

Rhode Island Supreme Court Decides STOA Case

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The Supreme Court of Rhode Island recently considered two questions of first impression: (i) whether an insurable interest requirement applies to an annuity with a death benefit, and (ii) whether an immediate incontestability provision is enforceable as a matter of public policy. In what the court characterized as a "rapacious investment scheme," the defendants in *Western Reserve Life Assurance Co. of Ohio v. ADM Associates* purchased and named themselves as beneficiaries of Freedom Premier III annuities with a Double Enhanced Death Benefit, which virtually guaranteed a risk-free investment. "The macabre *sine qua non* of the investment strategy" was that the defendants paid terminally ill individuals, identified through advertising to hospice patients, to serve as annuitants. Western Reserve's suits challenging the annuity purchases as void *ab initio* for lack of an insurable interest were dismissed, and on appeal the First Circuit certified the controlling questions to the Supreme Court of Rhode Island. A divided court held that (i) neither Rhode Island's longstanding common law nor more recent statutory insurable interest law applied to annuities; (ii) the 2009 Life Settlements Act was silent as to annuities and stranger-originated annuity transactions, and therefore does not govern the scheme; and (iii) the transactions were not wagering contracts (a ruling disputed in the two-justice dissent). The court also held the immediately-effective incontestability clause enforceable. **While the court recognized the ruling might "allow a perpetrator of fraud to profit from the fraudulent behavior," its precedents have long held that "an incontestability clause is effective even against a defense of fraud."** The ruling raises questions regarding the application of insurable interest statutes and common law protections to annuity transactions, and additional legislative efforts may be required to extend to annuities the longstanding protections available to life insurance policies.

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