IN THE COURT OF APPEALS OF THE STATE OF OREGON

AMERIVEST FINANCIAL, LLC, Plaintiff-Appellant, Cross-Respondent, v. LEWIS P. MALOUF; and CHARLES FINANCIAL LLP, Defendants, and PACIFIC NORTHWEST TITLE AND ESCROW COMPANY; ROBERT TAUROSA; IDEAL SETTLEMENTS; and MICHAEL A. AMATO, Defendants-Respondents Cross-Appellants.	)	Multnomah County Circuit Court No. 0802-01987 CA No. A144457

Appeal from the Judgment of the Multnomah County Circuit Court

Honorable Henry Kantor, Judge

PROPOSED AMICUS BRIEF OF THE NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION, INC.

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STATEMENT OF INTEREST

The North American Securities Administrators Association, Inc. ("NASAA") is the non-profit association of state, provincial, and territorial securities regulators in the United States, Canada, and Mexico. It has 67 members, including the securities regulators in all 50 states, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands. Formed in 1919, NASAA is the oldest international organization devoted to protecting investors from fraud and abuse in connection with the offer and sale of securities.

The members of NASAA include the state agencies that are responsible for regulating securities transactions under state law. Their fundamental mission is protecting investors, and their jurisdiction extends to a wide variety of securities, including "investment contracts." Their principal activities include registering certain types of securities, such as life settlements; licensing the firms and agents who offer and sell securities; investigating violations of state law; and, where appropriate, filing enforcement actions. State securities regulators also educate the public about investment fraud and advocate for the adoption of strong, fair, and uniform securities laws and regulations at both the state and federal level.

NASAA supports the work of its members by coordinating multi-state enforcement actions, offering training programs, publishing investor education materials, and presenting the views of its members in testimony before Congress on matters of securities regulation. Another core function of the association is to

represent the membership's position, as *amicus curiae*, in significant cases involving the interpretation of securities laws and the rights of investors.

STATEMENT OF THE CASE

NASAA and its members have a substantial interest in the outcome of this appeal for several reasons. First, the investments involved in this case have been the focus of numerous state enforcement actions because of the abuses involved in the marketing and sales of these products, and the trial court's erroneous conclusion that the investment program was not a security will have an adverse impact on the ability of regulators to bring successful enforcement of securities law violations. Specifically, the trial court's ruling that the life settlements were not securities under an investment contract analysis stands well outside the mainstream of state securities law and will accordingly narrow the jurisdiction of the state securities regulator and weaken the deterrent effect vital to state securities regulation. Finally, if the trial court's ruling is not reversed, it will have a far-reaching impact by undermining investor protection not only in Oregon, but in other jurisdictions as well. As a result, in a very real sense, the citizens of Oregon, and potentially elsewhere, will be more vulnerable to fraud and abuse in the offer and sale of securities.

NASAA relies on the Statement of the Case as presented by Plaintiff-Appellant, Amerivest Financial, LLC, in its Opening Brief and Excerpt of Record, filed in this Court, on January 18, 2011.

STATEMENT OF FACTS

NASAA relies on the Statement of Facts as presented by Plaintiff-Appellant, Amerivest Financial, LLC, in its Opening Brief and Excerpt of Record, filed in this Court, on January 18, 2011.

ARGUMENT

I. LIFE SETTLEMENTS MUST BE REGULATED AS SECURITIES FOR THE PROTECTION OF ALL INVESTORS.

A life settlement occurs when "an insurance policy owner sells a life insurance policy to a third party for an amount that exceeds the policy's cash surrender value, but is less than the expected death benefit of the policy."[1] SEC, "Life Settlements Task Force" at 3 (July 22, 2010) ("SEC Report"). Life settlements are typically made up of two transactions. The first transaction is the sale of an insurance policy by its owner to a third party provider, and is regulated by a majority of states under their insurance laws.[2] GAO, "Life Insurance Settlements: Regulatory Inconsistencies May Pose a Number of Challenges" at 5 (July 2010) ("GAO Report"). The second transaction, the investment in the life settlement itself, is the sale of the insurance policy by the third party provider to an investor. GAO Report at 5. This second transaction is a securities transaction regulated under state and federal law. GAO Report at 5. The life settlement

