



Life Insurance Settlement Series Edition No. IX

Overview of the Life Insurance Secondary Market from an Investment Perspective

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Abstract

What's happening? Is the Life Insurance Secondary Market ("LISM") booming, or is it on the decline? Has the LISM matured? Are investors investing in life insurance policies, or is investor interest stagnant? The media, investors and industry stakeholders are asking these questions for several reasons: 1) the recent economic recession has seen capital exit many markets including the LISM; 2) life insurance settlement regulations have now been established in most states; 3) prices paid for life insurance policies have decreased from levels paid prior to the recession; and 4) court cases continue to question various life insurance policy ownership rights.

While answers to these questions remain unclear, recent developments suggest that while the LISM is down in volume, it remains vibrant. The LISM is maturing and gaining strength with fewer numbers; and investor capital is finding new opportunities within the LISM.

This paper highlights salient excerpts from media articles published over the past twelve months in an attempt to identify trends affecting the LISM. Over 65 articles have been researched and summarized into several categories:

- I. General Developments in the Life Insurance Secondary Market
- II. The Landscape of the Financial Markets
- III. Investments and Available Capital in the LISM
- IV. Securitization of Life Insurance Settlements
- V. Best Practices and Standards
- VI. Conclusion

I General Developments in the Life Insurance Secondary Market

IRR's have increased to 15-20% while transaction volume has decreased by 40-50% from 2008. New niche services are being offered. New "stress tests" reveal that insurers are strong enough to withstand periods of severe financial stress. The new U.S. Financial Reform Law will bring more oversight to insurance practices that should benefit the LISM. However, the LISM continues to suffer from unfair practices of insurers and lack of knowledge/awareness among agents and consumers.

Questions Remain, but Potential is Strong

Ironically, there were plenty of investors when IRRs were at 9% to 10%, but now with 15% to 20% percent IRRs there are fewer investors. Why? It may be because mortality tables increased by as much as 30 percent in 2008. But more likely, it is because capital markets are still uncertain of economic trends and government actions.

The U.S. General Accountability Office 2010 survey of life insurance settlement providers reports a 40-50% decrease in settlements from 2008 to 2009. Even though life insurance settlements are subject to the same laws of supply and demand as any other investment, and investments in the LISM are down, the industry is not gone ... quite the opposite.¹

The LISM endures because the essential dilemma -- what to do with an outdated or unwanted policy -- hasn't gone away. Conning estimates the average U.S. Gross Market Potential where the insured is impaired by only a single health criterion, will range between \$105 billion and \$209 billion in face value for 2009 through 2017, or an average Gross Market Potential face value of \$177 billion. However, should the market focus on policies where the insured suffers from two health criteria, Conning estimates the range to be between \$67 and \$134 billion in face value with an average Gross Market Potential face value of \$114 billion.² Adding to life insurance settlement potential in the next few years is evidence that the sale of life insurance to seniors in September, 2010 is up 8.7% over September 2009.³ Reports from brokers indicate that supply of policies continues to be large and can be easily turned up. Further, Conning reports that the life insurance settlement market has begun to stabilize following the economic downturn and capital has started to return into the space. Outlook remains strong as concerns over regulation and insurer interference begin to ease, which will lead to increased capital from the primary and tertiary markets.⁴

The global financial crisis was a wake-up call for many investors who discovered that hedge funds, stock markets and bonds failed to provide adequate diversification. With the asset class set for renewed growth, firms such as Mercer (Melbourne, Australia) expect to see more interest from sophisticated investors in their region.

But important issues remain unresolved:

- Should life insurance settlements be treated as securities?
- Should the federal government replace state regulations?
- Should insurers be allowed to change terms of policies after they are sold to investors?
- Should insurers be allowed to discriminate against seniors seeking to sell policies?
- Should insurers be allowed to intimidate and threaten agents with their jobs to discourage life insurance settlements?
- Should insurers be allowed to engage in manipulative paperwork beyond existing laws and regulations to intimidate sellers?



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- Should a senior be allowed to purchase a policy with the intent to sell it for profit?
- Should insurers be required to notify policyholders of the secondary market when considering lapsing or surrendering?

