STATE DEPARTMENT OF FINANCE WARNS AGAINST VIATIONAL FRAUDS

Risky ‘death futures’ draw warning from securities regulators, congressional scrutiny; High commissions entice independent insurance agents to sell viatical settlements.

Boise (February 26, 2002) – Citing deceptive marketing practices and numerous instances of fraud, Gavin Gee, Director of the Idaho Department of Finance warned Tuesday that investors should not be misled by claims that viatical settlements – interests in the death benefits of terminally ill or older Americans – offer safe, guaranteed returns like certificates of deposit. Noting February is Idaho Financial Literacy Month, Gee encouraged investors to become educated about the particulars of these investments before handing over their money.

Tuesday’s warning came as the Subcommittee on Oversight and Investigations of the House Financial Services Committee held a hearing into viatical investments. The viatical industry began in the early 1990s as a way to help the terminally ill. In a typical transaction, the person holding a life insurance policy sells it to a third party “broker” in return for a portion of the death benefit. The broker then sells shares of the policy to investors, who collect a share of the death benefit from the broker when the original policyholder dies.

Securities regulators from 18 states report bringing actions on behalf of thousands of investors nationwide who were defrauded of more than $400 million over the past three years. Gee pointed to low interest rates and aggressive marketing as fueling a potential rise in viatical contract sales.

In many cases, independent insurance agents have been recruited to sell viaticals, according to Gee.

“Viaticals contracts are legitimate products, but state securities regulators have two concerns,” says Gee. “First, we’re concerned that the inherent risk of viatical investments – gambling on when someone will die – aren’t being adequately disclosed, and second, many investors have been outright defrauded by some viatical companies or their sales agents.”

This second concern surfaced in a case brought by the Department against Personal Choice Opportunities (PCO) and several associated entities and individuals. The Department’s lawsuit alleges that the defendants solicited Idaho residents to purchase securities in the form of loan transactions. Investors lent money to PCO in order for PCO to purchase the benefits of life insurance policies from terminally ill individuals. Investors were promised returns on their investments of 21-25%.
The complaint further alleges that instead of being used to purchase insurance policies, most of the money was diverted to some of the defendants. Idaho investments were approximately $3.4 million of the more than $60 million taken nationwide. A receiver has been appointed and continues to work toward recovering investor money.

Fraud in the marketing of viaticals is well documented. For example, a viatical settlement company known as American Benefits Services, Inc., offered investors in Texas and other states a 42 percent rate of return, with 15 percent guaranteed. Over 3,000 people invested $117 million. Investor funds collected by American Benefits were forwarded to another viatical settlement company, Financial Federated Title & Trust, which spent only $6 million to buy interests in actual life insurance policies. Regulators say the rest was diverted for the personal benefit of company organizers, including the purchase of a helicopter, boats, luxury cars (including four Aston Martins), luxury homes and large salaries.

“There’s an old saying, ‘The only sure things in life are death and taxes’ and viatical salesmen play on that,” said Gee. “They tell investors that because death is a sure thing, viaticals are too. But the only sure thing with viaticals are the large commissions some brokers get, making it even tougher for investors to get the returns they’re promised.”

In Vermont, state regulators allege that Mutual Benefits Corporation, a large nationwide seller of viatical policies, concealed insurance fraud and misrepresented the life expectancies on dozens of policies sold to investors. Mutual Benefits marketed viatical settlements as safe investments with “no risk of loss.” In reality, only 8 percent of Mutual Benefit’s policies posted returns within the range that was advertised, according to Vermont regulators.

Before making any investment, Gee urges investors to ask the following questions:

• Has the seller given you written information that fully explains the investment? Make sure you get proper written information, such as a prospectus or offering circular, before you buy. The documentation should contain enough clear and accurate information to allow you or your financial adviser to evaluate and verify the particulars of the investment. Watch for jargon that sounds sophisticated but makes no sense.

• Are claims made for the investment realistic? Some things really are too good to be true. Use common sense and get a professional, third-party opinion when presented with investment opportunities that seem to offer unusually high returns in comparison to other investment options. Pie-in-the-sky promises often signal investment fraud.

• Does the investment meet your personal investment goals? Whether you are investing for long-term growth, investment income or other reasons, an investment should match your own investment goals.

The Department urges Idaho residents to make sure that the investments and investment professionals with whom they deal are registered. Investors can contact the Department at (208) 332-8004 or toll free within Idaho at 888-346-3378.