

APPLICATION OF NEW FINANCIAL AND HEALTH INFORMATION PRIVACY LAWS TO THE VIATICAL AND LIFE SETTLEMENT INDUSTRY

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Introduction

This article analyzes the application of the modern privacy laws to the viatical and life settlement industry. Specifically, this article addresses how (1) the financial and health information privacy laws and regulations pursuant to the Gramm-Leach-Bliley Act (“GLB”) and (2) the health information privacy regulations under the Health Insurance Portability and Accountability Act of 1996 (“HIPAA”) apply to a viatical settlement company¹ or life settlement company.² While this article focuses on the privacy compliance obligations of viatical and life settlement companies, viatical and life settlement brokers face similar issues.

Typical Viatical/Life Settlement Transaction

Assume that a typical viatical and life settlement company, Settlement Company, Inc. (the “Settlement Company”), is looking to purchase qualified in-force life insurance policies. Generally, either an individual owner (a “viator”) of an in-force life insurance policy or an individual (who is oftentimes a licensed life insurance agent) representing the viator (the “Viatical Settlement Broker”) will contact the Settlement Company to ascertain whether the Settlement Company is interested in purchasing the life insurance policy from its owner. In connection with evaluating whether to purchase the policy, the Settlement Company obtains from the insured (who may or may not be the policy owner) a signed, broadly worded release by which the insured authorizes any individual, entity or person having medical records and information relating to the insured (including any physician, hospital and other medical professional, bank, employer, and creditor) to disclose such information to the Settlement Company. Often, the Viatical Settlement Broker provides some of the insured’s nonpublic personal information to the Settlement Company. The release also usually authorizes the Settlement Company and any individual, entity or person who provides any product or service to the Settlement Company to disclose and use such information in order to effect, administer, maintain and service the settlement transaction and in connection with the resale of the policy after it has been purchased by the Settlement Company. The Settlement Company usually then discloses this nonpublic personal information to a company that assesses the life expectancy of the insured based on such information and provides an estimated life expectancy to the Settlement Company. This article examines how the new privacy laws apply to these uses and disclosures of nonpublic personal information.

The Regulatory Backdrop

GLB established new privacy standards for the financial services industry (including insurance) to protect the disclosure and use of individuals’ nonpublic personal information. Pursuant to GLB, various federal regulatory agencies and some state legislatures or regulatory agencies, including the state departments of insurance, have adopted laws or regulations to effectuate GLB’s privacy mandates. Under these laws and regulations, financial institutions must, among other things, adopt privacy policies and provide notice of these policies to certain individuals at required times. In some instances, individuals may have a right to prevent such disclosure by opting-out of such disclosure, or a right to refrain from opting-in and allowing such disclosure.

The U.S. Department of Health and Human Services has promulgated regulations under HIPAA related to the privacy of personal health information (the “HIPAA Privacy Regulation”),³ which generally become effective on April 14, 2003.⁴ The HIPAA Privacy Regulation applies to health plans, health care clearinghouses, and health care providers who conduct certain financial and administrative transactions (e.g., electronic billing and funds transfers) electronically.⁵ These three types of entities are referred to as “Covered Entities.” The HIPAA Privacy Regulation establishes obligations regarding medical records and other personal health information used or disclosed by Covered Entities in any form, whether electronically, on paper or orally.

GLB Analysis

The first inquiry to be made under GLB is whether the Settlement Company is a “financial institution,” which is defined broadly as “any institution the business of which is engaging in financial activities.”⁶ “Financial activities” is in turn defined to include: (i) lending, exchanging, transferring, investing for others, or safeguarding money or securities; (ii) insuring, guaranteeing, or indemnifying against loss, harm, damage, illness, disability, or death, or providing and issuing annuities, and acting as principal, agent, or broker for purposes of the foregoing, in any State; (iii) providing financial, investment, or economic advisory services, including advising an investment company; (iv) issuing or selling instruments representing interests in pools of assets permissible for a bank to hold directly; and (v) underwriting, dealing in, or making a market in securities.⁷ The definition of “financial activities” also includes other activities the Federal Reserve Board has determined or does determine to be incidental or complimentary to the financial activities described above.⁸