These issues need to be addressed and resolved promptly as they are frustrating and impeding investors.

The GAO Validates Life Insurance Settlement Vitality, but Insurers Continue to Distort the Facts

In contrast to the insurance industry's best efforts to add confusion to the life insurance settlement discussion, the General Accountability Office 2010 survey revealed that the LISM has provided substantial value to seniors who were fortunate enough to discover and understand the benefits of the life insurance settlement option. The survey demonstrates that the LISM is maturing as life insurance settlement laws, STOLI laws and regulations take hold. But the survey also shows that the financial market meltdown has had a daunting impact on the LISM, which is unfortunate for the many seniors who now seek maximum value from their life insurance to help replace depleted retirement funds.⁵

Of 98 provider firms, 25 firms reported closing 4,505 transactions in 2008 and 2,636 in 2009. This represents \$12.9 billion face in 2008 and \$7 billion in 2009. The full market is something greater than these numbers. Other data through July suggests 2010 continues to operate at about the 2009 level.⁶

Consumer surveys reveal that 80% of seniors have at one point in their lives purchased life insurance, but 40% report that they have terminated a policy, claiming they no longer needed the coverage. Regrettably, more than half do not know they can sell their policies because they have not been adequately educated and conflicting messages have led to skepticism.⁷

Unfortunately, life insurers have employed many questionable methods to thwart the growth of the LISM, even going so far as to threaten to fire agents for participating in a life insurance settlement, which is in direct conflict with agent fiduciary duties and a violation of some state laws. Media articles are inconsistent and often use sensationalism to negatively portray the life insurance secondary market.⁸

The LISM is gearing up to "fight back," such as Coventry suing AXA for refusal to provide illustrations and policy status reports. The complaints posit an insurance industry-wide conspiracy to tamp out the secondary market for life insurance policies and alleges that "AXA Equitable makes a practice of undermining life insurance settlement transactions involving policies it has issued. It does so in various ways that, taken individually or in combination, are designed to frustrate a given life insurance settlement indefinitely and to preclude its competitors in the life insurance settlement market from exercising their property rights as owners of the policies in question."⁹

In their attempts to paint all life insurance settlements as illegitimate, the life insurance industry seems to be facing an uphill battle. In another blow to life insurers, a California federal judge granted summary judgment upholding the enforceability

of nonrecourse premium financing, rejecting Lincoln National's efforts to rescind such policies on grounds of insurable interest. Further, a federal judge in Minnesota applied the two year contestability period to a stranger-originated life insurance lawsuit filed by PHL Variable Insurance Co. by dismissing the claim for being filed one day after the two year period.¹⁰ But STOLI is gone as evidenced by:¹¹

- Insurable interest of a policy applicant is a requirement in every state.
- 40 states have life insurance settlement laws.
- 25 states have specific STOLI definitions.
- The LISM avoids STOLI, even though insurers and their agents issued such policies with vigor several years ago.

New Products Emerge to Assist Investment in Life Insurance Settlements

The life insurance settlement market is poised for growth as investors look for alternatives to diversify their risk exposure. With increased capital ready for deployment, innovative products are being developed, with many more yet to come. However, investors are going to require greater accuracy from the medical underwriters and greater assurance of the life insurance industry's solvency. Further, the new financial regulations will impact how securitizations are structured.

Life expectancy underwriting will continue to evolve with ongoing research, accumulation of data, medical advances, new technologies, and efforts to establish "best practices." New firms and academic developments currently in process may bring enhancements.

The next update to the VBT mortality tables is expected in 2012, but barring a major medical breakthrough, LE underwriters are not expecting large changes as were experienced in 2008. There will be fine tuning by impairment, but no wholesale changes. Further, today's yields of 15-20% include contingencies for longevity risks.

