NOTE

WANTED DEAD, NOT ALIVE: WHY CANADA SHOULD ALLOW LIFE SETTLEMENTS

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I. INTRODUCTION

An Australian man named David Walsh made his fortune as a card-counting blackjack player, but his most controversial bet took place away from a casino.[1] In 2009, he made a simple bet with Christian Boltanski, a sixty-five-year-old French artist: Walsh agreed to buy the rights to a piece of Boltanski's work, with the payments arranged as a monthly stipend until Boltanski's death.[2] Walsh ran the numbers and concluded that the market value of the purchased work would be paid off after eight years of these monthly payments.[3] This meant that if Boltanski died within eight years, the payments would stop and Walsh would end up paying less than the worth of the art; if Boltanski lived for longer than eight years, however, Walsh would need to continue making payments even after he paid off the market price of the artwork.[4] In effect, Walsh made a bet on the life of Boltanski.[5]

Although Walsh's gamble on Boltanski's life may seem uniquely macabre, similar bets of a different name are made every day in many countries across the globe.[6] These transactions are known as life settlements and typically work as follows: an elderly or ill patient who owns life insurance sells the policy for much-needed cash, always at a

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1. Richard Flanagan, *Tasmanian Devil: A Master Gambler and His High-Stakes Museum*, NEW YORKER (Jan. 21, 2013), http://archives.newyorker.com/?i=2013-01-21#folio=050.

2. *Australian David Walsh Gambles on Artist Christian Boltanski's Life*, NEWS.COM.AU (Nov. 25, 2009, 6:11 AM), http://www.news.com.au/national-old/australian-david-walsh-gambles-on-artist-christian-boltanskis-life/story-e6frfkvr-1225803521408.

3. Flanagan, *supra* note 1.

4. *Id.*

5. *Id.*

6. *See* James Vlahos, *Are You Worth More Dead than Alive?*, N.Y. TIMES MAG. (Aug. 10, 2012), http://www.nytimes.com/2012/08/12/magazine/are-you-worth-more-dead-than-alive.html?.

discount of the payout value of the policy; the buyer continues paying the premiums to the insurance company, keeping the policy in good standing; and when the seller dies, the insurance company relinquishes the payout to the new buyer of the policy.[7] Because the buyer commits to continue paying premiums for as long as the seller lives, there is a concrete financial interest in the death of the seller—if he lives too long, the premium payments needed to maintain the validity of the policy will consume the buyer's profits in the transaction.[8] Because of this incentive system, investors seek to accurately gauge the life expectancy of the sellers, usually by enlisting the help of independent doctors who examine sellers and relevant medical records while also continuing to monitor their health until death.[9]

This Note will focus on the life-settlement market in Canada, arguing that Canada should abolish the laws prohibiting the resale of life insurance. This change will improve the flexibility available to insureds, better respect the property rights that arise from the significant investment of life-insurance enrollment, and ensure uniformity in the country's insurance laws. Currently, most Canadian provinces prevent life settlements because they continue to uphold a law that prevents anyone other than a licensed insurer or his agent from trafficking in life-insurance policies, thereby keeping the nonlicensed life-settlement brokers from operating.[10] This law, enacted in the aftermath of the Great Depression, was meant to achieve three goals: help support insurance companies struggling with the Depression by eliminating competition from unlicensed sources; protect vulnerable consumers; and promote uniformity among the provinces.[11] Any effect on the life-settlement practice is purely coincidental, as this antitrafficking law precedes the invention of life settlements by almost fifty years.[12] This antitrafficking law has outlived its usefulness in the contemporary life-insurance market.

Additionally, Canada still maintains the insurable-interest doctrine, the legal principle developed in eighteenth century England that requires the buyer of an insurance policy to hold an interest in the person or object insured in order to be valid.[13] While this legal principle re-

7. Life Partners, Inc. v. Morrison, 484 F.3d 284, 287 (4th Cir. 2007); Kelly J. Bozanic, *An Investment to Die for: From Life Insurance to Death Bonds, the Evolution and Legality of the Life Settlement Industry*, 113 PENN ST. L. REV. 229, 233–34 (2008).

8. *See Life Partners*, 484 F.3d at 287.

9. *Id.*

10. CANADIAN CTR. FOR ELDER LAW STUDIES, B.C. LAW INST., STUDY PAPER ON VIATICAL SETTLEMENTS 11 (2006) [hereinafter STUDY PAPER ON VIATICAL SETTLEMENTS].

11. *Id.* at 12–15.

12. *Id.* at 12.

13. CRAIG BROWN & JULIO MENEZES, INSURANCE LAW IN CANADA 65–66 (2d ed. 1991).

mains in effect, it does not serve to prevent life-settlements in Canadian provinces other than Manitoba, as non-Manitoban Canadian courts require the presence of an insurable interest only at the start of the life-insurance contract and not at the time of death; the lack of an insurance interest upon the resale of the insurance to an investor does not therefore void the contract.[14] Under Manitoban law, though, a life-insurance policyholder has a special judicial recourse to cancel policies where an insurable interest no longer exists.[15] Canada upholds the insurable-interest doctrine for three main reasons: first, the insurable-interest doctrine discourages wagering; second, it limits indemnification to the amount lost, thereby preventing windfalls; and third, it removes the moral hazard of standing to benefit from the loss of a life.[16] All three rationales lose their importance in the face of the modern life-insurance industry.

Canada should remove these twin obstacles of the antitrafficking law and the Manitoban insurable-interest requirement in order to allow for life settlements. This change would better serve the country by giving its citizens better control over their own finances, more accurately recognizing the property rights of life-insurance owners, and promoting uniformity throughout the provinces. Canada should also create a new regulatory agency in the model of Australian Prudential Regulation Authority to administer and oversee the new secondary market for life insurance.

Part II of this Note will trace the rise of the life-settlement industry from its birth during the U.S. AIDS crisis in the 1980s through its brief subsequent decline up until the present global phenomenon. It will define the terms and mechanics of a life-settlement transaction before shifting to the history of the insurable-interest doctrine in England and the countries that share her legal tradition. Part II will culminate in an overview of the current state of the law in Canada, with a comparison to Australia's divergent approach. Part III will describe why Canada would be better served by eliminating its antitrafficking law and insurable-interest requirement and will analyze how Canada may implement such a change. Last, Part IV will conclude by examining the broader implications of eliminating the antitrafficking law and the insurable-interest doctrine in Canada.

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14. STUDY PAPER ON VIATICAL SETTLEMENTS, *supra* note 10, at 16–17.

15. *Id.* at 17.

16. *Id.* at 14–17.

II. BACKGROUND

A. *Development of the Life-Settlement Industry*

Of all the far-reaching implications of the AIDS crisis in America during the 1980s, perhaps the least predictable outcome was the quiet revolution in life-insurance practice that resulted in what eventually became known as life settlements.[17] The rise of AIDS prevented many of its sufferers from working and required experimental—and often very expensive—medications and treatments.[18] Sadly, even with these treatments, the life expectancy for an AIDS patient was extremely short.[19] This combination of crushing financial pressures and predictably short life expectancies birthed a new market for life insurance, creating a new investment product referred to as a viatical settlement.[20] Today, the term viatical settlement is used to refer to the sale of life-insurance policies of those people with a life expectancy of less than two years, while life settlement is the term for the negotiation of policies owned by those expected to live longer than two years.[21] For the ease of understanding, this Note will use the term life settlements to refer to both viatical and life settlements.

While the nascent industry was limited to insurance policies owned by individuals stricken with AIDS, it did not take long for the idea of reselling life insurance to spread.[22] Only a few short years passed until treatments for AIDS progressed to the point where patients were not usually in danger of dying only months after diagnosis; there was even speculation that medical researchers would soon develop a cure for the disease.[23] This welcomed medical advancement was at the same time "a severe blow" to the fledgling life-settlement industry.[24] The industry responded by diversifying beyond AIDS patients, with investors expanding their focus to include those with such diseases as Alzheimer's, cancer, advanced heart disease, and Lou Gehrig's disease.[25] This ex-

17. Susan Lorde Martin, *Betting on the Lives of Strangers: Life Settlements, STOLI, and Securitization*, 13 U. PA. J. BUS. L. 173, 184–86 (2010).

18. *Id.*

19. *Life Settlement History*, LIFE INS. SETTLEMENT ASS'N, http://www.lisa.org/content/51/life-settlement-history.aspx (last visited Feb. 18, 2014).

20. Life Partners, Inc. v. Morrison, 484 F.3d 284, 287 (4th Cir. 2007).

21. LIFE SETTLEMENTS TASK FORCE, STAFF REPORT TO THE UNITED STATES SECURITIES AND EXCHANGE COMMISSION 4 (2010), *available at* http://www.sec.gov/news/studies/2010/lifesettlements-report.pdf.