The Settlement Company is likely engaged in a financial activity and therefore a financial institution. If an entity is a financial institution, one must then look to which regulatory agency has enacted regulations pursuant to GLB to govern the entity’s privacy practices. GLB provides the following guidance on this issue: (i) Banks and their subsidiaries are to be regulated by any or all of the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Board of Directors of the Federal Deposit Insurance Corporation, or the Office of Thrift Supervision; (ii) Federal credit unions are to be regulated by the National Credit Union Administration; (iii) Brokers and dealers, investment companies, and investment advisers are to be regulated by the Securities and Exchange Commission; (iv) Persons engaged in providing insurance are to be regulated by the applicable state insurance authority of the state in which the person is domiciled; and (v) *Any other person that is not subject to the jurisdiction of any agency or authority described above is to be regulated by the Federal Trade Commission.*⁹

However, GLB provides that state privacy laws or regulations that afford more protection than GLB are not superceded by GLB.¹⁰ In response to this provision of GLB, the National Association of Insurance Commissioners (the “NAIC”) promulgated the Model Privacy of Consumer Financial and Health Information Regulation (the “NAIC Privacy Regulation”), which has been adopted by state legislatures or insurance departments in approximately 36 states according to the NAIC.¹¹ Thus, the next question is whether GLB and any federal privacy regulation issued pursuant to GLB or a state privacy law or regulation, or somehow both, apply to the Settlement Company.

While it is clear that the Settlement Company is not a bank, credit union, or broker dealer, at first blush one may conclude that the Settlement Company is a “person engaged in providing insurance.” To determine whether the Settlement Company is regulated by the state departments of insurance, one needs to determine whether the Settlement Company is a “licensee” for insurance purposes in a particular state. However, not all states regulate viatical settlement and life settlement transactions. Some states regulate neither viatical settlement nor life settlement transactions,¹² while others regulate both viatical settlement transactions and life settlement transactions.¹³ Some states regulate viatical settlement transactions but not life settlement transactions.¹⁴ In states that regulate the purchase and sale of in-force life insurance policies and require the Settlement Company to hold a license issued by the state insurance department, state insurance laws adopted to effectuate GLB’s privacy mandates will apply. Generally speaking, this means that the NAIC Privacy Regulation will apply, subject to any privacy provisions of the viatical or life settlement laws of these states.

The NAIC Privacy Regulation regulates the disclosure of two categories of nonpublic personal information: (i) nonpublic personally identifiable financial information (“NPF”) and (ii) nonpublic personally identifiable health information (“NPH”), which are received by a licensed insurer, producer or other person licensed or required to be licensed under state insurance law (a “licensee”) from or about a “consumer” or a “customer.” Insurance licensees must deliver privacy notices only to their “consumers” and “customers” in certain circumstances.

Prospective and actual viators do not squarely meet the definitions of a “consumer” or “customer” under the NAIC Privacy Regulation. A “consumer” is “an individual who seeks to obtain, obtains or has obtained an insurance product or service from a licensee that is to be used primarily for personal, family or household purposes . . .”¹⁵ Arguably a viatical or life settlement transaction is not an insurance product or service inasmuch as it is not a

product or service provided by an insurance company or agent. Thus, if a viatical or life settlement is not an insurance product or service, then a prospective or actual viator is not a “consumer” of a viatical or life settlement company. A “customer” is “a consumer who has a customer relationship with a licensee.”¹⁶ Therefore, if a prospective or actual viator is not a “consumer,” he or she cannot be a customer. Moreover, the NAIC Privacy Regulation expressly states that a “consumer” does not have a continuing relationship with a licensee “if the individual is no longer a current policyholder of an insurance product or no longer obtains insurance services with or through the licensee.”¹⁷ Naturally, after a viator has sold his or her life insurance policy to the Settlement Company, the viator is no longer a policyholder. In all viatical or life settlement transactions regulated under state insurance laws, the viator must receive an all cash payment in exchange for the sale of his or her life insurance policy, and thus there is no continuing financial relationship between the Settlement Company and the viator; although, the Settlement Company usually tracks the health of the insured after the settlement transaction.

