The court specifically discounted the pre-purchase activities performed by Life Partners (e.g., identification of potential viators, rating of medical risk, negotiation of contract price) as not meeting the intent of the third prong.[63] Thus, the court established a bright-line test in that an investment contract would only be considered a security if, post-purchase, the seller continued to perform some substantial activity that affected the profitability of the arrangement.

The *Life Partners* decision has been widely cited and frequently criticized. Several state appellate courts have considered similar viatical investment plans and ruled that they are securities for the purpose of state securities regulation. In *Joseph v. Viatica Management, L.L.C.*, the Colorado Court of Appeals ruled that the "units" of investment in a viatical fund met the state definition of a security.[64] Viatica Management sold investment units for a minimum price of $25,000.[65] The plan was to pool these monies into multimillion-dollar funds which would then purchase large numbers of viaticated policies.[66] When the return on investment proved to be smaller than promised, a disgruntled investor complained to the state securities commission.[67] Here, the court applied the *Howey* test and found that all three prongs were met. In its analysis of the

60 328 U.S. 293 (1946).
61 *Life Partners*, 87 F.3d at 540.
62 *Id.* at 546.
63 *Id.*
64 55 P.3d 264, 267 (Colo. Ct. App. 2002).
65 *Id.* at 265.
66 *Id.*
67 *Id.* When advances in medical treatment led to longer lives for AIDS patients, the returns on their viatical settlements did not come as quickly as expected. *Id.*

critical third prong, the court distinguished the case from *Life Partners*; it also noted that the reasoning followed in *Life Partners* was unpersuasive.[68] Essentially, the investors in *Life Partners* were sold fractional shares in specific viatical policies; in contrast, Viatica Management sold shares in a fund which then purchased multiple policies.[69] The identification of these policies and the negotiation of the viatical settlements were all done post-investment, or at least were not identified to the potential investors at the time they were making their decision to buy into the fund.[70] In this way, the bright-line test established in *Life Partners* was met because profits were determined by activities carried on post-purchase by the plan sponsors.[71]

In *Siporin v. Carrington*, an Arizona case, the "bright-line" distinction between pre- and post-purchase activities was challenged.[72] Carrington had solicited investors with brochures promising double-digit returns; he also marketed to potential viators through local health service organizations.[73] Carrington did his homework by investigating a number of factors that could affect the outcome of the viatical arrangement.[74] After being given access to medical records, he would contact the viator's physician for an estimation of life expectancy.[75] He also investigated the rating of the life insurance company and determined whether the policy allowed assignment of beneficiaries.[76] Finally, Carrington required that former beneficiaries formally waive their rights under the policy.[77]

The court concluded that the profitability of the viatical investment was directly related to Carrington's pre-purchase activities.[78] The success or failure of the investment was largely determined by his skill in selecting appropriate viators who had policies with strong insurers and whose policies contained the particular clauses that permitted viatication.[79] In applying the *Howey* test and con-

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68 *Id.* at 267.
69 *Id.*
70 *Id.*
71 *Id.*
72 23 P.3d 92 (Ariz. Ct. App. 2001).
73 *Id.* at 93. "In the 'Win/Win Investing' brochure, Carrington suggests returns of from 10% to 11% for policies in which the viator had a projected life expectancy of up to 12 months, to as high as 68% to 70% for policies in which the viator's projected life expectancy was up to 48 months." *Id.* at 94.
74 *Id.* at 93-94.
75 *Id.*
76 *Id.* at 94.
77 *Id.*
78 *Id.* at 98.
79 *Id.* at 99.

cluding that all three prongs were met, the *Siporin* court noted that it was taking a position contrary to that of the *Life Partners* court.[80] Although state courts typically follow the rulings of federal courts, here, the court felt that the rigidity of the *Life Partners* bright-line test undermined the purpose of the securities regulation statutes.[81] In concluding that Carrington's plan constituted the sale of securities, the court stated that "[w]hat truly determines viatical settlement profitability is the realization, over time, of an outcome predicted by the seller through its analysis of the viator's life expectancy, the soundness of the insurer, the actions needed to keep the policy in effect for the original face amount, and the insurer's unconditional liability under the policy's terms."[82] Whether the activities occur before or after the investment is immaterial to the determination that the investment is a form of security transaction.[83]

The rigidity of the *Life Partners* approach has also been rejected by other federal courts. In *SEC v. Tyler*, the U.S. District Court for the Northern District of Texas reasoned that because the defendant performed a post-purchase service when he bought viaticals in his own name and sold fractions to investors, he created a form of liquidity which heightened the value of the investment.[84] If investors wanted to sell their shares, Tyler would either sell them to others or buy them back himself, thus creating an artificial secondary market.[85] Even though the investors may not have been aware of his actions, the court felt that they relied on his description of the investments as being liquid.[86] This was found to be sufficient to pass the third prong of the *Howey* test and supported the court's finding that the viatical investment met the definition of a security.[87]

Despite the group of decisions contrary to *Life Partners*, state courts continue to adopt various positions on whether viatical settlements should be treated as securities. In a recent Ohio decision, *Glick v. Sokol*, the court reverted to the position that "the only variable that can impact the profitability of the viatical settlements at

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80 *Id.* at 98.
81 *Id.*
82 *Id.* at 99.
83 *Id.*
84 No. 3:02-CV-0282-P, 2002 U.S. Dist. LEXIS 2952, at *18-19 (N.D. Tex. Feb. 21, 2002).
85 *Id.* at *6.
86 *Id.*
87 *Id.* at *19.

issue is the timing of the death of the insured."[88] Although this court did not cite the *Life Partners* decision, its reasoning was essentially the same: the value of the investment is determined by the timing of the insured's death, not by any actions taken by the viatical settlement provider or broker.[89]