22. Martin, *supra* note 17, at 185.

23. Carl T. Hall, *Viatical Firm's Stock Hit Hard*, S.F. CHRON. (July 18, 1996, 4:00 AM), http://www.sfgate.com/bayarea/article/Viatical-Firm-s-Stock-Hit-Hard-2974339.php.

24. Martin, *supra* note 17, at 185.

25. David W. Dunlap, *AIDS Drugs Alter an Industry's Math; Recalculating Death-Benefit*

pansion of the industry in the United States was swift, growing from an estimated $5 million in life-insurance value sold to buyers in 1989 to a total of $200 million by 1998.[26] Eventually, the industry expanded to include elderly sellers of life-insurance policies who were not terminally ill at all,[27] leading to an industry worth an estimated $18 billion in the United States by 2008.[28]

Like most financial instruments, the life-settlement industry stagnated during the recent global recession.[29] Even so, the total value of the industry in the United States is projected to grow to $148 billion by 2019, due to both the intense interest of investors and the willingness of seemingly ever-increasing numbers of policyholders to sell.[30] On the one hand, investors grew attracted to life settlements precisely because of their uniqueness: these investments are not correlated to the traditional markets of stocks, bonds, and commodities, allowing for a truer diversification of portfolios.[31] On the other hand, policyholders gained a financial incentive to sell their life insurance if they were unable to continue making premium payments.[32] The price policyholders could command from investors looking to purchase a life settlement was greater than the amount they stood to earn from collecting the cash-surrender value of the policy from the insurance companies.[33] The underlying appeal for both buyers and sellers seems to have only strengthened in the aftermath of the global financial crisis of 2008. Both the push from policyholders and the pull from investors were strengthened, as many elderly policyholders faced increased financial pressures due to dramatic losses in their retirement savings[34] and investors became increasingly aware of the high-level of correlation between traditional in-

Deals, N.Y. TIMES, July 30, 1996, http://www.nytimes.com/1996/07/30/business/aids-drugs-alter-an-industry-s-math-recalculating-death-benefit-deals.html.

26. Life Partners, Inc. v. Morrison, 484 F.3d 284, 288 (4th Cir. 2007).

27. Martin, *supra* note 17, at 186.

28. *Id.* at 189.

29. Leslie Scism, *Ruling Is Defeat for Death-Bet Investors*, WALL ST. J., Sept. 26, 2011, http://online.wsj.com/article/SB10001424052970204010604576592780764849782.html ("The industry, like many financial markets, froze in 2008.").

30. Vlahos, *supra* note 6. Some estimates expect the worth of the U.S. life-settlement market to reach $160 billion by the year 2030. *Life Partners*, 484 F.3d at 288.

31. *See* Tara Perkins, *Manulife Unit Battles U.S. 'Life Settlements' Industry*, GLOBE & MAIL (Aug. 23, 2012, 4:56 PM), http://www.theglobeandmail.com/globe-investor/manulife-unit-battles-us-life-settlements-industry/article573948.

32. *See id.*

33. *See id.*

34. *See Betting on Death in the Life Settlement Market: What's at Stake for Seniors?: Hearing Before the S. Spec. Comm. on Aging*, 111th Cong. 1–3 (2009) (opening statement of Sen. Herb Kohl, Chairman, S. Spec. Comm. on Aging).

vestment instruments.[35]

The expansion of the industry also motivated a change in name.[36] The term "viatical" derives from the Latin word *viaticum*, meaning provisions for a journey.[37] This euphemistic name, even as it highlighted the benefits that would accrue to the seller, was considered to be too "ghoulish" for the fledgling industry, with the provisions in this case referring to the settlement money that would allow an AIDS sufferer to pay for his needs during the journey of his final months before death.[38] Instead, the industry settled on the term "life settlement."[39]

Two specialized applications of the normal life-settlement process deserve particular mention. The first is the operation known as stranger-oriented life insurance (STOLI).[40] A STOLI action differs from a typical life-settlement transaction in how the policy is acquired: an investor convinces people, usually senior citizens, to take out life-insurance policies that they would not otherwise have purchased, with the intention of later selling the policies to the investor.[41] Investors have induced these senior citizens to agree to purchase insurance policies by promising free insurance, money, or gifts.[42] This is opposed to the normal life-settlement transaction, in which the policyholders acquire the policies for their own uses, deciding only later to sell their interests in the insurance.[43] The second is the securitization of life settlements, the most recent development in this narrative.[44] This process occurs when investors—usually investment banks—buy large numbers of life settlements, earning the right to payments upon death of the insured.[45] The investors pool hundreds or thousands of different life set-

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35. Bilkan Erkmen, *On Life Settlement Pricing*, 4 MICH. J. BUS. 71, 72 (2011) (describing the realization of many investors of the high correlation of traditional investment instruments during the mortgage-backed-securities crisis of 2007).

36. *See* Martin, *supra* note 17, at 186.

37. *Life Partners* provides the following explanation for this terminology:

> A 'viaticum' in ancient Rome was a purse containing money and provisions for a journey. A viatical settlement, by which a dying person is able to acquire provisions for the remainder of his life's journey by selling his life insurance policy, is thus thought to provide a viaticum. In the language of the industry, the insured is the 'viator,' who sells his policy at a discount to a 'provider' of the viaticum.

484 F.3d 284, 287 (4th Cir. 2007).

38. *See* Martin, *supra* note 17, at 185–86.

39. *See id.* at 186.

40. Bozanic, *supra* note 7, at 241–42.

41. *Id.*

42. Martin, *supra* note 17, at 187.

43. J. Alan Jensen & Stephan R. Leimberg, *Stranger-Owned Life Insurance: A Point/Counterpoint Discussion*, 33 ACTEC J. 110, 110 (2007).

44. Bozanic, *supra* note 7, at 239.

45. *Id.*

tlements together according to risk.[46] The investors sell shares of these pools to others, with the buyers of these life-settlement-backed securities enjoying a more limited exposure to risk because the difficult-to-project lifespan of any one person represents only a small portion of the return possibility.[47] The securitization of life settlements holds a strong appeal for several influential actors: investors who wish to diversify their portfolios with an investment based on demographic facts and not economic ones,[48] bankers who collect fees from creating and selling the products,[49] and ratings agencies who are paid for rating the new securities.[50] Nevertheless, the actual growth of life-settlement-backed securities has been relatively slow, in part because successfully diversifying the risk across the lives of different insureds would require at least five hundred life settlements to be pooled together, a feat that would require an investment of "$500 million to $1 billion face in order to fund the policies."[51]

While the life-settlement industry originally developed in the United States, and the U.S. market is the largest in the world, the practice of reselling life insurance has spread across the globe, with industries of varying sizes active in England, Germany, Austria, the Netherlands, and Norway, to name only a few.[52] Particularly interesting are the twin markets of Canada and Australia, two countries that share the English legal tradition but have diverged spectacularly in their treatment of life settlements. Most Canadian provinces have made it illegal for individuals to sell their life insurance, resulting, unsurprisingly, in a practically nonexistent life-settlement market in Canada.[53] Australia, in contrast, in recent years has removed most of the legal obstacles to life settlements, leading to one of the most active markets outside of the United States.[54]

46. *Id.*

47. *Id.*

48. Martin, *supra* note 17, at 194.

49. *Id.* at 193.

50. *Id.* at 194.

51. *Life Settlement Securitizations Need Warehousing, Liquidity to Flourish*, RISKMARKET NEWS (Oct. 2, 2009, 9:40 AM), http://www.riskmarketnews.com/files/938280891c3fe3457d11705368c62895-67.php; *see also* BROWN & MENEZES, *supra* note 13, at 39 ("Insurance is an industry that requires . . . a vast dispersion in the market so as to benefit from the law of large numbers.").

52. Paul A. Siegert, *What Are Life Insurance Settlements—History and Evolution*, *in* TOOLS & TECHNIQUES OF LIFE SETTLEMENT PLANNING 1, 5 (2008), *available at* http://www.lifesettlementsfund.com/scripts/download.php?fn=isi-%20what%20are%20life%20settlements%20-%20history%20and%20evolution.pdf.

53. Perkins, *supra* note 31, at 1.

54. Sharo Michael Atmeh, *Regulation Not Prohibition: The Comparative Case Against the Insurable Interest Doctrine*, 32 NW. J. INT'L L. & BUS. 93, 139 (2011).

