

Robin & Peter on LIFE SETTLEMENTS



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Another Nail in STOLI's Coffin

In *PHL Variable vs. Price Dawe 2006 Insurance Trust Insurance Company*, the Delaware Supreme Court recently ruled that a life insurance policy issued to someone without insurable interest could be rescinded by the insurer even after the expiration of the two-year contestability period. Except for a few outliers with unique insurable interest statutes, like New York and Michigan, this is the law in most states and is consistent with the thinking of most legal scholars.

The court ruled that a policy issued to someone without insurable interest is an illegal wagering contract and is void *ab initio* (from inception). Since the contract itself is void, provisions like the contestability clause are also invalid and unenforceable. As a result, Stranger Originated Life Insurance (STOLI) policies are therefore void and illegal and can be rescinded without regard to the contestability period.

Even more significantly, the decision also confirmed that an insured has an insurable interest in their own life and may purchase and later sell that policy in a life settlement transaction. This applies even if the insured intends to sell the policy, provided that the sale has not been pre-arranged and the insured is not simply acting as a straw man to get the policy into the hands of someone without insurable interest. The court held that the intent of the insured should not be considered, but rather, the focus should be on whether a pre-arrangement existed at the time of issue and who paid the premium.

The decision, that intent to sell would not be a violation of insurable interest laws, is an important victory for consumers and the life settlement industry. It means that consumers and investors can buy a policy and be confident that many years later the insurer cannot challenge a policy's validity based on the insured's state of mind at the time of issue.

The life settlement industry applauds the ruling as the court distinguished STOLI from legitimate life settlement transactions. The court said:

"Over the last two decades, however, an active secondary market for life insurance, sometimes referred to as the life settlement industry, has emerged. This secondary market allows policy holders who no longer need

life insurance to receive necessary cash during their lifetimes. The market provides a favorable alternative to allowing a policy to lapse, or receiving only the cash surrender value. The secondary market for life insurance is perfectly legal."

As this ruling so clearly demonstrates, legitimate life settlements continue to be an important and valuable option for consumers and one that should not be overlooked when your clients no longer want, need or can afford a policy.

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