Below are a few examples of innovative products that are making it easier for investors to enter this space:

- Stone Cross Capital says it can help investors comply with Shariah when buying longevity-linked assets. This is a niche that represents progress in opening the LISM to all investment markets.¹²
- Veris Settlement Partners and Life insurance settlement Leads are offering a black box "system" to help assess life expectancy of an insured when considering a life insurance settlement.¹³ There are a number of these systems now available online, as reported in the Life Expectancy paper published by Insurance Studies Institute (ISI) in July of this year.
- Risk Capital Partners announced that it structured longevity extension coverage in cooperation with a leading European carrier. There are several other entities offering similar longevity risk indemnities, now bringing alternatives to such risk management.¹⁴





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Insurance Regulation and Financial Reforms Point to Stability

Moody's new "global stress test" measures the risk that operating liabilities of insurance companies may cost more than expected, and that unexpected losses on debt securities may hurt investment yields, leading to a liquidity stress that can force an insurer to sell "hold-to-maturity" investments at a loss. But the news is good. Based on this test, most of the world's life insurers have enough cash, or access to cash, to cope with periods of severe financial stress.¹⁵

Despite the apparent financial strength of the insurers, the 2010 Financial Reform Law continues state-based regulation of insurance carriers, but the law also creates a Federal Insurance Office to monitor the insurance industry and to recommend specific insurance companies and regulations that should be treated as systemically important. The Office will examine inconsistencies and lack of clarity in state insurance and life insurance settlement laws and regulations. It will also analyze costs and benefits of potential federal regulation, and the ability of a federal regulator to provide policyholder protections.

The new law requires issuers of securities backed by an asset (subject to certain exemptions) to retain not less than 5% of the "credit risk," most likely including future securitizations of life insurance settlements. The law also forces most over-the-counter derivatives onto exchanges and clearing houses, resulting in increased collateral requirements. Except for hedging a bank's own exposures, U.S. banks may not enter into longevity swaps or synthetic trades in life insurance settlements.

The new law creates an "Office of Financial Protection for Older Americans," which is supposed to identify unfair or deceptive certifications of financial advisors. This office is granted very broad authority to regulate products and services that are senior-related, including those that involve financial advisors, insurance products and life insurance settlements. Jack Kelly of the McPherson Group notes: "This Office has the potential to play a significant role in the future of the life insurance settlement industry and could serve as a forum for the development of standards of conduct for the primary life insurance settlement market."

The Financial Reform Law could increase the popularity of family offices. The law requires hedge fund advisors, who manage more than \$150 million in assets, to register with the SEC. But it allows family offices that manage the affairs of wealthy families, and the advisors of those offices, to do business without registering with the SEC.

II The Landscape of the Financial Markets

A Turbulent Time for Many Investors

American companies have more than \$1.7 trillion in S&P rated bonds and loans maturing in 2011 through 2014. In 2011, about \$300 billion in debt comes due of which 41 percent is considered speculative. By 2014, the amount climbs to about \$550 billion, of which 72 percent is speculative.¹⁶ S&P believes that many borrowers at the low end of the ratings scale will encounter serious hurdles to their refinancing needs in 2013 and 2014. S&P fears that the continuing sovereign debt crisis in Europe will deter investors from buying up speculative debt.¹⁷

Will new bonds be without ratings? Must investors develop their own ratings?¹⁸ Immediately following signing of the new Financial Reform Law, Standard & Poor's, Moody's Investors Service, and Fitch Ratings refused to allow their ratings to be used in documentation for new bond sales. This is because the new law makes rating firms liable for the quality of their ratings. There were no new asset-backed bonds put on sale that week, in stark contrast to the prior week when \$3 billion of issues were sold. Several companies shelved their bond offerings "indefinitely." But the SEC moved to defuse turmoil by temporarily allowing bond sales to go ahead without credit ratings.¹⁹

