United Policyholders
Empowering the Insured

When Life Insurance Is Suddenly Canceled

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Earlier this year, an elderly man went to the hospital for stomach pains. The doctors advised him that he had gallstones. Days after the emergency room visit, the man and his wife purchased some life insurance. Only later did they learn that the "gallstones" were cancer. Now the insurer is refusing to pay.
"He died pretty quickly," says Michael Young, a Sherman, Texas, attorney representing the widow, who declined to provide more information about them or their case because it may go to litigation. "Insurance companies have gotten creative."
Tucked into the fine print of all life insurance policies is what's known as the "Contestable Period," which usually gives the insurance company within two years of the insured's death to cancel payment of a life insurance claim — they are not obligated to pay if a material misrepresentation is found in the application. Often the insurance company will argue that the deceased purposely hid information about a preexisting condition such as cancer. Also, if there's a question about whether the deceased committed suicide, the policy's beneficiaries may not get paid.
For instance, when actor Heath Ledger suddenly died in 2008 of an accidental prescription drug overdose, his life insurance company, ReliaStar Life Insurance Co., initially balked at honoring his policy because it was concerned that the star of Brokeback Mountain may have committed suicide. Ledger's family sued and a year later reached a settlement with ReliaStar.
What the Texas widow and the Ledger family went through is still the exception rather than the rule. Last year, life insurers paid out $59 billion to life insurance beneficiaries, according to the American Council of Life Insurers ACLI). Less than 2% of claims are contested, says Steven Brostroff, an ACLI spokesman. But according to a recent Los Angeles Times story, this trend of canceled life insurance is growing.
"The amount of money life insurers withheld from beneficiaries has more than doubled over the last decade, to $372 million last year, even as policy sales went down, according to a Times' analysis of data compiled by the National Assn. of Insurance Commissioners," the newspaper says.
LA Times staff writer Lisa Girion tells WalletPop that she derived the information in reports filed to state regulators. The ACLI is "not convinced" that Girion's numbers are accurate, Brostroff says, adding he isn't aware of any peer-reviewed statistical analyses backing this point.

Dennis J. Wall, a Florida attorney specializing in insurance matters, isn't so sure either. "This is an area where we don't have a lot of hard evidence," he says. "It's anecdotal."

Nonetheless, it's pretty compelling.

Rescissions are so well known in the health insurance field that tighter restrictions on the cancelations were included in the health care reform law. A few years ago, Amy Bach, executive director of the consumer group United Policyholders, says she noticed the practice was spreading to the traditionally stodgy life insurance business.

"The issue of rescission is just a fact of life in the modern day insurance industry," she says. "Now that virus of bad ethics is spreading to the life insurance products."