[1] SEC, "Life Settlements Task force" (July 22, 2010), *available at* http://www.sec.gov/news/studies/2010/lifesettlements-report.pdf

[2] GAO, "Life Insurance Settlements: Regulatory Inconsistencies May Pose a Number of Challenges" (July 2010), *available at* http://www.gao.gov/new.items/d10775.pdf.

market grew out of the viatical settlement market when third party providers started looking beyond terminally ill policy holders. SEC Report at 4. Viatical investments are similar to life settlement transactions, but viatical investments typically involve policyholders with shorter life expectancies.[3]

As will be demonstrated below, life settlement investments are viewed as securities by the overwhelming majority of states, under federal law, and even by the securities industry itself. Therefore, a decision holding that life settlements are not securities will disrupt the overwhelmingly uniform treatment of these products as securities and create an Oregon specific regulatory gap ripe for exploitation by financial predators.

A. Public Policy Requires That Oregon Securities Laws Be Construed Broadly For The Good Of All Investors.

Over the last decade, there have been widespread problems in the sale of life settlement investments, and as a result, thousands of investors have lost significant amounts of money.[4] The patterns of investor abuse in the sale of life

[3] "The transaction of selling one's policy to a life settlement provider is referred to as either a viatical settlement or a life settlement. The only difference between the two terms is that viatical settlements deal with insured individuals who have a life expectancy of less than twenty-four months and life settlements deal with individuals who are expected to live more than twenty-four months." Sachin Kohli, Comment, *Pricing Death: Analyzing the Secondary Market for Life Insurance Policies and its Regulatory Environment*, 54 BUFF. L. REV. 279, 281 (2006)

[4] State securities regulators have brought many enforcement actions related to fraudulent life settlement investments. The U.S. Securities and Exchange Commission ("SEC;" the federal securities regulator) and the Financial Industry Regulatory Authority ("FINRA;" the industry self-regulatory orgsnization) have also taken similar actions. For example, in *SEC v. American Settlement*

settlement investments are well documented. Many investors have sustained losses due to outright fraud, as when life settlement companies sell non-existent policies or pocket investment proceeds. Other investors have lost their investments when life settlement companies misrepresent the medical condition of the policy holders, particularly if the certifying physicians are not truly independent.[5] Sales agents have asserted bold, but unfounded claims, about the rates of return on life settlement investments, leading to unsuitable purchases and sales that have been ruinous for investors.

Likewise, there are many risks inherent in life settlement investments and these risks may not be adequately disclosed to prospective investors. For example, rates of return are difficult to predict – and yields vary greatly – because of uncertainties in calculating the policy holders' life expectancy. The health of policy holders must be monitored so death certificates can be obtained at the proper time. There is no return whatsoever until the policy holders die and claims for death benefits are properly filed and paid. There is little recourse for an

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Associates, LLC, et al., the SEC alleged that the defendants sold almost $3.5 million in life settlement policies to investors, but failed to use the investors' money, as promised, to cover premium payments. See SEC Report Appendix C-1. Another example is *SEC v. Lydia Capital, LLC et al*. In this case, the SEC charged the defendants with engaging in a scheme to defraud approximately $34 million from investors who were told their funds would be used to acquire life settlements. See SEC Report Appendix C-1. FINRA enforcement actions are also showcased in the SEC Report, in Appendix D.

[5] In many instances, policies have been sold with assurances that the policy holder is ill and likely to die soon. When policy holders live on, investors find that premiums must be paid for indefinite periods to avoid lapse of policies and forfeiture of investments.

investor needing access to his or her funds because a secondary market for life settlement investments is non-existent. Policies that have been transferred may not be honored by the insurance companies that issued them. Policies may still be in their contestable periods. Term or group policies may be subject to subsequent contract changes. Policy holders may not have taken all the necessary steps to perfect the transfer of interests in their policies, and surviving family members may contest the transfer of such interests.