B. *Buying the Life of Another: A History of the Insurable-Interest Doctrine from 1745 to the Present*

1. A Brief Historical Sketch of Life Insurance

The institution of life insurance dates, at the latest, to the early fifteenth century as Mediterranean merchants took out insurance policies on cargo that included slaves.[55] The practice grew in scope fairly quickly as borrowers began insuring their own lives, naming their lenders as beneficiaries in order to more easily gain access to credit.[56] In some cases, lenders took out policies on borrowers to ensure payment even in case of death.[57] The practice of life insurance expanded yet again as ordinary citizens took out life-insurance policies on such famous personages as popes and princes; these citizens bought the policies as "mere wagers," in the hope that the individual would die before the insurance payments grew larger than the agreed-upon payout.[58] Most European cities and states, finding this type of wagering distasteful, outlawed either the institution of life insurance generally or, in a more limited approach, the practice of purchasing life insurance on such enumerated eminent people as popes, cardinals, bishops, emperors, kings, dukes, and princes.[59]

The reaction across Europe was understandable, as life insurance involves an inherent financial tension. The insurance company's profits are maximized when the insured lives as long as possible, continuing to make premium payments.[60] More pronounced even than any conflict between insurer and insured, though, is the internal dissonance for policyholders who, along with their beneficiaries, receive the greatest financial benefit[61] when they die early.[62] These tensions manage to stand in equipoise in normal circumstances because the desired outcomes of each party are socially unproblematic.[63] The insurer wants the insured to live because this would mean additional profits through the collection

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55. Martin, *supra* note 17, at 175; *see also The History of Life Insurance and Life Settlements*, HABERSHAM CAPITAL, http://web.archive.org/web/20131005211230/http://habershamcapital.com/brief-no2-history (last visited Feb. 19, 2014) (positing that the practice of insuring lives developed in ancient Rome, through so-called burial clubs, which helped pay for burial costs of club members).

56. Martin, *supra* note 17, at 175.

57. *Id.*

58. *Id.*

59. *Id.*

60. *Id.* at 173.

61. As measured by premiums paid versus payout received.

62. Martin, *supra* note 17, at 173–74.

63. Vlahos, *supra* note 6.

of premium payments.[64] The insured wants to live because of the basic evolutionary desire for self-preservation and, similarly, the beneficiaries in a typical scenario want their parent, spouse, relative, or friend to live more than they want the monetary payout.[65] The most interesting questions arise when these normal circumstances break down.

2. History of the Insurable-Interest Doctrine in England

The main exception to this continent-wide constriction of life insurance would prove to be England.[66] Italian merchants introduced the life-insurance industry to England in the mid-sixteenth century.[67] The lack of a ban there—in contrast to the actions of the rest of Europe—most likely stems from the desire of the English Parliament to continue accruing the tax revenues that were collected on insurance policies.[68] By 1745, though, Parliament took its first step toward limiting wagering through insurance by passing the Marine Insurance Act.[69] This Act required that all who wished to take out insurance policies on marine cargo have a pecuniary interest in the goods.[70] From there it was only a small step to addressing life insurance directly: the public outcry that resulted from the increasingly popular gambling practice of wagering on the lives of public figures eventually convinced Parliament to enact the Life Assurance Act of 1774.[71] This Act stated the following, known as the insurable-interest doctrine:

> No insurance shall be made by any person or persons, bodies politick or corporate, on the life or lives of any person, or persons, or on any other event or events whatsoever, wherein the person or persons for whose use, benefit, or on whose account such policy or policies shall be made, shall have no interest, or by way of gaming or wagering[.][72]

This Act required that the purchaser of life insurance hold an interest in the life of the person insured to be valid.[73] The Act also limited the size of the insurance recovery available, so that "no greater sum shall be recovered or received from the insurer or insurers than the amount of val-

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64. *Id.*

65. *Id.*

66. *The History of Life Insurance and Life Settlements*, *supra* note 55.

67. Martin, *supra* note 17, at 176.

68. *Id.*

69. Marine Insurance Act, 1746, 19 Geo. 2, c. 37 (Eng.).

70. *Id.* (noting that the lack of an interest in the goods "hath been productive of many pernicious Practices, whereby great Numbers of Ships, with their Cargoes, have . . . been fraudulently lost and destroyed").

71. Martin, *supra* note 17, at 176.

72. Life Assurance Act, 1774, 14 Geo. 3, c. 48 (Eng.).

73. *Id.*

ue of the interest of the insured in such life or lives, or other event or events."[74] Last, the Act declared that any insurance policy made contrary to this directive would be null and void.[75]

The preamble to the Life Assurance Act of 1774 gives some hint of the motivation behind the new legislation, positing that the new insurable-interest requirement is necessary because "it hath been found by experience that the making insurances on lives or other events wherein the assured shall have no interest hath introduced a mischievous kind of gaming."[76] The Act does not explicate what form this mischievous gaming had taken, but this reference may be understood as nothing more than reflection of a societal discomfort with gambling in general and wagering on the death of another in particular.[77] There is a possibility, though, that there was a more nefarious danger in play, a danger perhaps best exemplified by a "notorious case" from Pennsylvania.[78] There, a group of men purchased an insurance policy on the life of an elderly man, with the group expecting to collect a tidy profit when the man died.[79] The elderly man, to the chagrin of the group members, proceeded to live longer than expected and the group responded to the growing premium payments by killing the man; the murderers were "hanged for their trouble."[80]

More important, though, is the ambiguity not of the motivation for the Act but rather of its scope: the legislation never defined what precisely is an interest in "the life or lives of any person"[81] or who is considered to hold such an interest.[82] It was thus left to the courts to discover a passage through this morass. The 1806 case of *Lucena v. Craufurd* was the first major effort to define this required interest, expanding the definition beyond one who owns the life or goods to include also those people who would benefit by the continued existence of the insured and those who would be damaged by its demise.[83] This ap-

74. *Id.*

75. *Id.* ("[E]very assurance made contrary to the true intent and meaning hereof shall be null and void to all intents and purposes whatsoever.").

76. *Id.*

77. *See The History of Life Insurance and Life Settlements*, *supra* note 55 (noting a pronounced discomfort of religious groups toward life insurance as an institution because "they felt that it would be akin to anticipating one's own death").

78. Col Fullagar, *Using a Life Settlement Vehicle to Tackle Term Insurance Challenges*, MONEY MGMT. (Aug. 16, 2010), http://www.moneymanagement.com.au/opinion/insurance/life-settlement-vehicles.

79. *Id.*

80. *Id.*

81. Life Assurance Act, 1774, 14 Geo. 3, c. 48 (Eng.).

82. Martin, *supra* note 17, at 177.

83. Lucena v. Craufurd, [1806] 27 Eng. Rep. 630 (H.L.) 643 (appeal taken from Eng.) (find-

proach became known as the economic-relationship test.[84] This decision provided the basis for understanding the insurable-interest doctrine in both England and its many territories.[85] From this common background, two of England's former territories—Australia and Canada—diverged greatly in their treatment of the insurable-interest doctrine and, eventually, the modern life-settlement industry.[86] These parallel yet divergent developments are informative, demonstrating how Canada may benefit by liberalizing its approach to life settlements by following the model of Australia.

3. Development of the Life-Settlement Market in Australia

Australia's treatment of the insurable-interest doctrine remained identical to the existing English law until 1909 when Australia passed the Marine Insurance Act.[87] This legislation, while preserving the general doctrine of requiring an insurable interest, repealed the English Marine Insurance Act of 1745.[88] The 1909 Act redefined the scope of the insurable-interest doctrine for Australia by recognizing as valid the insurance taken out on marine cargo both when an insurable interest existed at the time of the contract and when there was a reasonable expectation that an interest would later be acquired, even if no interest was in place at the time the contract was made.[89] This Act is noteworthy because it indicated a willingness to deviate from the English precedent at the definitional margins of what is considered an insurable interest, even as the legislature declined to revoke the insurable-interest doctrine altogether.[90]

Australia took this same approach again when considering life insurance through passage of the Life Insurance Act of 1945.[91] This Act preserved the requirement of an insurable interest for an insurance contract to be valid even as it expanded the definition of when an insurable interest was present.[92] While at common law a mere relationship with an-

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ing that "to be interested in the preservation of a thing, is to be so circumstanced with respect to it as to have benefit from its existence, prejudice from its destruction").

84. Atmeh, *supra* note 54, at 100.

85. *Id.*

86. STUDY PAPER ON VIATICAL SETTLEMENTS, *supra* note 10, at 1 (noting that most Canadian provinces do not allow life settlements); *Life Insurance Act 1995* (Cth) s 200(1), (3) (Austl.) (allowing for the sale of life settlements).

87. *Marine Insurance Act 1909* (Cth) ss 5–6 (Austl.).

88. *Id.*

89. *Id.* s 10(2).

90. *See* Atmeh, *supra* note 54, at 136–37 (discussing ways in which Australia's Marine Insurance Act altered definitional landscape of what amounted to an insurable interest).

91. *Life Insurance Act 1945* (Cth) (Austl.).