While courts remain divided on the issue of viaticals as securities, some states have taken legislative or regulatory action to resolve the problem. For example, the Pennsylvania Securities Commission (PSC) has issued a notice that viatical settlements are "investment contracts" and as such are considered to be securities and subject to the regulation of the PSC.[90] Although it noted the *Life Partners* decision to the contrary, the PSC pointed out that a federal case is not automatically binding on state courts.[91] Under PSC regulations, sellers of viatical arrangements are required to be registered in the state as brokers and must disclose all information material to the transaction.[92]

## V. Model Act and Regulation

The National Association of Insurance Commissioners (NAIC) has developed a Viatical Settlements Model Act[93] and Viatical Settlements Model Regulation[94] to guide states in their supervision of the viatical industry. Originally issued in 1993 and 1994 respectively, both models have been extensively amended to reflect the changing characteristics of the industry.

The Model Act provides that a viatical settlement provider or broker must be licensed in the state in which the viator resides, and it gives the state authority to approve the formats of viatical contracts.[95] The content of disclosure statements to the viator is specified in detail and includes warnings that the proceeds of the settlement may be subject to creditor claims and may adversely af-

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88 777 N.E.2d 315, 316 (Ohio Ct. App. 2002).

89 *Id.* at 319. The court reached its decision in spite of its recognition that, by statute, Ohio declared all viatical arrangements to be securities subject to registration under the Ohio Securities Law, effective Oct. 5, 2001. The Glick investment was made in 1998. *Id.* at 316.

90 Securities Commission, *Compliance Notice to the Viatical Industry*, 30 Pa. Bull. 6670 (Dec. 23, 2000) LEXIS.

91 *Id.*

92 *Id.*

93 Viatical Settlements Model Act (National Association of Insurance Commissioners 2001), *at* http://advancedsettlements.net/newsite/compliance/naic.pdf (on file with the New York City Law Review).

94 Viatical Settlements Model Regulation, *supra* note 42.

95 Viatical Settlements Model Act, *supra* note 93, at §§ 3-5.

fect the viator's eligibility for Medicaid and other government benefits.[96] The viator is given a 15-day period within which he or she may rescind the settlement contract after receipt of the payment.[97] If the viator dies within this period, the contract is deemed to be rescinded, the viatical payment must be refunded, and the policy payment is made to the original beneficiary.[98] Viators are also protected from excess intrusiveness by the providers: the Model Act limits visits to once a month if the insured has a life expectancy of less than one year and once in three months if the life expectancy is longer than a year.[99]

The Model Act also includes an extensive section regarding guidelines for advertising of viatical settlements and viatical investment plans.[100] Certain terms are assumed to be false or misleading on their face and are prohibited; these terms include "guaranteed," "no risk," "high yield," and "quick profit."[101] The viatical settlement provider or broker is also required to develop an "antifraud plan," which must be submitted to the state insurance commissioner.[102] The plan must provide for the detection and elimination of fraudulent activities by any personnel involved in the viatical settlement process.[103]

The NAIC Model Regulation includes sample disclosure statements and consumer warnings.[104] It also provides a set of standards for determining reasonable viatical payments. These standards are based on the life expectancy of the insured and range from 50% of policy face value when the insured's life expectancy is greater than 24 months to 80% when life expectancy is less than six months.[105] Among its other protections, the Model Regulation provides the interesting stipulation that "[a] viatical settlement provider shall not knowingly solicit investors who have treated . . . the illness of the insured whose coverage would be the subject of the investment."[106]

Thirty-seven states have adopted some version of the NAIC models. On July 4, 2002, Pennsylvania passed its Viatical Settle-

96 *Id.* at § 8.
97 *Id.*
98 *Id.* at § 9.
99 *Id.*
100 *Id.* at § 11.
101 *Id.*
102 *Id.* at § 12.
103 *Id.*
104 VIATICAL SETTLEMENTS MODEL REGULATION, *supra* note 42, at App. A.
105 *Id.* at § 5.
106 *Id.* at § 7.

ments Act, which became effective in January 2003.[107] Although largely drawn from the NAIC Model Act, the Pennsylvania statute omitted the large section in the Model Act that provided guidelines for advertising viatical settlements and investments. The legislators may have felt that the issue would be adequately covered by the state securities commission in its oversight of viatical investment plans. However, clear legislative direction in this area would have been advisable, as misleading advertising has been at the center of much of the fraudulent activity in the viatical industry. Perhaps the forthcoming regulations will address this problem.

## Conclusion

An elderly person who is considering involvement in a viatical settlement, either as a viator or an investor, must make a cautious appraisal of the benefits and risks. For the viator, the cash received from a previously hidden asset may help pay for medication, assisted living or one last vacation. But the viator must be careful that he or she is receiving reasonable value for the policy and that the viatical "deal" is better than alternatives of tapping an accelerated death benefit or simply borrowing against the policy. Individual circumstances also must be considered, such as the desire to provide for beneficiaries, as well as the potential impact on Medicaid eligibility.

For the potential investor, the key word is caution. Viatical plans are not low risk and a positive rate of return is not guaranteed. What looks like a simple way to make money, and maybe even help a fellow human being in need, is really a complex financial transaction designed to enrich many parties before the individual investor gets his or her return. Only those wealthy enough to afford speculating with their funds should even consider viatical investments.

In spite of these limitations, the viatical industry continues to grow and is apparently fulfilling multiple needs among the terminally and chronically ill. It is hoped that the heightened surveillance from state regulatory agencies will reduce the more flagrant abuses and allow the ill and the elderly to benefit from the positive features of viatical arrangements.

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[107] Viatical Settlements Act, 40 PA. CONS. STAT. §§ 626.1-17 (2003).