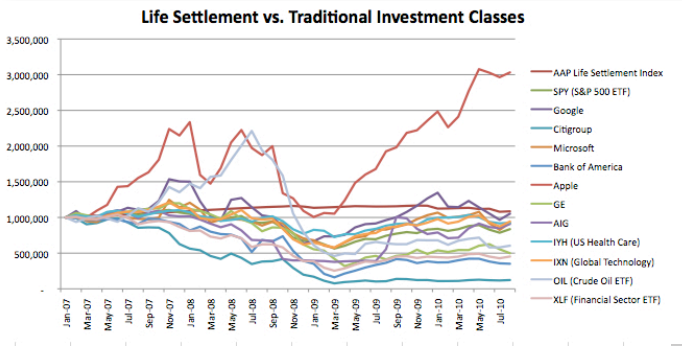
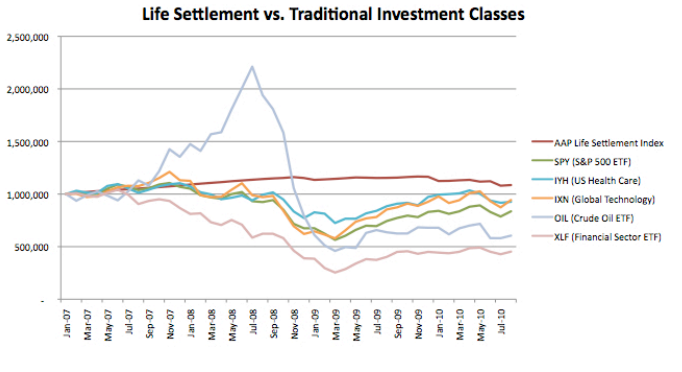
Are bonds no longer safe without credit ratings? Have investors ceased investing in bonds? Investors now have to find alternatives to credit rating agencies, e.g., using ratios and other measures of risk. Does this put investments in life insurance policies on a par with bonds, i.e., having no ratings?

In a flight to safety, mutual funds, households and banks boosted the domestic share of the \$8.2 trillion in tradable U.S. Treasuries to 50.2% as of May. Demand for Treasuries from U.S. investors is climbing as consumer spending and incomes stagnate and the savings rate reaches the highest level in almost 18 years. Is this another vulnerable bubble? Yields are going lower and are expected to stay low for another 1-2 years.²⁰



Investments in Life Insurance Settlements Outperform Traditional Market Investments

While the past three years have been turbulent for investors, investments in life insurance settlements have been relatively steady. Except for mortality table adjustments in 2008, the AAP Life Insurance Settlement Index²¹ shows that investments in life insurance policies, after including adjustments for mortality table changes, maintained steady growth from January, 2007 through April, 2010 and remained at a higher value as of April, 2010, than all other major investment indexes. The investors avoided the peaks and valleys of major market indexes in 2008 and 2009. The following charts show it all. Except for those who invested heavily in Apple, Inc. stock, life insurance settlements outperformed them all.



The Value, as of August 2010, if \$1 million was invested in January of 2007. Life Settlement returns are calculated using the AAP Life Settlement Index

Investing in Life Insurance Settlements Enters the Mainstream

As of May, 2010, defined benefit pension plans saw asset decreases of \$41 billion with concurrent liability increases of \$14 billion. Total pension funding deficit rose to \$294 billion. Defined benefit pensions needed investment gains of over 34% for the balance of 2010 to reach a 90% funded ratio—and that would still leave the deficit at \$138 billion. But the market has decreased further, adding to the problem.²²

In response to this growing problem, pension funds have been looking for alternatives to make up some of the ground lost during the current financial recession. In 2008, the Pensions Institute produced a report that concluded: “There are no particular ethical issues associated with investing in life insurance policies, provided products and processes are fully transparent and provided the privacy of the policyholder is safeguarded.” Life insurance settlements are little different than the pension industry where annuities are based on life expectancy.²³

In a show of strength for life insurance settlements, public pension funds have been making sizeable investments into this asset class, with many more expecting to come. In October of this year, the Oregon Investment Council, which oversees investments of the state pension fund, approved a proposal to commit \$100 million to Apollo Global Management to purchase a life insurance settlement portfolio. Apollo’s individual partners expect to invest about \$37 million. Apollo wants to raise a total of \$525 million.²⁴

Life insurance settlement mortality risks also compare to long-term care contracts and reverse mortgages. Anyone invested in these assets is managing the same longevity risks.