The Oregon Supreme Court has "held that the Oregon Blue Sky Law [] is to be "'liberally construed to afford the greatest possible protection to the public.' *Adamson v. Lang*, 236 Or. 511, 516, 389 P.2d 39 (1964); *Spears v. Lawrence Sec., Inc.*, 239 Or. 583, 587, 399 P.2d 348 (1965), and *Gonia v. E.I. Hagen Co.*, 251 Or. 1, 3, 443 P.2d 634 (1968)." *Adams v Am. W. Sec.*, 265 Or. 514, 524, 510 P.2d 838, 842 (1973). Given the myriad of problems associated with these investments as outlined above, public policy necessitates that Oregon securities laws be construed broadly to include life settlement investments in the definition of a security. An Oregon decision holding that investments in life settlements are not securities will set a negative precedent that will harm Oregon investors and, serve as a means by which unscrupulous promoters will argue both here, and in other jurisdictions, that these investments are not securities and are not subject to the investor protection provisions in state securities law. Oregon securities laws should be construed broadly for the good of all investors, and life settlement

investments should be treated as securities, thereby providing investors with all the rights and protections afforded by the Oregon securities law.

B. The Overwhelming Majority Of States Regulate Investments In Life Settlements As Securities.

All but two states regulate investments in life settlements as securities under their respective state securities laws. GAO Report at 6. "Thirty-fives states have statutes defining a "security" or "investment contract" to expressly include investments in life settlements under their securities laws." GAO Report at 53. The remaining "[t]hirteen [] states and the District of Columbia [] apply the investment contract test to life settlement investments to determine whether these investments fall within the definition of a security and are subject to their securities laws." GAO Report at 54.

As the "local cops on the beat," state securities regulators have long been concerned with the dangers inherent in life settlement transactions.[6] In 2002, in response to many of the problems it was seeing in the life settlement market, NASAA issued its "Guidelines Regarding Viatical Investments." ("2002 Guidelines").[7] As previously noted, viatical investments are similar to life settlement transactions, differing only in the insured's life expectancy. In the 2002 Guidelines, NASAA affirmatively adopted the position that "viatical investments,

[6] "[S]tate [] securities regulators have played the primary role in protecting investors by regulating the sale of life settlement investments." GAO Report at 7.
[7] NASAA Guidelines Regarding Viatical Investments, *available at* http://www.nasaa.org/content/Files/NASAA_Guidelines_Regarding_Viatical_Investments.pdf

commonly known as investments in viatical, senior or *life settlement contracts*, are securities and must be registered with a state securities division as required by state law." *Id.* at 1 (Emphasis added). The 2002 Guidelines also asserted that "this type of investment is unsuitable for the financial needs and interests of the average individual investor." *Id.*

Regulation of the life settlement industry under the securities laws is necessary because life settlements have proven to be fertile ground for investor abuse. Over the years, NASAA and its members have been particularly successful in dealing with the harms associated with life settlement investments.[8] For example, in May 2007, the Colorado Division of Securities filed an enforcement action against Life Partners and its affiliates and agents. The Colorado Division of Securities alleged that from 2004 to 2007, the defendants sold unregistered viatical settlement investments to at least 110 Colorado investors, netting over $11 million. The Department also alleged that the Life Partners sales agents were unregistered and that they marketed the investments using fraudulent misrepresentations and omissions about the risks, costs, and returns associated with viaticals. In December 2008, the court held that the offerings were unregistered securities marketed through unlicensed agents. Life Partners

[8] Unfortunately, unscrupulous elements in the life settlements industry continue to target our nation's investors, and state securities regulators continue their fight against fraud and abuse. Life settlements were recently identified as one of the top investor traps in NASAA's 2009 "Top 10 Investor Traps" list, *available at* http://www.nasaa.org/NASAA_Newsroom/Current_NASAA_Headlines/11129.cfm.

subsequently stipulated to a permanent injunction and agreed to make a rescission offer to all Colorado investors. See *Joseph v. Life Partners, Inc.*, No. 07CV5218 (Denver D. Ct. Dec. 2, 2008).

Another example of a state securities regulator taking a life settlements related action was a March 2009 case by the Securities Bureau of the Idaho Department of Finance. The Idaho Securities Bureau filed a complaint against a group of entities and individuals who defrauded 40 Idaho investors of more than $5 million by selling them unregistered securities in the form of a "life settlement purchase" program. The Complaint alleged that the defendants promised returns of 10% per month, but in fact never purchased any insurance policies and instead diverted the investors' funds to offshore accounts for defendants' personal use. The Idaho Securities Bureau sought injunctive relief, restitution, and substantial civil penalties. In January 2010, the defendants stipulated to the unregistered sale of securities, a permanent bar from offering or selling securities in Idaho, and $5,373,464 in restitution to Idaho victims. See *State of Idaho, Dept. of Fin., Sec. Bur. v. Potter*, CV OC 0905488 (D. Ct. 4th Jud. Dist. Mar. 20, 2009).

