

Florida Office of Insurance Regulation

Report of Commissioner, Kevin M. McCarty



STRANGER-ORIGINATED LIFE INSURANCE ("STOLI") AND THE USE OF FRAUDULENT ACTIVITY TO CIRCUMVENT THE INTENT OF FLORIDA'S INSURABLE INTEREST LAW

January 2009

Seniors May Lose the Ability to Purchase Additional Life Insurance

An individual has only a finite amount of "insurance capacity" on his or her life, and insurers may refuse to write additional insurance. Once a senior has life insurance on his or her life and then sells the policy, the senior may be unable to obtain more life insurance should a legitimate need for life insurance arise. At the STOLI hearing, Scott Berlin, Senior Vice-President at New York Life Insurance Company commented on this issue and stated:

One of the things that's not well understood among the senior community is that there's a certain amount of insurance you can get, that you can qualify for... You can't -- it's not just you can get as much as you want. And once you've bought that insurance and given it to somebody else, it doesn't free up that capacity for you to get more. There's only a certain amount of insurable interest on you based on your current status.²⁸

STOLI promoters often do not discuss the insurance capacity issue with the seniors that they are trying to induce into applying for multi-million dollar life insurance policies. Bob Rubin, on behalf of AALU, addressed the issue in his comments at the hearing and stated:

[T]he consumer thinks that he's taking care of his estate planning, business succession plan, or accomplished some sort of estate planning...the reality in most cases is exactly the opposite...he now has a significant life insurance policy on his life, usually up to the maximum allowed or more than the maximum allowed by a particular life insurance company's financial underwriting guidelines. Since he has now used up his capacity, his insurance capacity, he'll be hard-pressed to purchase any more life insurance that will truly benefit his family for whatever the future circumstances might dictate.²⁹

Attorney Joy Ryan representing insurer MetLife echoed the sentiments of those expressed by New York Life regarding the dangers to consumers presented by STOLI arrangements. Ms. Ryan stated, "consumers may not be aware that participating in these types of arrangements may exhaust their life insurance purchasing capability..."³⁰ As Stephan R. Leimberg, Esq. has reported, "[T]his

²⁸ Transcript of Public Hearing - Appendix I, pp. 38 – 39.

²⁹ Transcript of Public Hearing - Appendix I, pp. 104 –105.

³⁰ Transcript of Public Hearing - Appendix I, p. 136.

consequences of participating in a STOLI transaction.³⁵ The Office is not aware of any response to the letter from the Treasury Department.

Bob Rubin, on behalf of the Association for Advanced Life Underwriting (“AALU”), addressed the tax liability issue and stated:

Tax issues are glossed over. Most of the time these deals involve quite a bit of premium to be paid up front. Since the premium is borrowed, a substantial debt is unsecured. Since it's a non-recourse type of finance, what happens in two years when the policy is sold or given up or whatever and that debt is discharged? I'm not a CPA, but is that a discharge of debt issue?³⁶

Currently the proceeds to the beneficiary of a life insurance policy are non-taxable. In response to Commissioner McCarty’s question of the potential of putting life insurance policies’ favorable tax treatment in jeopardy due to STOLI profiteers, Scott Berlin of New York life responded:

Well, I think that there is the risk that the IRS could look in and say, you know, life insurance isn't providing the purpose that it once did. It's now a vehicle for speculators to get rich. It's not for people to protect their families and their businesses so we're going to change the tax law. And I think that that would be a very bad outcome for both individuals and the industry.³⁷

³⁵ Id.
³⁶ Transcript of Public Hearing - Appendix I, pp. 105 – 106.
³⁷ Transcript of Public Hearing - Appendix I, pp. 31– 32.

Seniors Risk Substantial Liability if their Life Insurance Policy is Rescinded

The relief sought by three multi-million dollar federal lawsuits recently filed in Florida by several life insurers include rescission of alleged STOLI policies because the true nature of the transactions were allegedly misrepresented.³⁸ Seniors that are lured into participating in STOLI schemes for financial gain are at risk of owing money when the fraudulent scheme is uncovered. As

Bob Rubin stated at the public hearing:

The rescission of the policy should be the one issue that should really scare the consumer from never going near one of these transactions. Assume for a minute that the policy is rescinded. Big debt was incurred. The consumer received some money up front. He signed an indemnification clause. And further assume the life insurance company rescinds the policy. It wants the commissions it paid back, that same commission that was used to make the deal work in the first place. Guess who wants to be made whole? The promoter. Guess where they're going to try to get their money back, besides obviously the agent? The consumer. He signed an indemnification to make whole if something goes wrong. This is not a good place for the average consumer to be.³⁹

The “free insurance” that may have been part of the incentive to participate in the STOLI scheme may be voided if the policy is rescinded based on fraud.

³⁸ See AXA Equitable Life Insurance Company vs. Infinity Financial Group, LLC, et al., Case No.: 08-cv-80611, filed June 6, 2008 (case involves alleged STOLI transactions on 5 life insurance policies with a total face value of \$73 million). The AXA case is currently set for trial in July of 2009 although a joint motion to stay the lawsuit was filed by the Plaintiff and some of the defendants and granted by the federal judge until November 3, 2008 to narrow or resolve issues in the case); American General Life Insurance Company vs. Steven Brasner, Infinity Financial Group, LLC, et al., Case No.:08-cv-80855, filed August 4, 2008 (case involves alleged STOLI transactions on 2 policies with a \$10 million total face value); West Coast Life Insurance vs. Life Brokerage Partners, LLC, et al., Case No.: 08-cv-80897, filed August 13, 2008 (case involves alleged STOLI transactions on 9 policies with a total face value of \$50 million).

³⁹ Transcript of Public Hearing - Appendix I, pp. 107 – 108.

Proliferation of STOLI may cause increase in life insurance rates

Based on the testimony presented at the hearing, STOLI transactions may lead to an increase in life insurance rates. Scott Berlin, Senior Vice-President at New York Life, responsible for the individual life business, raised concerns regarding the potential for an increase in life insurance rates due to the proliferation of STOLI:

And so I think that the victim in the long run is the purchasers of life insurance, for legitimate reasons. So some people can get rich today, there is that potential, there is the possibility of that potential today or at least it appears that way. But the ultimate result five years from now will be that the price of life insurance will go up, that arbitrage opportunity will get closed, and people who want to buy life insurance for legitimate reasons like estate planning and protecting their families will have to pay more for that insurance.⁴⁰

Bob Rubin, Senior Vice-President and insurance advisor with Wachovia Insurance Services, testified on behalf of the Association for Advanced Life Underwriting (“AALU”). Mr. Rubin stated that he has been in the insurance business since 1985 and has lived in South Florida for over 35 years. He further stated that STOLI transactions are “reducing the availability of life insurance of people over the age of 70. There's less companies that are offering them. And the ones that are, they're charging more for it, making it harder to get.”⁴¹

In response to Commissioner McCarty’s question about the affect on price already seen in the market, Mr. Rubin responded:

Everybody reprices their products. I mean, company [sic] always reprice products, but they generally used to go down. Now they go up. You know, it's one of the few times that insurance costs have actually gone up.⁴²

⁴⁰ Transcript of Public Hearing - Appendix I, p. 32.

⁴¹ Transcript of Public Hearing - Appendix I, p. 110.

⁴² Transcript of Public Hearing - Appendix I, p. 110.