The secondary life insurance sector has attracted hundreds of millions since late 2008, with some funds consistently delivering about 10% per annum through an appalling global financial crisis that sent investor returns plummeting across many asset classes.²⁵

III Investments and Available Capital in the LISM

New capital is entering the LISM in time to enjoy high IRRs of 15% to 20%. Industry stakeholders are reaching “out-side-of-the-box” to expand business models and tap new resources, finding keen levels of interest to invest. Insurance brokers expect more clients will be looking to sell policies, confirming that supply of policies should remain strong. Concurrent with heightened interest in alternative asset classes, interest in life insurance investments among international investors continues. Stressed life insurance settlement portfolios provide valuable opportunity for well capitalized investors seeking highly attractive and probable yields.

Significant Growth Potential Exists for the Life Insurance Settlement Market

Sixty-nine percent (69%) of insurance brokers expect that more of their clients will be looking to sell their policies within five years. Seventy percent (70%) of companies feel ‘favorable’ or ‘very favorable’ about the prospect of life insurance settlements as an investment. It is estimated that the bulk of investment comes from hedge funds, often via a third party fund which specializes in Traded Life Policies, such as Managing Partners Limited’s (“MPL”) Traded Policy Fund.²⁶

The vast excess of traded life policies (“TLP”) over their purchase prices provides an arbitrage opportunity to buy at a deep discount and later use the asset as leverage for further investment. A well-managed TLP fund has the ability to offer a steady annual return of 9%. MPL’s Fund returned 66% net of all charges over six years through June, 2010, recording no negative returns in any quarter over that period.

A growing base of firms is catering to increasing demand from smaller investors who are looking for higher returns that are not directly correlated with the markets. Some of these firms include:²⁷

- GWG Life
- Life Policy Group
- Vertical Capital Holdings
- Page & Associates



Strong Offerings by Settlement Participants Demonstrate Market's Strength

Lifeline: The Lifeline Program, an Atlanta-based provider, obtained capital to purchase policies worth \$100 million in face value. The deal was signed in May with a domestic fund of funds. Lifeline is cutting out brokers by going direct to consumers through a media campaign.²⁸

Abacus Settlements: Abacus Settlements, a New York-based provider, announced it has new capital in Europe to purchase policies, in excess of \$130 million.²⁹

Life insurance settlement Solutions: Life insurance settlement Solutions, a San Diego-based provider, announced that it has new agreements with two funders and is looking at offering new products.³⁰

Life Partners: For the quarter ended August 31, 2010, Life Partners expects to report \$30.3 million in revenues, a 4.1% increase over the same period last year. For the six months ended August 31, 2010, the company expects to report revenues of \$57.0 million, a 0.8% increase over the same period last year.³¹

Coventry: Coventry continues its innovative leadership by forming a boutique investment bank to handle mortality and longevity related transactions. The bank provides investment opportunities for institutional investors who want life insurance policies, policy-linked notes, life-linked notes and other customized structures. The opening of the investment bank is only one of numerous ventures by Coventry to diversify its business. Others include a broker-dealer and overseas businesses.³²

New Capital Enters the Life Insurance Settlement Space

Apollo Global Management: Apollo Global Management LLC is bidding on life insurance policies with a combined face value of \$6 billion held by Belgian bank KBC Group NV. Apollo joins rival buyout firms in seeking to expand beyond traditional buyouts as private-equity deal making is down about 80 percent from its peak in the second quarter of 2007.³³ This action pursues the stressed life insurance settlement portfolios that have insufficient funding to maintain premiums. Such portfolios provide valuable opportunity to well-capitalized investors seeking highly attractive and probable yields.

Oregon Public Investment Group: As noted above, the Oregon Investment Council, which oversees investments of the state pension fund, approved a proposal last week to commit \$100 million to Apollo Global Management to purchase a distressed portfolio.³⁴

SL Investment's LifePlus Series 2: Fund managers are moving back into the scandal-hit UK life insurance settlement market by offering a new generation of products said to "reduce or even eliminate" investor risk. This week saw the launch of SL Investment's LifePlus Series 2 – the first life insurance settlement fund fully compliant with a new industry code of practice aimed at raising standards and improving transparency for those investing in the alternative asset class. It comes less than a week after 19,000 UK investors who invested in so called "death bonds" through Keydata learned that they could be eligible for compensation after Lifemark, the Luxembourg-based issuer, went into administration.³⁵