A third example involves an April 2009 case where the Texas State Securities Board issued an Emergency Cease and Desist Order against The Stamford Group and its affiliates and principals, who were selling interests in portfolios of senior life settlement policies. The Texas Board found that the investments were unregistered securities and that the respondents were not properly licensed to sell them. The Board also found that the respondents were

making numerous misrepresentations and omissions in the sale of the investments, including bold claims of guaranteed returns and omissions regarding the principals' complaint history. See *In the Matter of the Stamford Group, Inc.*, No. ENF.-09-CDO-1671 (Tex. Secs. Bd. Apr. 2, 2009).

State securities actions against life settlement providers and companies have sent an important message of deterrence to other providers and companies that might consider fraudulently selling in – or relocating to – a particular state. In the instant case, the trial court's ruling threatens to eliminate this deterrent effect in Oregon. A judicially created gap in Oregon securities law will attract financial predators that have been turned away by the overwhelming majority of states that continue to regulate life settlements as securities.[9] Unethical life settlement providers will prey upon the citizens of Oregon to a disproportionate degree, viewing them as safe targets of fraud and abuse.

In addition to the deterrent effect, uniformity amongst the states is important for another reason: it not only maximizes investor protection nationwide, it also promotes fairness. Uniformity helps ensure that the citizens of

[9] Should this Court find that the facts of this case are truly unique and therefore do not meet the definition of a security (and NASAA does not believe that it should so find), NASAA urges this Court to limit its holding on the facts here presented. In the interests of investor protection, NASAA asks that the Court make clear that it is *not* ruling that life settlements are not securities as a matter of law. Otherwise, the court will leave Oregon's position on life settlements ambiguous and therefore make the investing public of the State of Oregon an attractive target for frauds based on the sale of life settlements.

every state receive investor protection in roughly equal measure, so that no state becomes a preferred haven for financial fraud.

C. The Oregon Division Of Finance And Corporate Securities Has Determined That Life Settlements Are Securities Under State Law.

The Oregon Department of Consumer and Business Services, Division of Finance and Corporate Securities ("DFCS") is the state agency responsible for administering Oregon's securities laws and regulations. The DFCS is responsible for, *inter alia*, the registration or denial of registration of securities (ORS 59.075), licensing of broker-dealers and salespersons (ORS 59.165), general supervision of persons dealing in securities (ORS 59.235), and investigations of violations and enforcement of the Oregon Securities Law (ORS 59.245).

Oregon law states that "the court shall not substitute its judgment for that of the agency as to any issue of fact or agency discretion." ORS 183.482(7). Further, Oregon case law provides that an agency's interpretation may be given an appropriate degree of assumptive validity if the agency was involved in the legislative process or if the court infers that the agency has expertise based upon qualifications of its personnel or because of its experience in the application of the statute to various facts. *Springfield Educ. Ass'n v. School District* 290 Or. 227-228, 621 P.2d 547 (1980). Additionally, the court's review of an interpretation of a delegative term is largely deferential when the agency has special expertise and has made a statutory interpretation at least as plausible as any challenger's. See

Lombardo v. Warner, 340 Or. 264, 270-71, 132 P.3d 22 (2006); *Booth v Tektronix*, 312 Or. 463, 473, 823 P.2d 402 (1991).

In October 2006, the DFCS prepared a memorandum on the "Regulation of Life Settlements" ("DFCS Memo"). See attached Memorandum from Kevin Anselm, Chief of Enforcement, on Regulation of Life Settlements as Securities to Patrick A. Fitzgerald, Enforcement Officer (Oct. 13, 2006). After providing a brief summary on the regulation of life settlements as securities, the DFCS Memo concluded that "life settlement investment[s] meet[] the modified *Howey* test and [are] an investment contract and therefore [securities] under Oregon law." DFCS Memo at 6. Given that DFCS is responsible for enforcing the state's securities laws, the conclusion in the DFCS memo that life settlement investments are securities under the Oregon Securities Act should be given due deference and DFCS's judgment and discretion on this matter should govern.