Nevertheless, a viatical or life settlement is likely within the ambit of the definition of an “insurance product or service” under the NAIC Privacy Regulation. To be sure, the NAIC’s Privacy Q&A dated October 1, 2001 states that, in the NAIC’s view, a licensee under viatical settlement laws is subject to the NAIC Privacy Regulation.¹⁸ Therefore, in states that have adopted the NAIC Privacy Regulation, the Settlement Company should comply with the NAIC Privacy Regulation, subject to whether that state has also adopted the NAIC’s Viatical Settlement Model Act or similar law. In states that do not regulate the Settlement Company as an insurance “licensee,” the Federal Trade Commission’s Privacy of Consumer Financial Information (the “FTC Privacy Regulation”) should apply because the FTC retains residual jurisdiction over financial institutions that are not subject to GLB privacy regulations promulgated by other federal agencies.

Beyond the NAIC Privacy Regulation and the FTC Privacy Regulation, the Settlement Company may be subject to viatical industry-specific privacy laws and regulations because some states that regulate the viatical and life settlement industry may have adopted the NAIC’s Viatical Settlements Model Act (“Viatical Settlements Act”), which contains specific provisions relating to the privacy of personal information. In states which have adopted the Viatical Settlements Act, the Settlement Company must obtain the prior written consent of the viator and the insured in order for the Settlement Company to lawfully disclose the insured’s identity or financial or medical information. In addition, Section 8 A (9) of the Viatical Settlements Act mandates that a viatical settlement provider or broker provide a disclosure to each viator which contains, among other items, the following statement regarding privacy:

All medical, financial or personal information solicited or obtained by a viatical settlement provider or viatical settlement broker about an insured, including the insured’s identity or the identity of family members, a spouse or a significant other may be disclosed as necessary to effect the viatical settlement between the viator and the viatical settlement provider. If you are asked to provide this information, you will be asked to consent to the disclosure. The information may be provided to someone who buys the policy or provides funds for the purchase. You will be asked to renew your permission to share information every two years.

The NAIC Model Viatical Settlements Regulation (the “Viatical Settlement Regulation”) further states that a “viatical settlement provider, viatical settlement broker or viatical settlement investment agent shall obtain from a person that is provided with patient identifying information a signed affirmation that the person or entity will not further divulge the information without procuring the express, written consent of the insured for the disclosure.”

In effect, the Viatical Settlement Act and Viatical Settlement Regulation go further than the NAIC Privacy Regulation and require that the Settlement Company obtain an opt-in from an insured with respect to the Settlement Company’s disclosure of the insured’s personal health information and an affirmation from the disclosees of the Settlement Company that the disclosees will not redisclose such information.

Accordingly, in states (1) that have adopted the NAIC Privacy Regulation and (2) in which the Settlement Company is licensed as a viatical or life settlement provider, the Settlement Company is subject to the NAIC Privacy Regulation. In states that have adopted both the NAIC Privacy Regulation and the Viatical Settlements Act, the Settlement Company is subject to the NAIC Privacy Regulation (e.g., deliver the requisite privacy notice) and, under the Viatical Settlements Act, it must obtain the prior written consent of the viator and the insured in order for the

Settlement Company to disclose the insured's identity or financial or medical information. Finally, in states that have adopted the Viatical Settlements Act but not the NAIC Privacy Regulation, the Settlement Company must only obtain the prior written consent of the viator and the insured in order for the Settlement Company to disclose the insured's identity or the insured's financial or medical information. In states that have not adopted either the NAIC Privacy Regulation or the Viatical Settlements Act, the Settlement Company is subject to the FTC's Privacy Regulation (e.g., deliver the required privacy notice).

HIPPA Analysis

The HIPAA Privacy Regulation governs Covered Entities: health plans, health care clearinghouses, and certain health care providers. "Health Plans" are defined as any individual or group plan that provides or pays the cost of medical care. There are 27 enumerated examples of Health Plans, including health insurers, HMOs, Medicare supplement policy issuers, long-term care policy issuers, and ERISA plans that provide medical care to employees or dependents via insurance, reimbursement or otherwise that have 50 or more participants or are administered by an entity other than the employer. However, Health Plans specifically exclude any policy, plan or program to the extent it provides for or pays for the cost of "Excepted Benefits," which include life insurance. "Health Care Clearinghouses" are entities that process health information received in a nonstandard format or containing nonstandard data into standard data or standard transactions, or receive standard transactions and process health information into nonstandard format or nonstandard data. "Health Care Providers" are broadly defined as any provider of medical or health services and any other person who furnishes, bills or is paid for health care in the normal course of business. The Settlement Company is not a Health Care Clearinghouse or a Health Care Provider and thus not a Covered Entity of any kind.


