

## **VIRGINIA INSURANCE ISSUES REGARDING PRE-NEED AND FINAL EXPENSES**

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### **INTRODUCTION:**

According to a 2007 survey by AARP, 34% of the over 50 years of age population has done some pre-planning and 23% have pre-paid a portion or all of the funeral or burial expense for themselves or someone else.<sup>1</sup> That translates into 20,000,000 people age 50 or older who have already paid some funeral expenses or made provisions for such payments.<sup>2</sup> Once your pre-planned arrangements are set you can elect to pay a portion or all of the bill before your death. This lifts the burden from family members and helps insure that the decedent's wishes are carried out. There are three main ways to fund a pre-paid funeral:

- A. Final Expense Insurance ("FEI")
- B. Pre-Need Insurance ("PNI")
- C. Pre-Need Trust ("Trust")

FEI is basically a life insurance policy with a low face value somewhere between \$5,000 and \$50,000 that you buy from a fully licensed life insurance agent representing a licensed and approved life insurance carrier. You can name any beneficiary who would make a claim at the time of your death and receive the money upon your death. That beneficiary normally would be responsible for using the cash proceeds to carry out your wishes. For example, if you have a final expense insurance policy for \$20,000 and your burial services end up costing \$15,000.00, your beneficiary would pay the bill and keep the extra \$5,000.00. Final expense insurance policies are normally low face value term or whole life policies.

PNI is different and is intended for the person who has selected specific arrangements at a funeral home and wants the assurance that those arrangements will be paid for and implemented. Unlike FEI, which you buy through a fully licensed insurance agent, PNI is sold by a funeral home director who is also licensed but is a "limited insurance licensed agent."<sup>3</sup> A limited insurance licensed agent normally does not have the multitude of continuing education requirements, exams, etc. that are required of a fully licensed life insurance agent.<sup>4</sup> Normally under a pre-need arrangement, the insured pays for this policy with a one-time premium or periodic payments and the beneficiary (normally a family member) executes an assignment of the proceeds to the funeral home. From an informal inquiry, three of the largest pre-need insurance companies, Forethought, Homesteaders and National Guardian, estimate that over 95% of their policies are offered at a guaranteed price.<sup>5</sup> Normally the funeral director makes the claim, receives the money and carries out the decedent's (insured's) wishes. Pre-need insurance laws vary by state and New York does not allow the sale of pre-need insurance at all.<sup>6</sup>

Trusts. Another option is to make prearrangements with your funeral director and fund those arrangements by putting cash into a trust which holds the money until your death and then disburses it to the funeral home. The arrangement also relieves your family of last minute decisions. Your payment for funeral arrangements is deposited into a federally or state insured bank until your death. Depending on your estate, your money may be put into individual cash trust accounts or "master trust accounts" which pools many individual trusts. The value of the trust can rise and fall depending on the investment performance elected by the funeral director;

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however, if you have a guaranteed price contract from your funeral director, he takes on the market risks and must provide the services that have been selected by the decedent no matter how well or poorly the trust investments have performed.

### ISSUES:

New Virginia Insurance Advertising Regulation.<sup>7</sup> Virginia, effective July 1, 2011, has promulgated rules governing advertisement of life insurance and annuities. This new rule was published and distributed by the Virginia Bureau of Insurance ("VABOI") a year ago with a request for comments. The new rule states "an advertisement for life insurance or an annuity in which the face amount or any part of the face amount is based on actual or estimated cost of funeral goods or services shall contain the following disclosure: "This is (life insurance or an annuity). This (life insurance or annuity) does not specifically cover financial goods or services. The beneficiary of this (life insurance or annuity) may use the proceeds of this (life insurance or annuity) for any purpose, unless otherwise directed. The face amount of this life insurance is not guaranteed to increase at the same rate as the cost of a funeral increase."<sup>8</sup> This new regulation became effective July 1, 2011 and has caused unrest among both pre-need insurance companies and final expense insurance companies.

First, there appears to be confusion as to whether it is applicable only to insurance for final expense and not to pre-need or applicable to all insurance policies. Second, as a practical matter, almost every life insurance policy sold in Virginia is likely to be based on some cost related to burial expenses. This probably places an unintended consequence on the VABOI by imposing a burden upon itself to review the marketing materials and advertisements of all insurance companies so as to equally apply this new regulation. Third, I believe that it is a regulation that adds unnecessary cost and burdens to all insurers doing business in Virginia, creates a new enforcement obligation upon the VABOI and may allow one portion of the marketplace (pre-need) to have a benefit over other life insurance companies who specifically market their product for final expense. Fourth, since this new regulation appears to be a result of a combination of the Code of Virginia, the old Chapter 40 of our Virginia Administrative Code and the NAIC Model Regulation (on this subject) it has become confusing to insurers. Finally, I would suggest that it is a solution looking for a problem that really does not exist in the Commonwealth of Virginia.

