Robin & Peter on LIFE SETTLEMENTS

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Setting the Record Straight on Kramer

In a recent decision, the New York Court of Appeals ruled that an insured could buy an insurance policy with the intent of transferring the policy to a third party without insurable interest. Although this ruling is important, **there are some who mistakenly believe that the court has somehow endorsed STOLI** (Stranger Originated Life Insurance).

First, here is some background on the case. Kramer vs. Phoenix, et al., involves a multitude of brokers, insurers, trusts, banks, and investors. According to the pleadings in the case, around 2005, Mr. Kramer bought several large policies with premiums supplied by investors and immediately transferred these policies to trusts that were set up ultimately for benefit of the investors. When Mr. Kramer died a few years later, Mrs. Kramer, his widow, sued the investors and the insurers saying that she is entitled to the death proceeds because the STOLI transactions lacked insurable interest and therefore the transfer of the policies to the trusts was invalid. The upshot is that Mrs. Kramer, the insurers, the brokers, the investors, and other intermediary parties are all suing each other and cross-claiming and counterclaiming for the death proceeds, rescission of the policies, return of commissions, breach of agent/broker contracts, etc.

Prior to the case coming to trial, the lower court asked the NY Court of Appeals to clarify a single point of New York law: whether intent to immediately transfer a policy could be considered in determining if insurable interest existed at the time the policy was issued. The appeals court held that the New York law, which is similar to many other states, does not have any intent requirement. The statute quite clearly automatically gives an insured an insurable interest in their own life and intent is irrelevant.

The case is important because it protects consumers as well as the life settlement industry. The decision means that a policy owner does not have to worry about the insurance company challenging the validity of an insurance policy based on intent after the insured's death. Opening up the issue of intent would create uncertainty for beneficiaries and be difficult or impossible to prove. The ruling means that insurers cannot use intent to resell a policy as an argument to rescind an insurance policy bought

by an insured on their own life no matter who they subsequently make the owner or beneficiary.

Some misguided souls have interpreted the case to be an endorsement of STOLI, but that is just NOT accurate. In 2009, New York enacted a life settlement industry sponsored life settlement law that prohibits the Kramer type transfer of a life insurance policy within two years of issue. Additionally, the Kramer ruling only applies to a policy originated by the insured himself or herself, not by some third party. Finally, even if the decision does, in theory, permit an insured to speculate on their own life by buying a policy intending to sell it two years later, such a strategy makes no economic sense. With the longer life expectancy tables now in use, an insured would have to suffer a very substantial decline in health for the policy to have value as a life settlement after only two years. Advising a client to speculate that way would be extremely foolhardy.

The Kramer decision upholds the rights of insureds to do what they wish with their insurance policies and prevents undermining the certainty that beneficiaries of life insurance policies should be entitled to. STOLI, on the other hand, remains dead and that is as it should be.

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