D. There is Significant Support For The Treatment Of Life Settlements As Securities In Federal Law.

In recent years, the issue of whether life settlement investments should be treated as securities has become more settled due in large part to pronouncements by the SEC as well as a federal appeals court decision holding that viatical contracts were in fact securities. In *SEC v. Mutual Benefit Corp.*, 408 F.3d 737 (11th Cir. 2005), the SEC filed an action against a promoter that had sold over $1 billion in viatical investments to 29,000 investors through a fraudulent marketing campaign. *Id.* at 738-741. The defendant invoked the decision in *SEC v. Life*

Partner, 87 F.3d 536, 318 U.S. App. D.C. 3025 (D.C. Cir. 1996) to challenge the SEC's jurisdiction, but the Eleventh Circuit squarely rejected that challenge. *Id.* at 743. Citing to the lack of a persuasive rationale underlying *Life Partners*, and to Supreme Court precedent requiring a flexible – not technical – application of the securities laws, the court held that Mutual Benefits' viatical investments "amount[ed] to a classic investment contract." *Id.* at 744.

Adding further support, the SEC released the report of its Life Settlements Task Force ("Task Force") on July 22, 2010. The Task Force met with NASAA, other regulators, and members of industry. *See* SEC Report Appendix B. In its report, the Task Force recommended that the SEC "consider recommending to Congress that it amend the definition of "security" under the Securities Act of 1933, the Securities Exchange Act of 1934, and the Investment Company Act of 1940 to include life settlements." SEC Report at 39. The Task Force made this recommendation based upon the belief that "this amendment to the definition of "security" would bring clarity to the status of life settlements under the federal securities laws and provide a more consistent treatment for life settlements under both federal and state securities laws."[10] SEC Report at 39.

Concurrent with the release of the SEC Report, the Government Accountability Office ("GAO") released a report to the U.S. Senate's Special Committee on Aging regarding "Life Insurance Settlements." The GAO Report

[10] The Task Force recommended the amendment of the definition of "security" to include both viatical settlements and life settlements, since the only difference between the two is the life expectancy of the insured.

recognized that "[i]nconsistencies in the regulation of life settlements may pose a number of challenges." GAO Report at 6. The GAO Report concluded that *consistent* consumer and investment protection and financial oversight of the life settlements market had "not been fully achieved under the current regulatory structure[.]" GAO Report at 7. In its summary, the GAO Report recommended Congress "consider taking steps to help ensure that policy owners involved in life settlement transactions are provided a consistent and minimum level of protection." GAO Report at 24.

Both the SEC Report and the GAO Report indicate that the issue of life settlement investment transactions will be resolved on the federal level by an amendment to the definition of security to include life settlements. In fact, criminal prosecutions for the sale of life settlements are already occurring on the federal level. In October 2010, a defendant pleaded guilty in the Eastern District of Virginia for his role as a wholesaler for a group of businesses that sold life settlements to investors.[11] The defendant and his co-conspirators defrauded investors in 38 states and Canada of $100 million over a three year period.

E. Even The Securities Industry Considers Life Settlement Investments To Be Securities.

From at least 2002, the life settlement industry has supported the position that an investment in life settlements should be considered a security. In

[11] Press Release, U.S. Department of Justice, Texas Businessman Pleads Guilty in Virginia to Role in $100 Million Fraud Scheme Involving Life Settlements (Oct. 21, 2010) *at* http://www.justice.gov/opa/pr/2010/October/10-crm-1183.html

testimony before the Subcommittee on Oversight and Investigation of the Committee on Financial Services, of the House of Representatives, David M. Lewis, President of the Life Settlement Institute, asserted that the Securities Act of 1933 should be amended to include life settlement as securities.[12] *Retirement Protection: Fighting Fraud in the Sale of Death: Hearing Before the Subcomm. on Oversight and Investigation of the Comm. on Fin. Serv.*, 107th Cong. 47-62, 68 (2002), (statement of David M. Lewis, President, Life Settlement Institute). The life settlement industry's position was once again confirmed in a September 2009 testimony before Congress. In his written testimony, Russel Dorsett, the then President of the Life Insurance Settlement Association ("LISA") asserted that "LISA has steadfastly joined with the NASAA effort to establish that the regulation of investments in this arena must occur under state and federal securities laws …"[13]

In addition, FINRA,[14] a self-regulatory organization whose members are broker-dealers and registered representatives, has been vocal about life settlements