Coventry: Coventry has also partnered with SL Investment Management, a UK Investment Manager. Meetings have been held in Asia, Australia and New Zealand. According to Jeremy Brettell, CEO of SL Investment Management, the interest they are getting is substantial.³⁶



New Life Insurance Settlement Funds Emerge: Buttonwood Life insurance settlement Fund is a newly-organized Delaware trust registered under the Investment Company Act of 1940, as a non-diversified, closed-end management investment company. Its investment objective is to seek capital appreciation primarily in life insurance policies while providing a small to moderate level of current income. The Fund is initially offering up to 10,000,000 shares at an opening net asset value of \$10.00 per share, grossing \$100,000,000, plus a sales load, and thereafter will offer shares for purchase at the net asset value next determined after an order is accepted, plus a sales load. The minimum initial investment is \$5,000 for investors and \$1,000 for IRAs. The net proceeds to the Fund after sales loads and offering expenses are expected to approximate \$92,950,000. This offering remains subject to SEC approval.³⁷

Tranen Capital: Tranen Capital signed an agreement with wealth management firm iFAST Financial in Singapore to offer its Capital Alternative Investment Fund to high-net-worth investors. The life insurance settlements fund is based in the British Virgin Islands. The company expects to expand distribution in the near future to Hong Kong, Indonesia and India.³⁸

Strategic Life insurance settlement Fund: This Irish based life insurance settlement fund targets a minimum annual US \$ based return of 8-11%, net of expenses. The structure follows the AM Best Model.³⁹

Alternative Investment Capital: Alternatives are hot. Lured by hefty yields, investors are pouring billions of dollars into Master Limited Partnerships which own and operate pipelines, primarily for natural gas and oil. J.G. Wentworth says it has raised \$115 million by securitizing notes backed by fixed annuity and structured settlement contracts. U.S. companies issued risky "junk" bonds at a record clip in August, taking advantage of keen investor appetite for returns amid declining interest rates and tepid stock markets.⁴⁰

IV Securitization of Life Insurance Settlements

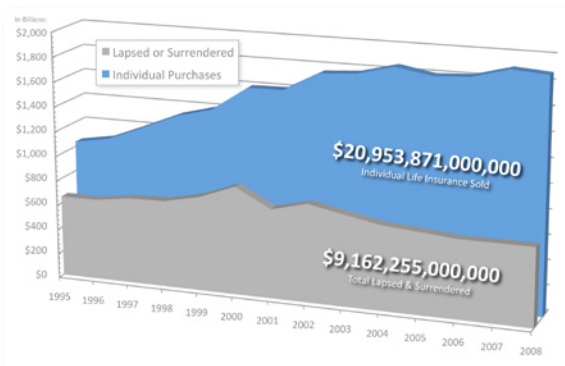
Efforts to create SEC approved securitizations of life insurance policies continue, with the goal to open investments to retail investors. This could put investments in life insurance policies on a par with mortgages, bonds, and other common asset classes. While ACLI opposes such securitizations, others see benefits for investors and for the LISM. The SEC Life insurance settlements Task Force recommends that life insurance settlements be defined as securities and that life insurance settlement brokers be brought under FINRA jurisdiction and registered with broker-dealers, but broker-dealers do not want them. A recent U.S. District Court ruling finds that an individual sale of a life insurance policy is not a security.⁴¹



Life Insurers Try New Angle to Thwart Rise of Life Insurance Secondary Market

ACLI claims that securitization of life insurance settlements exposes senior citizens and investors to increased risk of fraud, therefore securitizations should not be allowed. ACLI claims securitization will lead some settlement promoters to target senior citizens, inducing them to commit fraud in connection with STOLI transactions.⁴²

Policymakers need to realize that the true intention of ACLI and the life insurance industry is destruction of a vibrant secondary market for life insurance, which would deny seniors the option and right to realize full market value for their insurance policies. Public policymakers need to insist that policyholders have a right to the secondary market option. Market liquidity options are needed for investors.⁴³



During the period 1995 to 2008, life insurance sales to individuals totaled over \$20.9 trillion while concurrently lapsed and surrendered life insurance totaled \$9.2 trillion. That is about 45% of the total sales. Clearly, the life insurance industry is motivated to protect the revenue it earns from lapses and surrenders.

