

Typically life insurance policies are something you purchase so your family will have some money after you die. This isn't the only way insurance policies can be used. You can sell your policy to someone else before you die. Or you can purchase someone else's policy as an investment.

Whether you are selling your own policy or buying someone else's policy, you are involved in a viatical settlement. And no matter which side of the transaction you might be considering, you need to know how to protect yourself and your investment.

Cashing in Your Life Insurance Policy

You may be desperate for cash, perhaps to pay for medical or long-term care expenses. If you have a life insurance policy that you are tempted to convert into cash, explore your options before you decide. One option is to sell your policy for immediate cash to a viatical settlement provider or broker. The settlement provider pays you a discounted rate, collects a commission, and then finds an investor to purchase the policy and pick up your premiums. When you die, the investor collects your death benefits.

Check with your insurance agent or company for how much cash value you have in your policy. Your policy may provide for accelerated benefits. This way you would get some of the death benefit before you die and still keep the policy in force for your beneficiaries. You might also be able to use the policy as security for a loan.

The National Association of Insurance Commissioners (NAIC) offers these suggestions before you sell your policy to a third party.

- **Comparison shop.** Get quotes from several viatical providers to make sure you have a competitive offer.
- **Be sure you understand how much cash you will get.** You will get far less than the face value or even cash value of your policy.
- **Find out the tax implications.** Not all proceeds from the sale of your life insurance policy are tax free. Get independent advice from your financial advisor, estate planning lawyer, or tax consultant before making the sale.
- **Know that your creditors could claim your cash settlement.**
- **Find out if you will lose any public assistance benefits such as Medicaid if you get a cash settlement.**
- **Understand that the buyer of your policy can periodically ask you about your health status.** The buyer is required to give you a privacy notice outlining who will get this personal information. Be sure to read it.
- **Check all application forms for accuracy, especially your medical history.** All questions must be answered truthfully and completely.
- **Make sure the viatical settlement provider agrees to put your settlement proceeds into an independent escrow account.** This protects your funds during the transfer.
- **Find out if you have the right to change your mind about the settlement AFTER you get the money.** If so, how many days do you have to reconsider and return the money?
- **Ask how much the settlement provider is making in fees and commissions.**
- **Be aware that you may need to get permission from your employer if you obtained your life insurance policy through work.**

- **Independently verify that the viatical provider is licensed to do this work in your state!**

Investing in Someone Else's Life Insurance

When you buy a viatical, you're purchasing the life insurance policy of perhaps a terminally ill person at a discounted price from a viatical settlement broker. As an investor you'll get the full face value of the policy when the person dies. Brokers also sell a spin-off of viatical settlements—life or senior settlements—in which the investor is offered the life insurance policy of an older, healthy person. The investors are told they are helping older people stay financially solvent in their golden years. The pitch is based on a high rate of return—often 20 to 40 percent—and a humanitarian opportunity to help a sick person, a combination appealing to older investors.

James thought he was doing the right thing when he invested \$50,000 in a viatical contract. The retired investor was told he would be making a humanitarian investment by purchasing the life insurance policy of a terminally ill person and that he could expect a large profit for himself. But the insured person wasn't really sick at all and James was forced to pay the policy premiums to avoid losing his investment.

Pitfalls

Viaticals can end up costing investors a lot of money. The North American Securities Administrators Association (NASAA) calls viaticals one of the top ten investment scams. According to Joseph Borg, former president of NASAA, and director of the Alabama Securities Commission, securities regulators are "concerned that the inherent risks 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."

A Florida Grand Jury in 2000 found as much as 40-50 percent of the life insurance policies handled by viatical settlement providers may have been procured by fraud. The Securities and Exchange Commission (SEC) has taken action against one company that allegedly defrauded 30,000 investors of \$1 billion.

Here are a few of the ways people can lose money:

- With improved medical care, the ill or older person may live longer than expected. As the new owner of the policy, you have to pay the premiums to keep the policy in force. You tie up your money longer, and your profit declines the longer the person lives.
- Sometimes the insured person is not ill at all, so the investor will need to make insurance payments—sometimes for years—or the investment is lost.
- The insured person may have purchased the life insurance through fraud, and the insurance company will later refuse to pay the settlement.
- The insurance company or viatical settlement company may go out of business — along with your invested money.
- Some brokers have sold the same policy to multiple investors.
- The insured's heirs may challenge changes made to the policy.

Protect Yourself

It is important to learn all you can about a viatical before you invest. Failure to thoroughly research the investment could result in financial disaster. Some questions to ask include:

- Is this investment right for you based on your age, financial status and other personal circumstances? If the viator lives longer than expected, your investment dollars will be tied up for a longer time than expected, and you'll have to keep paying the policy premiums so the policy doesn't lapse.
- Is the viatical investment defined as a security in your state? Check with your state securities regulator to see if it should be—and is registered—and if the broker is licensed. In some states, viaticals are regulated as insurance products; in other states they are not regulated at all.
- Who holds the responsibility to pay policy premiums, and for how long? A lapsed policy means that you could lose your entire investment.
- What control, if any, do you retain over your investment?

- What financial information will the provider disclose about its history? If the viatical settlement provider and/or the insurance company goes bankrupt, you could lose or tie up your investment dollars indefinitely.

Your To-Do List:

- Check on any viatical offer and broker** with your state insurance or securities regulator whether you are considering selling your policy or investing in someone else's.
 - State securities regulators: www.nasaa.org and click "Contact your regulator" or call 1-888-OUR-AARP and ask for the phone number of the securities regulator for your state.
 - State insurance regulators: www.naic.org.
- Read Sid Kirshheimer's "Scam Alert"** in the *AARP Bulletin* about investors who have lost on viatical investments, www.aarp.org/money/consumer/articles/buyingthisinsurance.html.
- Study the questions** the California Department of Corporations suggests you ask before investing in a viatical settlement, www.corp.ca.gov/Education_Outreach/fraud/faq.asp.
- Heed the Michigan Department of Consumer and Industry Services' warning:** "Do not invest in viatical settlements until you have read the following information." (Adobe Acrobat is required.) www.michigan.gov/documents/cis_ofis_fispub_0562_25009_7.pdf.
- Share a copy of this Money Matters Tip Sheet with a friend. Order more copies at www.aarp.org/orderfinancialpubs.

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