92. *Id.* s 86.

other person was not sufficient to create an insurable interest for the purposes of life insurance unless there also existed a pecuniary relationship,[93] this new legislation recognized an insurable interest for parents in children under the age of twenty-one and for anyone in the life of a person who provided that individual support or education, even in the absence of any pecuniary association.[94]

It took until 1984 for Australia to depart in more than a surface-level manner from the traditional English insurable-interest requirement, when the Parliament of Australia passed the Insurance Contracts Act.[95] The Insurance Contracts Act stated that general-insurance contracts—those involving property insurance or indemnifications—were no longer void solely because of a lack of insurable interest at the time the contract was formed.[96] This Act addressed only a limited range of insurance contracts.[97] It took another eleven years for the decline of the insurable-interest doctrine to reach the realm of life insurance, as the Life Insurance Act of 1995 removed entirely the insurable-interest requirement for the formation of life-insurance agreements.[98] The rationale for this change was best expressed by the Australian Law Reform Commission in 1982, as it argued that policyholders should enjoy the rights of property owners—including freedom of assignment—when it came to insurance contracts.[99] Australia did not, though, remove the insurable-interest requirement without providing additional guidance.[100] The creation of the Australian Prudential Regulation Authority (APRA) in 1998 provided a regulatory authority to administer the Life Insurance Act of 1995, allowing for government oversight of life settlements.[101] APRA serves many regulatory purposes, including collecting data from life-insurance companies as part of its reporting requirements[102] and serving

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93. With the exception of a spouse. Atmeh, *supra* note 54, at 130.

94. *Life Insurance Act 1945* (Cth) s 86 (Austl.).

95. *See Insurance Contracts Act 1984* (Cth) (Austl.).

96. *Id.* s 17.

97. *See id.* s 9.

98. *Life Insurance Act 1995* (Cth) s 200 (Austl.).

99. *See* Law Reform Comm'n, Commonwealth of Austl., Insurance Contracts 87–88 (1982). The following excerpt shows the insurable-interest requirement:

> The need to allow policyholders to use policies as a form of property, together with the uncertainty that would be introduced into insurance practice if the policyholder were required to have an interest at the date of death of the life insured, constitute an adequate justification for not restricting the existing freedom of assignment.

Id.

100. *See* Atmeh, *supra* note 54, at 139.

101. *Id.*

102. *See Life Insurers and Friendly Societies Reporting Framework*, Austl. Prudential Reg. Authority (APRA), http://www.apra.gov.au/lifs/ReportingFramework/Pages/LIFS-Reporting.aspx (last visited May 19, 2014).

as the body that receives complaints about breaches in the law.[103]

4. Canada's Approach to Life Settlements

Canada, like Australia, maintains a strong English heritage.[104] This legacy extends to legal precedent, with Canada adopting the statutes and case law of England that were in effect at the time of its confederation in 1867.[105] In this way, Canada accepted England's insurable-interest doctrine, as the Life Insurance Act of 1774 predated Canada's confederation.[106]

Canada's courts and legislature have not followed the example of Australia in abolishing the insurable-interest requirement for insurance, though the Supreme Court of Canada has developed its own principles in defining when a satisfactory insurable interest is present.[107] This important legal development started in *Kosmopoulos v. Constitution Insurance Co.*, in which Mr. Kosmopoulos incorporated a business that had been a sole proprietorship.[108] Despite this change in status, Mr. Kosmopoulos continued signing documents—including a fire-insurance contract—without reference to the incorporated business.[109] After a fire caused significant damage to the business' assets, the insurance company refused payment by arguing that Mr. Kosmopoulos lacked an insurable interest in the damaged assets because he was merely a shareholder.[110] The Supreme Court diverged from the traditional English approach that would have resulted in a victory for the insurance company, ruling instead for Mr. Kosmopoulos by transitioning to a less-formalized understanding of who possesses an insurable interest.[111] Under this "factual expectancy" approach, an insurable interest is present whenever there is an economic relationship at stake—a more common-sense approach that recognizes Mr. Kosmopoulos' real-life interest

103. *See Breach Notification*, AUSTL. PRUDENTIAL REG. AUTHORITY (APRA), http://www.apra.gov.au/CrossIndustry/Pages/Breach-Notification.aspx (last visited Feb. 19, 2014).

104. *See* DAVID NORWOOD & JOHN P. WEIR, NORWOOD ON LIFE INSURANCE LAW IN CANADA 2 (3d ed. 2002).

105. *See id.*

106. *Id.*; *see, e.g.*, Kosmopoulos v. Constitution Ins. Co. of Can., [1987] 1 S.C.R. 2, 24 (Can. Ont. C.A.) (considering the English statutes on the insurable-interest doctrine—including the Marine Insurance Act of 1745—as binding law).

107. Marvin G. Baer, *Recent Developments in Canadian Law: Insurance Law*, 22 OTTAWA L. REV. 387, 392 (1990).

108. *Kosmopoulos*, [1987] 1 S.C.R. at 7.

109. *Id.*

110. *Id.* at 8 (citing Macaura v. Northern Assurance Co., [1925] A.C. 619 (H.L.) (appeal taken from N. Ir.) (arguing that shareholders hold insurable interests only in the company, not in its assets)).

111. *Id.* at 26.

in the assets of his company.[112]

While *Kosmopoulos* maintains the insurable-interest doctrine—and deals not with life insurance but with property insurance—it is noteworthy as the first instance in which Canada's highest court diverged from the traditional English approach.[113] The court in that case recognized three main policy rationales for requiring the insurable-interest doctrine: first, the insurable-interest doctrine would discourage wagering; second, it would limit indemnification to the amount lost, thereby avoiding windfalls to those who have not suffered a loss; and third, it would remove the moral hazard that results from the temptation to destroy property or lives that are insured.[114] None of these policy reasons would require, the court concluded, the highly formalized definition of insurable interest under which Canada was working before the decision.[115] Scholars applauded this result.[116] One scholar recognized that the "elaborate . . . technical legal rules" governing the insurable-interest doctrine in Canada were "ripe for reform."[117] In practice, the doctrine was used in most cases by insurance companies seeking to invalidate insurance policies—and avoid paying anything to the customers—on what amounts to a technicality.[118]

Although Canada still requires a valid insurable-interest for a valid insurance contract, most Canadian provinces interpret the doctrine in a way that does not bar the reselling of insurance to one with no insurable interest.[119] With the exception of Manitoba, Canadian jurisprudence requires the presence of an insurable interest only at the time the insurance contract was originally formed.[120] Therefore, so long as the life-insurance policy was originally purchased with a valid insurable interest, which is the normal procedure, the later reselling of the policy pre-

112. *Id.* at 3–4 (requiring only "some relation to, or concern in the subject of the insurance, which relation or concern by the happening of the perils insured against may be so affected as to produce a damage, detriment, or prejudice to the person insuring, that insured should be held to have a sufficient interest").

113. Baer, *supra* note 107, at 392.

114. *Kosmopoulos*, [1987] 1 S.C.R. at 25.

115. *Id.* at 28.

116. Baer, *supra* note 107, at 392.

117. *Id.* at 391.

118. *See id.* (arguing that these rules have taken on a life of their own, "invalidating insurance contracts at the behest of public spirited insurers to no clearly discernible social advantage").

119. STUDY PAPER ON VIATICAL SETTLEMENTS, supra note 10, at 17.

120. The following announces this rule:

> An insurable interest is acquired only at the commencement of the policy . . . . If the policy is validly issued, then in the absence of a contrary provision in the policy or the Act, the rights of the owner-beneficiary are not affected by the termination of his insurable interest in the life of the person insured.

See, e.g., Chantiam v. Packall Packaging Inc. [1998], 38 O.R. 3d 401 (Can. Ont. C.A.).

sents no problems under the insurable-interest doctrine.[121] Additionally, Canadians in many cases can, in effect, opt out of the insurable-interest doctrine altogether by consenting in writing to have insurance purchased on their lives.[122]

The one exception to this interpretation of the insurable-interest doctrine is the approach of the Canadian province of Manitoba, which in 1986 passed a law that had the effect of requiring an insurable interest upon the death of the insured.[123] Under this law, a policyholder may, "where insurable interest no longer exists, apply to the court for an order requiring the insurer to immediately terminate the policy and pay over to the policy owner any value that exists in the policy."[124] The judicial process of this legislation is fairly straightforward—courts will order the insurance company to terminate the insurance policy upon a simple showing that the owner no longer possesses an insurable interest in the policy; there is no need to prove any additional misconduct.[125]

Except for Manitoba, then, the insurable-interest doctrine does not present a barrier to life settlements in Canada. The main barrier to life settlements comes from a Depression-era law—enacted by every province other than Quebec, Saskatchewan, Nova Scotia, and New Brunswick—that was originally intended to prevent the unregulated trafficking of life-insurance policies in those times of financial desperation.[126] These statutes are functionally identical across the provinces and allow only authorized insurers to "traffic[] or trade[] in life insurance policies for the purpose of procuring the sale, surrender, transfer, assignment, pledge or hypothecation of them to himself or herself or any person."[127] These laws do not address the issue of life settlements directly but have the effect of prohibiting their use because the authorized insurance companies refuse to participate directly in the secondary market of life insurance in fear that this will harm the profitability of the primary life-insurance market.[128]

Despite its prohibition of reselling life insurance in a secondary market, Canada does allow for a broad primary life-insurance market, regu-

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121. NORWOOD & WEIR, *supra* note 104, at 85 ("Where a life insurance policy is issued with a valid insurable interest and is then assigned to a person who has no insurable interest, the validity and enforceability of the contract is not affected.").