Conning Research estimates total outstanding life insurance settlement policies approximated \$38 billion in 2008. That is a mere .3% of a total \$10.2 trillion of in-force individual life insurance. A mere .3% should not represent a threat to the life insurance industry.⁴⁴

It is interesting to note that the insurance industry welcomes investments from individuals for insurance based securitizations and life insurance policies, but the same insurers say they do not want individuals to realize full market value for their policies. That appears to be a double standard.

The SEC Says Settlements Should be Regulated as Securities; but U.S. District Court Disagrees

The SEC Life insurance settlements Task Force weighed in on life insurance settlement securitization by recommending that life insurance settlements be defined as securities. The report notes inconsistent regulation among the states and suggests that investors would benefit from baseline standards of conduct.⁴⁵

Few stakeholders in the LISM disagree with the concept that investment products based in life insurance policy assets should be treated as a security. But the SEC recommendation raises several fundamental questions:

- Should the Federal SEC versus state securities departments regulate such investments?
- Should individuals selling their policies be required to conform to securities laws?
- What expertise does the SEC have to establish standards and best practices for the LISM?

However, the SEC recommendations could hurt life insurance settlement brokers by requiring them to register under FINRA registered SEC broker-dealers. Technorati contacted nearly a dozen FINRA registered broker-dealers and their response was unanimous: they do not now, and are not planning in the future to allow life insurance settlement brokers to register with them.⁴⁶

When a consumer buys a life insurance policy, the agent selling it does not need a securities license. However, when the same consumer wants to sell it, the SEC says the same agent assisting with the sale must be securities licensed. Why should the agent change hats midstream? Is the agent an insurance regulated agent or an SEC regulated agent? Some argue the difference is that the policy will be purchased for investment. But this test is not applied to other industries. For example, why not require securities licensing for real estate agents selling real estate to investors?

Consequently, a U.S. District Court judge in Illinois ruled that life insurance settlements involving a single investor are not securities. The judge relied on the Seventh Circuit court's application of a "horizontal commonality" test, which requires that multiple investors must pool their investments and receive pro rata profits.⁴⁷

V Best Practices and Standards

The LISM is developing codes of conduct and standards on several fronts, which is creating professional disciplines and will lead to higher confidence for policy sellers and investors. NCOIL is pressing for regulations that require insurers to advise policyholders of all options, including life insurance settlements, when considering a policy lapse or surrender. And, more collaboration among U.S. and European associations will lead to greater transparency, transaction consistency and better investment decisions.

The Insurance Studies Institute

ISI is a non-profit research think-tank focused on: a) researching and analyzing challenges and opportunities within the many paradigms of insurance based risk management; b) publishing research findings on industry relevant topics; c) educating industry stakeholders, public policy makers and consumers in insurance based risk management, and advancing related scholarship; and, d) promoting dialogue to foster industry advancements, fair public policy and greater risk protection for consumers.





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Major Life Expectancy Providers (LEPr) Form Focus Group: Four of the major life expectancy firms in the life insurance settlement market formed a focus group to further refine best practices to guide their profession, although one major life expectancy firm, Fasano Associates, is not participating. “The goal of the LEPr focus group is to provide a comprehensive and consistent set of best practices and performance standards to all longevity markets that may benefit from life expectancy and mortality information,” the group said in a statement. “It is also the intent that all major life expectancy providers participate and adhere to our best practices and professional standards.”⁴⁸

ELSA Releases Code of Practices: The European Life insurance settlements Association (ELSA) launched a “Code of Practice” designed to increase protection for investors in the expanding asset class of life insurance settlements. The publication of the Code follows the collapse of UK fund provider Keydata and the under-performance of two Deutsche Bank funds which highlighted the need for greater transparency and education of life insurance settlement investment risks, as well as the need for more rigorous risk mitigation. The Code responds to increasing scrutiny from regulators and media alike as the asset class spreads further into the retail markets.⁴⁹

ILMA Plans to Develop Best Practices for Providers and Servicers: ILMA is developing best practices for providers and servicing firms, and seeks to encourage “uniformity for the institutional side of the marketplace.”⁵⁰