Covered Entities must, when dealing with protected health information, conduct themselves in accordance with the HIPAA Privacy Regulation relating to notice of use or disclosure of protected health information, consent or authorization for such use and disclosure, and the patient's rights to access, correct and receive an accounting of certain disclosures of such information. Furthermore, Covered Entities generally may only use and disclose protected health information in the "minimum amount necessary" for the particular purpose of the use or disclosure (the "Minimum Necessary Rule"). Although the Settlement Company is not directly subject to the HIPAA Privacy Regulation because the Settlement Company is not a "health plan" or other type of Covered Entity under HIPAA,¹⁹ the Settlement Company must be mindful of the "Minimum Necessary Rule," as the Settlement Company usually receives personal health information about insureds from Health Care Providers to evaluate life expectancies of insureds and make bids to purchase life insurance policies.

Conclusion

The determination of how the privacy laws and regulations created by GLB apply to the Settlement Company is a challenging task because these laws and regulations were not drafted with the viatical or life settlement industry in mind. Moreover, in the case of state insurance privacy laws and regulations adopted largely through the efforts of the NAIC's Privacy Working Group, the NAIC's Viatical Settlements Working Group has the responsibility for developing the regulation of all aspects of viatical and life settlement transactions, including uses and disclosures by Settlement Companies of nonpublic personal information about viators and insureds. However, it is clear that Settlement Companies are not subject to HIPAA. Nevertheless, because the viatical and life settlement industry's use and disclosure of nonpublic personal health information about insureds is at the heart of this business, privacy compliance may be yet another bugaboo for this industry.

Endnotes

1. A viatical settlement company purchases an in-force life insurance policy for an amount less than its death benefit where the insured has, at the time of such purchase, a catastrophic, life threatening or terminal illness.
2. 45 CFR §§ 161.101 et. seq. and 164.500 et. seq.

3. 45 CFR § 164.534.
 4. 45 CFR § 160.102 and § 164.500.
 5. 15 U.S. C. § 6809(3).
 6. Note that many states have recently amended their statutory definitions of a “security” under blue sky laws to regulate certain viatical investment transactions as a security, which further complicates the privacy compliance obligations of the Settlement Company.
 7. *See* 12 U.S.C. § 1843(k)(A)-(E).
 8. GLB § 505(a) (emphasis added).
 9. 15 U.S.C. § 6807(b).
 10. *See* NAIC’s web site at <http://www.naic.org/1privacy/>.
 11. *See, e.g.,* Alabama, Arizona, Colorado, District of Columbia, Georgia, Hawaii, Idaho, Maryland, Missouri, New Hampshire, Rhode Island, South Carolina, South Dakota, West Virginia, and Wyoming.
 12. *See, e.g.,* Alaska, Florida, Indiana, Iowa, Kansas, Kentucky, Massachusetts, Mississippi, Nebraska, Nevada, North Carolina, North Dakota, Ohio, Oklahoma, Tennessee and Texas.
 13. *See, e.g.,* Arkansas, California, Connecticut, Delaware, Illinois, Louisiana, Maine, Michigan, Montana, New Jersey, New Mexico, New York, Vermont, Virginia, Washington, Wisconsin.
 14. NAIC Privacy of Consumer Financial and Health Information Regulation, § 4, F(1).
 15. NAIC Privacy of Consumer Financial and Health Information Regulation, § 4, I.
 16. NAIC Privacy of Consumer Financial and Health Information Regulation, § 4, J(2)(iii).
 17. NAIC Privacy Q&A, “What Entities and What Lines of Insurance are Covered by the Model,” Section 1.
 18. Note that life insurance companies are not Covered Entities because they too are not “health plans” as life insurance is an “excepted benefit.”
 19. Note that life insurance companies are not Covered Entities because they too are not “health plans” as life insurance is an “excepted benefit.” 
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