122. STUDY PAPER ON VIATICAL SETTLEMENTS, *supra* note 10, at 16.

123. *See id.* at 17–18.

124. The Insurance Act, R.S.M. 1987, c. I40, art. 155(4) (Can. Man.).

125. STUDY PAPER ON VIATICAL SETTLEMENTS, *supra* note 10, at 18.

126. *See id.* at 11, 12.

127. Insurance Act, R.S.B.C. 1996, c. 226, art. 152 (Can. B.C.).

128. STUDY PAPER ON VIATICAL SETTLEMENTS, *supra* note 10, at 19.

lated in tandem by the federal and provincial governments.[129] Included in this broad regulatory scheme is the practice of corporate-owned life insurance, where a corporation owns life insurance on the lives of important personnel.[130] This type of insurance recognizes that certain key employees make up the corporation's most important resource and serves to ensure the smooth functioning of the business after the sudden loss of a key person.[131] To achieve this goal, the beneficiary of corporate-owned life insurance is the business itself.[132]

Life insurance in Canada is a matter of dual jurisdiction, with the provinces regulating the form and content of insurance contracts and policies and the federal government managing bankruptcy and winding-up procedures.[133] There is a great deal of consistency among the disparate provinces—all of the Canadian provinces, with the exception of Quebec, have adopted the Uniform Life Insurance Act of the Provinces of Canada as a piece of model legislation, recognizing the importance of national conformity in life-insurance issues.[134] Even though it has not joined in enacting the model legislation, Quebec's Civil Code mirrors the Uniform Life Insurance Act in many important aspects, especially after the Civil Code was revised in 1976.[135]

The federal and provincial governments—as twin law-making bodies—have their own regulatory structures to administer the law.[136] Each province maintains an Office of the Superintendent that oversees matters within its jurisdiction, including the regulation of insurance contracts and the licensing of insurance agents and brokers.[137] In 1987, the federal government established the Office of Superintendent of Financial Institutions, which focuses on the financial integrity of insurers.[138] There is a fair amount of collaboration between the federal and provincial regulators, as both groups hold biannual meetings as part of their membership in the Canadian Council of Insurance Regulators, seeking

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129. NORWOOD & WEIR, *supra* note 104, at 2–3.

130. *Id.* at 84.

131. HR HORIZONS, KEY EMPLOYEE LIFE INSURANCE/CORPORATE-OWNED LIFE INSURANCE (COLI) ARRANGEMENTS (2008) [hereinafter KEY EMPLOYEE LIFE INSURANCE], *available at* http://hrhorizons.nacubo.org/Documents/Fact%20sheet--key%20employee%20life%20insurance,%20COLI%20arrangements.pdf.

132. *See* NORWOOD & WEIR, *supra* note 104, at 3.

133. *Id.* at 3.

134. *Id.* at 5 (the non-Quebec provinces all adopted this model legislation between 1924 and 1931).

135. *Id.*

136. *Id.* at 7.

137. *Id.*

138. *Id.* at 8–9.

to solve industry-wide problems and promote uniform legislation.[139] Even with the growth in regulatory bodies in the Canadian life-insurance market, the overall state of the Canadian insurable-interest doctrine remains mostly unchanged from the English heritage it received in 1867.[140]

III. Analysis

Canada should liberalize its approach to life settlements to allow owners of life insurance to sell their policies in a regulated secondary market. The original motivations for enacting the antitrafficking law are not strong enough to restrict the hard-earned property rights of insurance policyholders. Additionally, the three stated rationales for maintaining the insurable-interest doctrine prohibiting life settlements are no longer applicable to the Canadian life-insurance market. Therefore, Canada should allow for the sale of life settlements in order to better protect the considerable investments of consumers while also respecting the property rights that come with owning life insurance. To accomplish this goal, Canada should repeal the Depression-era antitrafficking laws to enable the life-settlement market to grow away from the interested eye of the authorized primary insurance companies and should abolish the outdated insurable-interest law that provides another barrier to life settlements in Manitoba.

A. *Why Canada Should Liberalize Its Life-Settlement Industry*

Canada should allow life settlements in order to better recognize the property rights of insurance owners. Purchasers of life insurance pay considerable sums for the right to receive a payout upon death.[141] This investment is necessarily limited if it does not come with the ability to transfer this right.[142] Recognition of the property rights of insurance owners is even more important in light of the weakened policy rationales underpinning the antitrafficking laws and insurable-interest doctrine.

Additionally, this change will be beneficial to consumers.[143] The problem for consumers is that purchased insurance is a monopsony, a single-buyer marketplace.[144] If the purchaser of an insurance policy is no longer able to pay the monthly premiums, he can let the policy lapse

139. *Id.*
140. *Id.* at 2.
141. Vlahos, *supra* note 6.
142. *Id.*
143. *Id.*
144. *Id.*

and gain nothing, or he can sell it back to the insurance company for a small fraction of the value he has already paid.[145] Life settlements allow for a more productive use of resources by allowing people who have no further use for life insurance to sell it and recoup some of their investment.[146] Canadian courts have generally analyzed insurance contracts in a way that is "especially favourable to the insured."[147]

B. *The Stated Rationales for Prohibiting Life Settlements Are No Longer Valid.*

Canada should allow life settlements because the stated reasons for their prohibition are no longer valid. The antitrafficking law that is now the main barrier to accepting life settlements was not enacted to prohibit the resale of life insurance.[148] Instead, three motivations are said to underpin the law: to support struggling insurance companies in the aftermath of the Great Depression by eliminating the competition that arose from unlicensed insurance sales; to protect consumers who were newly vulnerable to financial pressures in the wake of the Depression; and to promote uniformity in the insurance laws of the various provinces.[149] Separately, Canada recognizes three main policy rationales for maintaining the insurable-interest doctrine that prohibits life settlements in Manitoba.[150] First, the insurable-interest doctrine seeks to eliminate wagering on the property or life of another.[151] Second, the doctrine preserves the indemnity principles of insurance, preventing the awarding of windfalls to people who have not suffered losses.[152] Third, the insurable-interest doctrine removes the moral hazard that results from a person standing to benefit from the destruction or death of another's property or life.[153] Upon close inspection, however, the rationales motivating both the antitrafficking law and the insurable-interest doctrine are no longer convincing.

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145. The following explains this principle:

> "You wouldn't want to buy a Ford and turn around 10 years later and find out that the only entity you could sell it to is back to Ford," says Vince Granieri, the chief actuary at the life-expectancy company 21st Services. Settlements let the consumer shop a policy to multiple buyers and potentially get anywhere from 2 percent to more than 60 percent of its face value.

Id.

146. *Id.*

147. Stock v. Inglis, [1884] 12 App. Cas. 564 (H.L.) 569; Trotter v. Calgary Fire Ins. Co., [1910] 3 Alta. L.R. 12 (Can. Alta. Q.B.).

148. STUDY PAPER ON VIATICAL SETTLEMENTS, *supra* note 10, at 12.

149. *Id.* at 14–15.

150. BROWN & MENEZES, *supra* note 13, at 70.

151. *Id.*

152. *Id.*

153. *Id.*

1. The Rationales for the Antitrafficking Laws Are No Longer Valid.

i. Insurance Companies No Longer Need Protection from Competition.

The Great Depression left Canadian insurance companies in a precarious position, threatening the very survival of many firms.[154] The antitrafficking law was one of many pieces of new legislation that attempted to prevent the failure of the insurance industry.[155] The idea behind the antitrafficking law was to prevent competition from unlicensed agents, thereby leaving the regulated insurance companies to do enough business to survive those tough financial times.[156]

Today, the goal of ensuring the survival of Canada's insurance companies can be judged a success, with dozens of firms offering life-insurance policies.[157] There is little danger that a firm such as Canada Life, which earned C$8.8 billion in premiums and fees in 2012, is threatened by the activities of unlicensed agents.[158] Indeed, even the insurance companies themselves do not argue that allowing life settlements will threaten their financial viability going forward.[159] Although it may be more profitable for insurance companies if life settlements are prohibited—as the probability of a lucrative surrender will likely be diminished with a robust secondary market—this is a long way from a law meant to specifically prevent the very failure of insurance firms. There must be a strong rationale to justify restricting the property rights of insurance policyholders, and this outdated measure meant to stabilize insurance companies in the wake of the Great Depression is not reason enough to limit ownership rights in this way.

ii. Consumers Would Be Better Protected Through a Well-Regulated Secondary Marketplace.

Part of the motivation for the antitrafficking laws was to protect consumers vulnerable to scams and fraud in the wake of the Great Depression.[160] Unfortunately, the total ban on life settlements has left consumers in a more dangerous position, as prohibition has served mainly to

154. STUDY PAPER ON VIATICAL SETTLEMENTS, *supra* note 10, at 23.

155. *Id.* at 14.