FASB Wants Fair Value Reporting: A proposal by FASB (“Financial Accounting Standards Board”) to require “fair value accounting” method for life insurance portfolios should appeal to investors. It will create greater transparency and consistency in financial reports. It should also benefit securitizations. If approved, the new rule will become effective in 2013. However, some firms today use the fair value accounting method and as a result the current net asset value of their portfolios reflects longevity changes, cost of capital and the current price at which the market might purchase the portfolio.⁵¹

A Study Documents Differences Among Life Expectancy Underwriters: A study released by Life Policy Dynamics reveals significant differences among Life Expectancy Underwriters, as well as some similarities. Fasano consistently provided the longest LEs, and EMSI appeared to have the shortest. AVS, 21st Services and ISC exhibit almost identical changes in slope. AVS and 21st LEs are now closer than they were last year.⁵²

ISC announced a mortality table change in June. The overall average increase in LEs from 2009 to 2010, without mortality wear-off, is 2.0%. Where wear-off patterns are applied, the average increase is 3.7%. Change for smokers was minor.

Lifeline announced that they now require a separate medical examination of insured when selling large policies.

ELSA Starts Educational Unit: The European Life insurance settlement Association (ELSA) has established an education unit to give investors, the public, media and regulators information

about life insurance settlements. The goal is to help the life insurance settlement industry respond to unfavorable publicity. ELSA is also working aggressively to establish standards and best practices for the industry.⁵³

Settlement Disclosure Model Advances at NCOIL: The National Conference of Insurance Legislators (NCOIL) is drafting model state legislation that would require life insurers to tell policyholders that life insurance settlements are among the alternatives to letting policies lapse.⁵⁴

Life Expectancy Providers to Refine Best Practices, Mortality Table: Life expectancy providers are refining best practices for utilizing the new actual-to-expected mortality table. The purpose of the table is to allow investors to compare results among life expectancy underwriters. The new best practices guidelines and mortality table are expected to be circulated among other industry groups for input, including the ILMA, ELSA, LSI, and BVZL. It is hoped to be universally accepted in major international markets.⁵⁵

VI Conclusion: “So What’s Happening?”

The Life Insurance Secondary Market has slowed but is vibrant and IRRs are up. The LISM is maturing and will be expanding. New “stress tests” reveal that insurers are strong enough to withstand periods of severe financial stress, and the new U.S. Financial Reform Law will bring more oversight to insurance practices that should benefit the Life Insurance Secondary Market. But, the LISM continues to fight unfair practices of insurers and the general lack of LISM knowledge amongst agents and consumers.

New capital is entering the LISM while industry stakeholders reach “out-side-of-the-box” to expand business models and tap new resources. Insurance brokers expect more clients will be looking to sell policies, confirming that supply of policies should remain strong. Concurrent with heightened interest in alternative asset classes, interest in life insurance investments among international investors continues.

Efforts to create SEC approved securitizations of life insurance policies continue, with the goal to open investments to retail investors.

The LISM is developing codes of conduct and standards on several fronts, which will lead to higher confidence for policy sellers and investors. NCOIL is pressing for regulations that require insurers to advise policyholders of all options, including life insurance settlements, when considering a policy lapse or surrender. And, more collaboration among U.S. and European associations will lead to greater transparency, transaction consistency and better investment decisions.

Investing in life insurance policies is strengthening after the 2008/2009 recession, and this asset class needs to be within the institutional investment spectrum. It is one of the options.





Footnotes

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- 7 Surveys of Seniors Reveal Roadblocks to Reliable Life Settlement Information, The Insurance Studies Institute, August 2010
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- 9 Commercial/Contracts, Williams & Connolly Alleges Conspiracy Among Insurers and Insurance Lawyers to Squelch Secondary Market for Life Insurance Policies, The AM Law Litigation Daily, October 2010.
- 10 Judge Dismisses PHL's STOLI Claim, Deal Flow Media, October, 2010
- 11 Premium Financing Is Not Dead, Victory over Lincoln National Life, Orrick Press Release, July 2010
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- 13 Settlement Firms Team Up, National Underwriter, November 2010
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