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[12] *Retirement Protection: Fighting Fraud in the Sale of Death: Hearing Before the Subcommittee on Oversight and Investigation of the Committee on Financial Services*, 107th Cong. (Serial No. 107-55) (2002), available at http://financialservices.house.gov/media/pdf/107-55.pdf

[13] *Recent Innovations in Securitization: Testimony Before the United States House of Representatives Committee on Financial Services Subcommittee on Capital Markets, Insurance and Government-Sponsored Enterprises* (Sept. 24, 2009, by Russel Dorsett, President, Life Insurance Settlement Association, *available at* http://financialservices.house.gov/media/file/hearings/111/dorsett_-_lisa.pdf.

[14] FINRA is the successor to the National Association of Securities Dealers, Inc. ("NASD").

as securities transactions.[15] In a 2009 Regulatory Notice to members, FINRA expressed its concern regarding the risks and costs associated with variable life settlements.[16] FINRA Reg. Notice 09-42. FINRA was unequivocal in its assertion that "variable life settlements are securities transactions that are subject to the federal securities laws and all applicable FINRA rules."[17] FINRA Notice to Members 06-38.

II. THE LIFE SETTLEMENT POLICIES THAT MALOUF OFFERED AND SOLD TO AMERIVEST ARE SECURITIES.

A. Life Settlements are Investment Contracts Under *SEC v. W.J. Howey*, 328 U.S. 293 (1946).

Congress drafted Section 2(a)(1) of the Securities Act of 1933 broadly "to encompass virtually any instrument that might be sold as an investment." *Reves v. Ernst & Young*, 494 U.S. 56, 61, 110 S.Ct. 945, 108 L.Ed.2d 47 (1990). To ensure a broad application, Congress included "investment contracts" in Section 2(a)(1) as a catch-all classification of securities. 15 U.S.C. § 77b(a)(1). The seminal U.S. Supreme Court case of *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946) established the federal standard for what constitutes an investment contract. In *Howey*, the Supreme Court declared that an investment contract exists wherever there is "an

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[15] About FINRA, *available at* http://www.finra.org/AboutFINRA/

[16] FINRA Reg. Notice 09-42, *available at* http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p119546.pdf.

[17] The NASD expressed virtually the same position in 2006, in its Notice to Members 06-38, *available at* http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p017131.pdf.

investment of money in a common enterprise with profits to come solely from the efforts of others." *Id.* at 301. Federal courts have consistently found life settlements and investment programs to purchase life settlements to be investment contracts, and therefore securities under *Howey*. *See* LOUIS LOSS, JOEL SELIGMAN & TROY PAREDES, SECURITIES REGULATION, 3, §2(a)(1)(f) n. 304 (2010) (citing *Hill & Ebert v. Dedicated Resources, Inc.*, 2001 Blue Sky L. Rep. (CCH) ¶74,246 (Kan. Dist. Ct. 2000) (holding that viatical settlement contracts satisfy all four elements of the *Howey* test); *SEC v. Mutual Benefits Corp.*, 323 F. Supp. 2d 1337 (S.D. Fla. 2004), aff'd, 408 F.3d 737 (11th Cir. 2005) (viatical settlements were securities); *SEC v. Tyler*, No. Civ.A.3:02 CV 0282 P, 2002 WL 32538418, at *3-6 (N.D. Tex. Feb. 21, 2002) (analyzing fractional shares in viatical settlements as both investment contracts under *Howey* and notes under Reves); *USAllianz Sec., Inc. v. S. Mich. Bancorp, Inc.*, 290 F. Supp. 2d 827, 828 (W.D. Mich. 2003); *Wuliger v. Christie*, 310 F. Supp. 2d 897, 901–908 (N.D. Ohio 2004) (viatical settlements constitute securities); *Wuliger v. Anstaett*, 363 F. Supp. 2d 917, 921–922 (N.D. Ohio 2005) (viatical settlements constitute securities); *Wuliger v. Owens*, 365 F. Supp. 2d 838 (N.D. Ohio 2005); *Wuliger v. Eberle*, 414 F. Supp. 2d 814 (N.D. Ohio 2006) (holding viatical investment to be a security and rejecting majority decision in Life Partners as unpersuasive)).