156. *Id.* at 14–15.

157. *See, e.g.*, *List of Canadian Life Insurance Companies*, LSM INS., http://lsminsurance.ca/canadian-life-insurance-companies (last visited Feb. 19, 2014).

158. *See* CAN. LIFE ASSURANCE CO., ANNUAL REPORT 2012, at 2 (2012), *available at* http://www.canadalife.com/web5/groups/common/@public/documents/web_content/s7_030229.pdf.

159. STUDY PAPER ON VIATICAL SETTLEMENTS, *supra* note 10, at 23.

160. *Id.* at 12, 22.

drive the secondary life-insurance market underground.[161] This result only weakens the hand of consumers in a number of different ways: a regulated life-settlement market would improve the fraud protections and disclosure requirements to the benefit of consumers, especially when compared to an unregulated underground market; there is currently little recourse for consumers who are cheated in their efforts to resell life insurance, as they can be hesitant to report abuses that take place in an illegal marketplace; even if cheated consumers do report harmful practices, the only penalty available under current law is a fine assessed to the cheater, with no compensation paid to the victim; and, perhaps most important, consumers will enjoy greater financial flexibility through the option of selling their life-insurance policies in an open market—instead of merely being limited to taking the surrender value from the insurance company if they are no longer able to make premium payments.[162] The best way for Canada to protect its consumers is not to ban life settlements but rather to provide a regulated and functioning market to allow for the reselling of insurance policies.

iii. Uniformity Would Be Better Promoted by Allowed Life Settlements.

If one of the goals of the antitrafficking laws was to promote uniformity of insurance law across the provinces, this effort itself must be deemed a failure: Saskatchewan, Nova Scotia, and New Brunswick never enacted any version of the antitrafficking law, and Quebec repealed its version of the law in 1974.[163] Between the repeal of Quebec's law and the proposal for a similar repeal of Ontario's legislation in the mid-2000s,[164] it is possible to detect the faint outline of a trend moving against the antitrafficking laws.[165] Indeed, the chances of any of the outlier provinces enacting an antitrafficking law at this stage are slim.[166] If the uniformity of insurance laws across the provinces is still a goal worth pursuing, then the objective "is more likely to be promoted by the enactment of modern legislation permitting viatical settlements within a regulated framework."[167] While a basic level of uniformity is important in a wide-ranging market like that of life insurance in Canada, there is reason to suspect that uniformity of insurance laws was less a goal than a tactic for the main advocates of the antitrafficking laws, meant to per-

161. *Id.* at 23.
162. *Id.*
163. *Id.* at 23–24.
164. *Id.* at 31–32.
165. *Id.* at 24 n.113.
166. *Id.* at 24.
167. *Id.*

suade others to come around to a position favorable to the organization.[168] Whether homogeneity is a worthy goal or not, uniformity should not stand in the way of allowing life settlements because there is a greater likelihood of achieving uniformity through elimination of the antitrafficking laws.

2. The Reasoning for the Insurable-Interest Doctrine Is No Longer Applicable.

i. Life Settlements Are Not Wagers.

A wager in Canadian law has a very particular definition, with one occurring only when two parties "professing to hold opposite views touching the issue of a future uncertain event, mutually agree that, dependent upon the determination of that event, one shall win from the other, and that the other shall pay or hand over to him, a sum of money or other stake."[169] A crucial element of these void wagering contracts is that "each party may under it either win or lose," with the outcome dependent on an uncertain event.[170] The contract is not a void wager, though, if "either of the parties may win but cannot lose, or may lose but cannot win."[171]

As a result, life settlements do not seem to fall under the traditional definition of a wager. Life settlements do not follow the format of a wager because there is no conventional winner or loser in these transactions. The seller of a life settlement is not interested in the outcome of the so-called bet in the same way a party to a traditional wager is. The seller decides to sell not because he thinks he can make a profit by living long enough to out-earn the profits of the buyer; in most cases, he decides to sell because he needs cash.[172] In fact, the seller of a life settlement has no opportunity to gain anything at all once the sale is made.[173]

Because the definition of a wager in Canada requires the possibility that "each party may under it either win or lose," a life-settlement contract is therefore not a legal wager because it is impossible for the seller to either win or lose.[174] Thus, even if the buyer may win the life-settlement transaction by earning more in the payout than the amount he

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168. *Id.* at 23.

169. Carlill v. Carbolic Smoke Ball Co., [1892] 2 Q.B. 484 at 490–91 (Eng.), *aff'd*, [1892] EWCA (Civ.), [1893] 1 Q.B. 256 (C.A.) (Eng.).

170. *Id.* at 491.

171. *Id.*

172. Life Partners, Inc. v. Morrison, 484 F.3d 284, 287–88 (4th Cir. 2007).

173. *Id.* at 288.

174. *Carlill*, [1892] 2 Q.B. at 491.

paid to acquire and maintain the insurance policy, a life settlement is not a wager without the possibility that the seller can also win.[175] To be sure, Canadian courts persist in the interpretation that life settlements are prohibited under the insurable-interest doctrine, in part because they are wagers.[176] Yet, under closer scrutiny, the rationale underlying the decision to prohibit life settlements is on shaky ground, as the policy to prevent wagering should not apply to a life settlement under Canadian law because life settlements are not wagers in the definitional sense.

ii. Life Settlements Do Not Violate Indemnity Principles.

The central premise of insurance is the indemnity principle.[177] Insurance distributes the risk of loss among many parties in order to provide funds to those who actually suffer the loss.[178] The basic mechanism plays out through the insurance contract, which "transfers the burden of potential loss to the insurer."[179] This only works, though, when the insured is able to recover only the value of the loss but nothing more.[180] Anything else would shift "from cushioning the economic impact of losses, to the redistribution of wealth."[181] This is why the indemnity principle plays such an important role in the insurable-interest doctrine. If the idea of indemnity insurance is to protect people from losses they may suffer, the principle breaks down when an insured is allowed to recover for a loss he has not suffered.[182] When an insured is able to recover when he fails to hold an interest in the loss, he has not truly lost anything and would therefore gain an unearned windfall upon collection of the insurance payout.[183]

Life insurance is not a traditional form of indemnity insurance.[184] Indemnity insurance functions, in essence, as a promise by the insurer to replace the value of insured property "up to but not beyond the actual extent of the loss at the time when the property is damaged or destroyed."[185] Life insurance works differently, as the insurer simply promises to pay a set amount of money to the beneficiary at the time the

175. *Id.* at 492.

176. BROWN & MENEZES, *supra* note 13, at 66–67.

177. *Id.* at 1.

178. *Id.*

179. *Id.*

180. *Id.*

181. *Id.*

182. *Id.* at 70.

183. *Id.* at 72.

184. *Id.* at 3; *see also* Chantiam v. Packall Packaging Inc., [1998] 38 O.R. 3d 401 (Can. Ont. C.A.) ("Life insurance is not a contract of indemnity . . . .").

185. NORWOOD & WEIR, *supra* note 104, at 85.

death occurs.[186] More important, it is "both very difficult and distasteful" to determine the precise monetary value of a human life.[187] Also, death is unlike other types of loss in that it is guaranteed to occur, with the only uncertainty being the time of its occurrence.[188] This is in contrast to indemnity insurance, where there is no guarantee that the risk insured against—for example, a car accident—will ever occur.[189] Indemnity principles, therefore, should not be applied to life insurance because life insurance does not function in the same way as indemnity insurance.

For example, consider car insurance. Car insurance is a typical form of indemnity insurance.[190] Removing the indemnity limitation from car insurance would render the transaction nonsensical as a car owner would be able to recover from the insurer, for example, more than the worth of the car she insured. This example becomes even more absurd if the owner of car insurance is able to collect insurance money for the destruction of a car she did not even own. This would go beyond protecting the value of owned property and enter the realm of unearned payouts, necessitating the indemnity limitation.

Unlike car insurance, though, there is no way to precisely measure the loss of a life. The entire danger of windfalls—earning more than the amount lost—does not apply to the inherently immeasurable value of a human life. It can hardly be said that the holder of life insurance may receive a windfall without knowing the exact amount lost in the first place. In this way, the indemnity-principle rationale for the insurable-interest doctrine fails to apply to life insurance.

iii. Life Settlements Do Not Pose Serious Moral-Hazard Risks.

