SEC charges pair of brokers, investment advisory firm, others with $80M variable annuity scam

$4.5M paid in total to settle charges in 'calculated fraud exploiting terminally ill patients'

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Bloomberg News, iStock; photo composite by Gerardo Tabones

The **Securities and Exchange Commission** Thursday filed charges against a group of brokers in a scheme wherein wealthy investors used variable annuities with death benefits to wager on the lives of the terminally ill.

The complaint targeted brokers Michael A. Horowitz of Los Angeles and Moshe Marc Cohen of Brooklyn, N.Y., slapping both with a cease-and-desist order and allegations of fraud.

The plan — which involved the sale of more than $80 million in variable annuities — ran its course from July 2007 to February 2008. Mr. Horowitz was allegedly the “architect” of a scheme to profit from the death of terminally ill hospice and nursing home patients, according to the SEC's complaint.

Mr. Horowitz allegedly obtained the personal health and identification data of the dying patients through fraud, marking them as annuitants on variable annuity contracts that he had marketed to wealthy clients, according to the SEC's complaint. He allegedly recruited Mr. Cohen to help facilitate the sale of these “stranger-owned annuities.” Under false pretenses, both men allegedly received their broker-dealers' approval to sell the annuities. The brokers reaped a windfall in commissions from their sale, the SEC claimed, with Mr. Horowitz obtaining more than $300,000 and Mr. Cohen snagging more than $700,000.

“This was a calculated fraud exploiting terminally ill patients,” Julie M. Riewe, co-chief of the SEC's Enforcement Division's Asset Management Unit, said in a news release.

At the heart of the matter is the fact that variable annuities don't require proof of insurable interest or a physical examination of the annuitant — the person whose demise would trigger the payout of the annuity's death benefits.

Mr. Horowitz allegedly told the contract owners — the wealthy investors funding the variable annuities — to invest aggressively to help drive up the value of the account, according to the complaint. His alleged argument was that there was no way to lose: If the value of the annuity contract climbed, the client would receive it as the death benefit payout following the demise of the terminally ill annuitant. If the value fell, then clients received a death benefit that guaranteed a payout equal to the premiums paid minus any withdrawals, according to the SEC's complaint.

At least 16 terminally ill people were designated the annuitants in some 50 variable annuity contracts that were allegedly sold by Mr. Horowitz, Mr. Cohen or other associates, according to the SEC. All of the patients lived in southern California or Chicago.

The SEC also singled out three individuals for their role in allegedly identifying sickly patients to be annuitants: Harold Ten of Los Angeles, Menachem “Mark” Berger of Chicago and Debra Flowers of Chicago.

In order to obtain identification information, Mr. Ten allegedly started up a business that purported to provide charitable aid to people in hospice care, according to the complaint. Mr. Berger, meanwhile, is the executive director of a firm that owns and operates nursing homes in Chicago and the owner of a firm that supposedly provided financial aid to the terminally ill. Ms. Flowers, meanwhile, had worked for Mr. Berger as an admissions and marketing director for the nursing homes he oversaw, according to the SEC.

In fall 2007, Mr. Horowitz allegedly sought to expand his variable annuities scheme beyond retail clients and tap institutional investors. He allegedly met with the principals of two affiliated hedge funds in New York, which led to the establishment of an affiliate called BDL Group, advised by BDL Manager, according to the suit.

The principals of the hedge fund allegedly retained commodities trader Howard A. Feder of Woodmere, N.Y. to operate BDL Group and BDL Manager, according to the SEC. The supposed investment strategy here was to obtain guaranteed short-term gains by exploiting the annuity contract's bonus credit and enhanced death benefit provisions, seeking terminally ill people to be annuitants, aggressively invest the premiums and then roll the death benefits into new stranger-owned annuity deals, according to the complaint.

Finally, the SEC filed a complaint against former registered representatives Richard Mark Horowitz and Marc Steven Firestone, both of Los Angeles, for negligently permitting point-of-sale forms for a dozen annuities in this scheme to be submitted to their broker-dealer, NFP Securities Inc.

The sales took place between mid-November and mid-December 2007, according to the SEC. Mr. Firestone allegedly signed off on the variable annuities — supposedly with the knowledge of Richard

Horowitz, his supervisor — and submitted them to NFP with incorrect information on the investors' time horizons, the SEC alleged.

NFP is not a named defendant in the SEC's case. Emily Deissler, a spokeswoman for NFP, said the firm declined to comment.

Though the litigation with Mr. Horowitz and Mr. Cohen is still continuing, the SEC also obtained some $4.5 million in settlements from other parties in the elaborate grift.

Mr. Ten agreed to pay a disgorgement of $181,147, plus prejudgment interest of $20,858 and a penalty of $90,000. Mr. Berger agreed to pay $119,000 in disgorgement, plus $11,579 in prejudgment interest and a penalty of $100,000.

Ms. Flowers, meanwhile, submitted a sworn statement of financial condition last May and a sworn declaration in October 2013, asserting her inability to pay the penalties and disgorgement.

Mr. Feder will pay a penalty of $130,000. BDL Manager will pay a disgorgement of $1.5 million, prejudgment interest of $196,608 and a penalty of $1.5 million.

Finally, Mr. Horowitz will pay a disgorgement of $292,767, plus prejudgment interest of $36,512 and a penalty of $40,800. Mr. Firestone will pay $127,853 in disgorgement, prejudgment interest of $17,140 and a penalty of $40,800.

Attorney Eliot Lauer of Curtis Mallet-Prevost Colt & Mosle is representing Mr. Feder and BDL Manager. He had no comment on the SEC's case. Attorneys for the other defendants did not immediately return calls.

As elaborate as this latest “stranger-owned annuities” caper is, it's hardly the first such scheme. Cranston, R.I.-based estate planning attorney Joseph Caramadre captured the attention of regulators, compliance professionals and the media more than four years ago when he was the subject of civil suits filed by life insurers for allegedly soliciting terminally ill people to be annuitants on variable annuity contracts with death benefits.

Litigation flew: The issuing insurers **sued the broker-dealers** and registered reps who allegedly sold the annuities. In turn, the broker-dealers **countersued the life insurers**.

Federal authorities filed conspiracy and wire fraud charges against Mr. Caramadre in relation to the scheme. He was sentenced to six years in prison last December.