This test has also been widely adopted by state courts with only slight modifications in some jurisdictions. *See* 2 JOSEPH C. LONG, BLUE SKY LAW § 2.01 (2010). Accordingly, numerous state courts have also found that life settlements

and investment programs purchasing life settlements are securities. *See* LOUIS LOSS, JOEL SELIGMAN & TROY PAREDES, SECURITIES REGULATION, 3, §2(a)(1)(f) n.304 (2010) (citing *Siporin v. Carrington*, 200 Ariz. 97, 23 P.3d 92 (Ct. App. 2001) (viatical settlements are securities under *Howey*); *Joseph v. Viatica Mgmt.*, LLC, 55 P.3d 264 (Colo. Ct. App. 2002) (units in Viatica Fund which purchased viatical settlements of life insurance policies constituted investment contracts); *Poyser v. Flora*, 780 N.E.2d 1191(Ind. Ct. App. 2003) (similar); *Michelson v. Voison*, 254 Mich. App. 691, 658 N.W.2d 188 (2003) (similar); *Accelerated Benefits Corp. v. Peaslee*, 818 N.E.2d 73 (Ind. Ct. App. 2004) (viatical settlement is a security under Indiana law following *Howey*)); *see also* NASAA Guidelines Regarding Viatical Investments.

B. Life Settlements are Investment Contracts Under *Pratt v. Kross*, 76 Or. 483, 555 P.2d 765 (1976).

The trial court committed an error that stands outside well established precedent in Oregon when it ruled that the Investment Program that Plaintiff-Appellant entered into with Defendants-Respondents was not an investment contract. The trial court further erred by ruling that the life settlement plans purchased by Malouf were also not securities notwithstanding the terms of the Investment Program.

ORS 59.015(19)(a) explicitly defines the term "security" to include an "investment contract." ORS 59.015(19)(a). In *Pratt v. Kross*, 276 Or. 483, 555 P.2d 765 (1976), the Oregon Supreme Court adopted a less restrictive version of

the *Howey* investment contract test. The *Pratt* test holds that an investment contract is "(1) an investment of money (or money's worth), (2) in a common enterprise, (3) with the expectations of a profit, (4) to be made through the management and control of others." *Id.* at 497. The *Pratt* test differs significantly from the *Howey* test by removing the requirement that the profits be made *solely* through the management of others. *Id*. This deviation underscores the importance that the securities laws must be read expansively in order to accomplish the important investor protection goals undergirding the statute.

The first and third elements were clearly present, and therefore uncontested by the parties. Conversely, the defendants contested both the existence of a common enterprise and the fact that the profits sought were to be made through the management and control of others.

In the trial court's ruling on competing motions for summary judgment, the court found that the investment plan and life settlements were not securities only because they did not satisfy the fourth element due to each investment being "made through the management and control of plaintiff AmeriVest's own Malouf." Order Regarding Summ. J. Mot. Sept. 24, 2009 (App. ER 22). The trial court did not rule on any other elements of the *Pratt* test.

1. The investment program was a common enterprise because there is vertical commonality between Amerivest and Charles Financial and Malouf because they were to share in the investment program profits.

Under Oregon law, the common enterprise prong of the *Pratt* test is met by either vertical or horizontal commonality. *Computer Concepts, Inc. v. Brandt*, 310 Or. 706, 715, 801 P.2d 800 (1990) ("a plaintiff may prevail by showing vertical commonality, as an alternative to showing horizontal commonality"). In *Computer Concepts*, the Oregon Supreme Court recognized that courts have held investors to various levels of proof of commonality, requiring investors to show 1) "only dependence on promoter expertise"; 2) "that the investment is interwoven with and dependent on the fortunes of others, so that the investor and the promoter can be said to conduct a common venture"; or 3) "that the fortunes of the investor and the promoter be intertwined as to both profit *and* loss." *Id.* (Emphasis in original). The Court endorsed the third and most restrictive test, but expressly declined to rule on the other two less-restrictive tests. *Id.* at 715 n.9. That distinction is inconsequential in the instant case because vertical commonality is clearly present even under the third, most-restrictive vertical commonality test.