Unlike the previous two policy rationales, there does remain an element of moral hazard to consider, as any time a person owns insurance on another's life or property there is a temptation to destroy the insured object.[191] That said, the desire to eliminate this temptation should not be strong enough on its own to prevent the acceptance of a regulated life-settlement market in Canada. First, there is already a situation in which Canada allows people to purchase insurance on the life of another: corporate-owned life insurance.[192] As discussed above, corporate-

186. *Id.*
187. BROWN & MENEZES, *supra* note 13, at 3.
188. *Id.*
189. NORWOOD & WEIR, *supra* note 104, at 23.
190. *Id.* at 22.
191. BROWN & MENEZES, *supra* note 13, at 3.
192. NORWOOD & WEIR, *supra* note 104, at 84.

owned life insurance is the practice of a corporation carrying insurance on the life of its key personnel.[193] Crucially, this key-person insurance is payable to the business.[194] Although the idea behind this type of insurance is that the corporation needs to protect itself against the loss of a crucial employee, a business that has already purchased corporate-owned life insurance will experience a financial benefit in the early death of the key employee. The payout to the business upon the death of the key employee is set when the business and the insurance company agree to the contract.[195] Just like in a life settlement, the profit of the business' payout can be eaten up by the annual premium payments if the key employee lives longer than expected. Here too, the temptation might arise to do what is best for the business and collect the insurance. This allowance of key-person insurance therefore suggests that Canada's insurance system will tolerate the moral hazard of one person or corporation serving to benefit upon the death of another person.

Additionally, although it may always be best to remove temptations for murder or unethical behavior, there is already a disincentive to murder that is stronger than voiding an insurance contact: life imprisonment.[196] These two factors suggest that, even though there remains an undesirable moral hazard in eliminating the insurable-interest doctrine, the desire to prevent this temptation from taking root should not be strong enough on its own to preclude the legalization of life settlements in Canada.

C. *Criticisms of Life Settlements Are Not Persuasive.*

Those concerned about the repeal of the antitrafficking laws and the insurable-interest doctrine have had ample opportunity to express their criticisms during the rise of the life-settlement industry in the United States.[197] Some of these concerns are more valid than others, but none of them is persuasive reason to prevent the allowance of life settlements in Canada.

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193. KEY EMPLOYEE LIFE INSURANCE, *supra* note 131.

194. Chris Griffiths, *Protect Your Business with Key-Person Insurance*, GLOBE & MAIL (June 26, 2012, 7:55 AM), http://www.theglobeandmail.com/report-on-business/small-business/sb-money/valuation/protect-your-business-with-key-person-insurance/article4364244.

195. *See* Al Emid, *Key Person Insurance an Overlooked Opportunity*, ADVISOR.CA (July 14, 2011), http://www.advisor.ca/insurance/life/key-person-insurance-an-overlooked-opportunity-52968 (explaining that the insurance company sets an annual premium based on this payout and the normal risk factors of the key employee).

196. Criminal Code, R.S.C. 1985, c. C-46, s. 235(1) (Can.) ("Every one who commits first degree murder or second degree murder is guilty of an indictable offence and shall be sentenced to imprisonment for life.").

197. Scism, *supra* note 29.

1. Life Settlements Are Unlikely to Inflate the Price of Life Insurance for Everyone.

While the institution of life settlements can help sellers by providing additional potential buyers, this same flexibility may prove harmful to the insurance companies.[198] In particular, most, if not all, life-insurance policies that are resold as life settlements are ones that would have lapsed or been redeemed—assuming the presence of a redemption clause in the contract—to the insurance company for a fraction of the face value.[199] These two outcomes are the most financially beneficial to the insurance companies, as they are able to collect all of the premium payments made over the course of many years while avoiding the substantial outlay of paying the face value of the policy.[200] In extreme cases, an insurance company may collect premium payments for decades upon decades and then pay out nothing if the policy is allowed to lapse.[201] By introducing a third alternative that is more lucrative to customers than a straight lapse or an insurance-company redemption, life settlements significantly reduce the likelihood that insurance companies will experience the financial boons of a lapse or redemption.[202]

Some who oppose the expansion of the life-settlement industry point to this change in how customers can sell their life-insurance contracts as bad public policy, with potentially negative consequences for others beyond those directly involved in life settlements.[203] The argument goes that life settlements will sharply depress the profitability of life-insurance companies by reducing the number of those lucrative lapses.[204] Then, to maintain profit levels and appease shareholders, the insurance companies will have no choice but to increase the price for life insurance across the board.[205] This price increase may then discourage others from purchasing life insurance, as the higher premiums either make the financial calculus less rewarding or simply put the product out

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198. *See* Eli Martin Lazarus, *Viatical and Life Settlement Securitization: Risks and Proposed Regulation*, 29 YALE L. & POL'Y REV. 253, 262 (2010).

199. Vlahos, *supra* note 6.

200. *See id.*

201. *Id.*

202. *See* Eryn Mathews, *STOLI on the Rocks: Why States Should Eliminate the Abusive Practice of Stranger-Owned Life Insurance*, 14 CONN. INS. L.J. 521, 530 (2008).

203. Lazarus, *supra* note 198, at 273.

204. *Id.*

205. Lazarus explains as follows:

> An insurer's financial planning depends on accurately forecasting these lapse rates: since an insurer does not pay death benefits on a lapsed policy, the insurer can charge lower premiums, making its policies more competitive in the primary market. Reduced lapse rates mean increased costs for insurance providers and hence, higher premiums for insureds.

Id.

of reach for consumers.[206] If it is in the public interest to encourage the purchase of life insurance, allowing for life settlements may arrest the development of this goal.[207]

Under greater scrutiny, this argument fails. First, it is far from clear that insurance companies would need to appreciably raise premium prices to account for fewer lapsed policies.[208] One analysis of the Canadian market places the lapse rate for life-insurance policies at eighty-eight percent.[209] This suggests that, while the insurance companies are indeed profiting quite handsomely by avoiding payouts to those customers who let their policies lapse, the companies may maintain profitability even with a decreased lapse rate.[210] Indeed, the insurance companies are most likely already pricing their products in anticipation of lowered lapse rates, meaning that any life-settlement induced price changes will probably be negligible.[211] This argument also assumes that policies are priced at the lowest possible cost that still allows profitability for the insurer. In truth, though, low lapse rates are likely already factored into the price of current life insurance.[212]

Additionally, the market for life settlements in Canada may be systemically weaker than that in, for example, the United States. The prototypical seller of a life settlement is an elderly person motivated to sell because of an urgent need for funds, often because of high medical bills.[213] As noted, life settlements originated in the United States in re-

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206. Bozanic, *supra* note 7, at 258.

207. Bozanic elaborates as follows:

> With an increase in premium rates, individuals who would otherwise procure insurance for legitimate purposes may be dissuaded from doing so. If policy principles are to encourage individuals to have insurance, then maybe restricting life settlement transactions could be justified on the ground that life settlements are creating a barrier for individuals to acquire life insurance.

Id.

208. *See* Atmeh, *supra* note 54, at 131.

209. Scot Blythe, *Life Settlements: Investing in Mortality*, BENEFITS CAN. (June 25, 2010), http://www.benefitscanada.com/investments/alternative-investments/life-settlements-investing-in-mortality-6954 ("Life insurance has a dirty little secret that I don't think it would like many people to know. But 88% of universal life insurance policies never pay a death benefit . . . . That creates an incredible amount of value for those life insurance companies.").

210. *See* Atmeh, *supra* note 54, at 131.

211. Atmeh concludes as follows:

> Therefore, an open and free transferability market, or insurance procurement market, will likely have a very small effect on both pricing and profitability of insurance companies. Indeed, according to one analysis, "a life settlements transaction generally has minimal or no impact on the anticipated profitability of a life insurance contract because the persistency of an unhealthy policyholder is precisely what is assumed at the time of original pricing."

Id.

212. *Id.*

213. Life Partners, Inc. v. Morrison, 484 F.3d 284, 287 (4th Cir. 2007).

sponse to the exorbitant costs of AIDS treatments during the 1980s.[214] Canada, with its universal health care, is less likely to find its citizens desperately seeking assets to pay for medical treatments.[215] That is not to say that there is no need for life settlements in Canada; rather, because one of the core motivations for people to sell their life-insurance policies is likely weakened, the life-settlement market itself may be stunted and therefore the industry may have a relatively lesser effect on lapse rates overall.

Second, the pessimistic predictions about higher pricing of life-insurance purchase rates caused by enabling life settlements remain firmly in the realm of conjecture. It may well turn out that consumers will be more willing to purchase life insurance—even at higher prices—if they know that there exists a viable secondary market for their policies. An accessible secondary market will make the insurance policies that consumers buy more valuable to them because consumers may resell these policies for sums greater than the relatively meager returns of letting the policy lapse or redeeming it to the insurance companies. Consumers, in other words, will not necessarily hesitate to purchase more expensive insurance if the policies they are getting retain more of their value by way of a lucrative secondary market.

2. Privacy and Fraud Concerns Can Be Managed Through a New Regulatory Body.

Like all financial transactions, life settlements are potentially vulnerable to instances of fraud.[216] In the United States, at least, fraud has been attempted at "every stage of the viatication and life settlement process."[217] This includes new customers hiding illnesses during the initial insurance-procurement process to secure more favorable policies, along with existing insurance-holders faking serious health issues to convince investors of an imminent death to inflate a life-settlement payout.[218] Because life settlements by their nature disproportionately involve elderly citizens, there may be an even greater risk that these potentially financially unsophisticated consumers may fall victim to fraud.