Hopefully our VABOI has been listening to comments from the entire industry and that either amendments to this new regulation or reconsideration and possible revocation could be in the near future.

Excess Funds for Medicaid Recipients. A funeral home director who operates his business in Virginia can legally establish an irrevocable trust for an individual for the purpose of paying for funeral and burial expenses. Under a "two-step" process, funds transferred from the individual to the funeral home are deemed a compensated transfer for value when the amount of the funds transferred does not exceed the value of the goods and services purchased. The entire amount of the trust is exempt from Medicaid eligibility when placed in an irrevocable trust by the funeral director.

The two-step process occurs when (a) the individual signs a pre-need contract with the funeral home director promising pre-payment in return for specific funeral merchandise and services and pays the agreed upon amount in the form of a direct cash payment or purchase of a life insurance policy or annuity to the funeral director; (b) then, the funeral home director in turn places the money, life insurance policy or annuity into a trust, established by a person other than the individual.

Virginia, as well as other states, are considering the situation where an individual who is a recipient of Medicaid, purchases a pre-need contract (either using all cash or funding it with insurance) and then dies and the decedent's beneficiaries elect to direct the funeral home director to provide a less expensive funeral than the one original contracted by the decedent. This "excess fund" or "Medicaid Reimbursement" topic is becoming a paramount issue in light of the economy and in light of the cut backs by the federal government

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and Medicaid funding to all states. New Jersey has a specific statute dealing with excess insurance proceeds or excess cash proceeds when placed in trust for a decedent who is a recipient of Medicaid.<sup>9</sup> This statute is relatively specific and states that in the case of an irrevocable funeral trust (presumably a cash trust) of a decedent who is a Medicaid recipient "the entire remainder after the payment of funeral and burial goods and services shall be paid to the Division of Medical Assistance and Health Services in the Department of Human Services, as though the division were the purchaser of the trust." It further specifically applies to an irrevocably assigned "newly issued funeral insurance policy of a decedent who is a Medicaid recipient" and states that this policy will not be excluded as a resource unless the Division of Medical Assistance and Health Services is named the sole beneficiary of the policy. This statute further states that "as an alternative to being named beneficiary, (DMAS) can be named as a payee of the balance of any remaining monies subsequent to the delivery of funeral and burial goods and services, . . ." <sup>10</sup> California and Ohio have provisions applicable to annuity contracts or life insurance policies making the individual's estate as an alternative beneficiary and thus presumably subject to Medicaid's ability to recover from the estate any funds in excess of the cost of a pre-need contract or funeral services.<sup>11</sup> Although New York does not allow insurance to be used for pre-need contracts, it does allow cash trusts and it requires that the agreement have a provision that "if any money is left over after your funeral and burial expenses have been paid, it will go to the County."<sup>12</sup> Similar to Virginia, New York probably delegates to its Counties the responsibility of handling all Medicaid eligibility and reimbursement issues. The new (effective July 1, 2011) Indiana statute on this Medicaid Reimbursement issue is pretty unique. It allows the state to use federal or state Medicaid funds to pay life insurance premiums and expenses for a Medicaid applicant or recipient who has irrevocably named the state as the beneficiary of an in force life insurance policy or assigned a life insurance policy to the state. It also provides that life insurance proceeds that exceed the amount of Medicaid benefits be paid to the beneficiary of the recipient and that the value of a life insurance policy owned by an applicant or recipient may not be considered in determining Medicaid eligibility if the applicant or recipient has irrevocably named the state as the beneficiary or assigned the life insurance policy to the state.<sup>13</sup>

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### Endnotes

1. [www.insure.com](http://www.insure.com); Tips for Buying Pre-Need and Final Expense Insurance, last updated June 1, 2010
2. *Id.*
3. § 38.2-1800 Code of Virginia (1950, as amended); § 54.1-2800 to § 54.1- 2825 Code of Virginia (1950, as amended)
4. § 38.2-1800 et seq., Code of Virginia (1950, as amended)
5. Forethought Life Insurance; Mr. Walt Dixon, Forethought Center, Batesville, IN 47006; Homesteaders Life Insurance, Mr. Gerry Kraus and Ms. Tracy Kelly, 5700 Westown Parkway, West Des Moines, IA 50266; National Guardian Life Insurance Company, Mr. Mark Neidinger, 2 East Gilman Street, Madison, WI 53703
6. Preneed Funeral and Burial Agreements: A Summary of State Statutes, written by Sandra B. Eskin, December 1999 © 1999 AARP Public Policy Institute.
7. 14 VAC 5-41-10 et seq. (effective July 1, 2011).
8. 14 VAC 5-41-40(H).

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9. New Jersey Statute Annotated: § 2A:102-22 (a) and (b).
10. Id.
11. California Chapter 22 HF No. 351(D); Ohio Administrative Code § 5101:1-39-30
12. New York General Business Law § 453
13. Indiana Code § 12-15-1-21