There is strict vertical commonality among the parties because Malouf and Charles Financial's prospects for profit or loss were completely intertwined with those of Amerivest. If the Investment Program was not successful, Malouf and Charles Financial would have lost the labor, expertise, efforts, and time invested in the venture, while Amerivest would have been out some, or all of the $10,000,000.00 it invested. Had the Investment Program gone according to plan, Amerivest and Malouf and Charles Financial would have realized profits according to the Cooperation and Profit Allocation Agreement between Amerivest

and Malouf ("C&PA Agreement") (App. ER 1). Moreover, according to the terms of the C&PA Agreement, there is no scenario wherein either party could profit or lose without the other party facing the same fate. Therefore, the Investment Program was a common enterprise because there was vertical commonality due to the fortunes of the Amerivest and Malouf and Charles Financial being intertwined as to both profit and loss.

2. The fourth element is satisfied because Amerivest expected profits to be generated through the management of Malouf and Charles Financial who were outsiders to Amerivest in all relevant aspects.

The trial court erred in ruling on competing motions for summary judgment by finding that the Investment Plan was not a security because "each investment was made through the management and control of plaintiff AmeriVest's own Malouf." App. ER 22. (Emphasis added.) The trial court erred because Malouf and Charles Financial had exclusive control over the management of the program. Oregon securities law considers the economic realities of an arrangement, not its form. *Jost v. Locke*, 65 Or. App. 704, 714, 673 P.2d 543 (1983) (recognizing the flexible enunciation of the modified *Howey* test established in *Pratt v. Kross*, 276 Or. 483, 497 (1976)). Therefore, consistent with Oregon precedent, Malouf's superficial designations as a limited director and officer of Amerivest are inconsequential. Only his control over the management of the program is at issue and is clearly established by the C&PA Agreement. Therefore, the fourth element of the *Pratt* test is satisfied.

i. Under Oregon law, Malouf's superficial designation as an officer and director is inconsequential as Oregon securities law values substance over form.

The fourth prong of the *Pratt* investment contract test is satisfied when profits are expected to be generated through the managerial and significant efforts of another that affect the success or failure of the enterprise. *Jost*, 65 Or. App. at 714. The *Pratt* test is less restrictive than *Howey* because the expectation of profit does not have to be "solely" derived from the effort of others. *Pratt*, 276 Or. at 497; *accord Black v. Corp. Div.* 54 Or. App. 432, 441 (1981). Under *Pratt*, it is permissible for profits to be derived, in part, from the investor's non-managerial acts. *Id.*

Moreover, the Oregon Supreme Court has consistently held that "[i]n searching for the meaning and scope of the word 'security' in the Act, form should be disregarded for substance and the emphasis should be on the economic reality." *Jost*, 65 Or. App. at 716. Accordingly, the Oregon Supreme Court has looked beyond the superficial flaws in the form of the arrangement to find a security where the economic reality dictates. *See Black v. Corp. Div*., 54 Or. App. 432, 442 634 P.2d 1383 (1981) ("We must apply the *Howey* test in light of 'the substance [of] the economic realities of the transaction rather than the names that may have been employed by the parties."). Applying this reasoning, the *Pratt* court held that the non-supervisory, non-managerial efforts of a limited partner did not preclude finding that the limited partnership interest was an investment contract. *Pratt*, 276 Or. at 497.

ii. Malouf had exclusive control over the management of the investment program.

In the instant case, Charles Financial and its agent Malouf exclusively controlled the Investment Program. The C&PA Agreement granted Malouf only limited rights as a director and officer, but granted him exclusive rights to conduct transactions consistent with his role as the "Provider" under the agreement. Conversely, Amerivest retained exclusive control of its operations outside the C&PA Agreement, but had no legal right to manage any of the transactions at issue, as it was simply the "Client." Malouf and Charles Financial also exercised exclusive control in practice. All transactions were effected at the direction of Malouf and there is no evidence that Amerivest was ever anything more than a passive investor.

CONCLUSION

For the reasons discussed above, NASAA respectfully requests that the Court reverse the trial court's finding that life settlements are not securities.

Respectfully submitted,

By_____
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Attorney for Amicus Curiae

ATTACHMENT

Index of Attachment

CERTIFICATE OF FILING AND SERVICE

I hereby certify that I filed the foregoing opening brief on January 25, 2011, by causing the original and 13 copies thereof to be mailed by first-class mail on that date to the Appellate Court Administrator for the state of Oregon, and that I served that same on January 25, 2011, by causing two true copies thereof to be mailed by first class mail on that date to the following:

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