Similarly, there are legitimate privacy concerns that are inherent in the life-settlement market.[219] Investors understandably demand to see

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214. *Id.* at 288.

215. *See Health Care System*, HEALTH CAN., http://www.hc-sc.gc.ca/hcs-sss/index-eng.php (last modified Feb. 10, 2014) ("Known to Canadians as 'medicare', the system provides access to universal, comprehensive coverage for medically necessary hospital and physician services.").

216. Lazarus, *supra* note 198, at 262.

217. *Id.*

218. *Id.*

219. Joy D. Kosiewicz, Comment, *Death for Sale: A Call to Regulate the Viatical Settlement*

comprehensive medical records, and in some cases require a full physical examination, of sellers of life insurance because life expectancy is so directly intertwined with the profit-potential of a life-settlement deal.[220] How existing and potential investors handle this health information obviously implicates the privacy of the insured.[221] The rise of securitization, which allows investors to purchase slices of an individual policy, thus exposing confidential information to dozens or hundreds of investors, only heightens these concerns.[222]

Yet, these fraud and privacy concerns, legitimate as they may be, are not sufficient reasons to prohibit the entire field of life settlements. Instead, these issues should be managed through regulation. In this instance, Canada should follow the model of Australia. Just as Australia established the Australian Prudential Regulation Authority in 1998 to administer the Life Insurance Act of 1995 and regulate the life-settlement industry, so too should Canada create a new regulatory agency to manage its new secondary market for life insurance.[223] In particular, Canada's new regulatory agency should take certain steps to minimize the deleterious effects of fraud and privacy invasions. While there will always be those people who attempt to cheat the system, no matter how well regulated, the damage can be contained by bringing life-settlement transactions out into the open. Additionally, the new agency can especially help those who are the most vulnerable to life-settlement fraud by educating senior citizens, who will make up the large majority of life-insurance sellers in the new secondary market.

In the same vein, the new regulatory agency can take certain steps to protect the privacy of sellers of life insurance. For example, the new agency can mandate that confidential health data be disconnected from any identifiable person before an insurance policy is sliced up and sold as a security. Last, the new regulatory agency would help ensure compliance with Canada's Personal Information Protection and Electronic Documents Act, which maintains the confidentiality of medical and personal information in federally regulated business and commercial activities.[224] While the insured should understand that the purchaser of her life-insurance policy requires access to her basic medical information to make an informed investment decision,[225] the open regulation of the secondary market for life insurance will be able to help protect the pri-

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Industry, 48 CASE W. RES. L. REV. 701, 721 (1998).

220. *See* Martin, *supra* note 17, at 185.

221. Kosiewicz, *supra* note 219, at 721.

222. *Id.*

223. Atmeh, *supra* note 54, at 139.

224. Personal Information Protection and Electronic Documents Act, S.C. 2000, c. 5 (Can.).

225. Kosiewicz, *supra* note 219, at 719.

vacy of this sensitive information during every step of the process. In this way, the more serious privacy breaches will be prevented, allowing life-settlement sellers to provide access to their health information to the only investment group that actually purchases the entire policy.

Canada does have multiple regulatory bodies for its life-insurance industry, ranging from provincial Offices of the Superintendent to the federal Office of Superintendent of Financial Institutions.[226] These regulators have been principally focused on the primary market of life insurance, ranging from the licensing of agents and brokers to the structuring of contracts.[227] While the duties suggested above for the new regulatory industry may be folded into the current responsibilities of the federal Office of Superintendent of Financial Institutions, Canada would do well to keep separate the regulatory bodies for the primary and secondary life-insurance markets. This division will ensure that the responsibility of managing the unique concerns—from educating senior citizens to protecting confidential information—of the secondary life-insurance market will receive the attention it needs to implement an entire new category of life insurance. By creating a new regulatory agency to administer the new life-settlement market, Canada will gain the benefits of allowing a secondary life-insurance market while minimizing the risks of fraud and privacy breaches.

3. Inability of Life-Settlement Sellers to Buy Life Insurance Again Should Not Prevent the Allowance of Life Settlements.

Sellers of life settlements are usually unable to buy life insurance again for their own use.[228] This may prove problematic for the insureds who purchase life insurance, sell it as a life settlement, and then find themselves in need of additional life insurance.[229] Opponents of life settlements point to this as a reason to ban secondary markets: to protect consumers by ensuring that no one who wants to purchase life insurance will be prevented from doing so.[230] This problem is most acute in life-insurance regimes that do not allow STOLIs, as investors hungry for life-settlement investment opportunities encourage citizens to buy insurance they may not need in order to buy them out.[231]

This problem is not serious enough to prevent the institution of life settlements as a whole. First, consumers should be able to make the

226. NORWOOD & WEIR, *supra* note 104, at 7–9.
227. *Id.* at 7–8.
228. Jensen & Leimberg, *supra* note 43, at 113, 115–16.
229. *See id.*
230. *Id.* at 115–16.
231. Atmeh, *supra* note 54, at 134.

choice to sell their life insurance, even if that decision will foreclose later opportunities to purchase additional life insurance. To ensure that consumers make these decisions with full knowledge of the consequences, the new Canadian regulatory agency should set out to educate the public, perhaps by requiring life-settlement buyers to disclose this very repercussion to insureds at the time of the transaction. Second, allowing for STOLIs will mitigate the problem of the unavailability of future life insurance by reducing the number of sellers of life insurance in the first place.[232]

The prohibition on STOLIs forces buyers to recruit owners of life insurance to sell their policies as the investors are unable to gain access to the insurance market any other way.[233] By allowing the secondary life-insurance market to grow naturally, investors will have little need to encourage people who would not otherwise buy life insurance to purchase a policy for the purpose of reselling it later.[234] This helps solve the problem of preventing sellers of life insurance from purchasing another policy by reducing the number of people who buy insurance for reasons other than their own personal use.

Ultimately, the criticisms of allowing life settlements are simply not persuasive enough to prevent the implementation of a secondary market for life insurance. The concerns of privacy and fraud in particular are valid, but a well-functioning regulatory body can mitigate them. The criticisms certainly do not justify sacrificing the financial flexibility and greater respect for property rights that would result from allowing life settlements, especially in light of the modern irrelevance of the stated policy rationales to prevent them.

IV. Conclusion

The antitrafficking laws and the insurable-interest doctrine that together work to prohibit the resale of life insurance are products of the particular circumstances of their times. These laws were meant to provide solutions to problems particular to Canada's 1930s life-insurance industry and to eighteenth century English life.[235] Those historical circumstances are no longer a reason to ban a beneficial practice in twenty-first century Canada, especially because the rationales that motivated these policy choices are now irrelevant. Instead, Canada should follow the model of Australia, another country that developed from the English

232. *Id.*

233. *Id.*

234. *Id.*

235. Study Paper on Viatical Settlements, *supra* note 10, at 14–15; Martin, *supra* note 17, at 176.

legal tradition,[236] and allow for the resale of life insurance known as a life settlement.

The liberalization of Canada's life-settlement policy will afford greater respect for the property rights of life-insurance owners, while allowing for a more efficient use of financial resources. The life-insurance industry no longer needs protection from unlicensed competitors, mitigating the original motivation for the antitrafficking law. Additionally, allowing for life settlements throughout Canada will actually help achieve the legislation's initial goal of promoting uniformity across the provinces. This change will also avoid the problems envisioned by the original English insurable-interest doctrine because the concerns of wagering, indemnification, and moral hazard are not found in the secondary life-insurance market. Canada should not, though, allow life settlements and then leave the fallout to be sorted out by market forces. Instead, Canada should create a new regulatory agency in the model of the Australian Prudential Regulation Authority in order to prevent fraud and protect the privacy of life-settlement sellers. These changes will secure the benefits of the secondary life-insurance market while minimizing the negative consequences.

Canada, by virtue of her geography and status as a participant in the English legal tradition, does not need to approach the issue of life settlements from a fresh slate. Insurance regulation, in particular, is an area especially suited for Canada to follow the lead of its neighbors, as "[i]n insurance . . . the courts have been prepared to be influenced by British and other Commonwealth decision."[237] It can look to the successes of the industry in the United States and Australia, two countries that developed their markets by adjusting and tweaking the traditional English insurable-interest doctrine, and select the best time-tested elements and strategies from each before embarking in the next development of insurance law in a uniquely Canadian way. Canada has already shown the willingness to tailor insurance law to its needs, and it should continue along this path to improve the financial flexibility of its consumer population.

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236. Horst Lücke, *Legal History in Australia: The Development of Australian Legal/Historical Scholarship*, 34 AUSTL. B. REV. 109, 114 (2010).

237. BROWN & MENEZES, *supra* note 13, at 21 ("Canadian . . . courts have also been willing to accept American judgments, both because of the common roots and because of the increasing similarity of industry practice within North America.").