

Life Settlements

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Movie plot and subplots

Civil War – success if other side dies

Bounty Hunting – money to turn in criminals– expected to hang 

Clint – expected death – but survives 

Eli – death expected also

Lee - Buried Treasure / Final Shootout– hope to profit from others deaths 

Similar to Life Settlement Investing

What is a Life Settlement?

Involves transfer of a life insurance policy from one party to another in return for a cash payment at transfer

Usually is irrevocable assignment

Beneficiary is the new owner

Insured has no further rights or obligations

New owner will pay premiums and receive proceeds

Assumes health of policyholder has deteriorated

Usually death in somewhat near term expected

What are Life Settlements?

Developed from prior Viatical Market

- Insured with <12 months to live (AIDS)
- Need money for Medical Expenses
- No Beneficiaries
- Pay Enhanced CV now instead of Face Amount later
- Marketplace collapsed after AIDS drug cocktails
- High Expected Returns not realized

LS – longer life expectancies

What are characteristics of an average Life Settlement?

Average age 75

Average Face Amount over \$1 million

LE of 3 to 10 years (some 0-12)

Results are like a substandard annuity or a reverse mortgage

Investor profits from earlier deaths

Life Settlements?

Great return for investors IF---

- Insured dies quickly
- High Expected Returns then realized

Not so good for insured?

- Better to keep policy – when possible?
- No law of large numbers apply
- Various opinions

Good

Older Age Patient

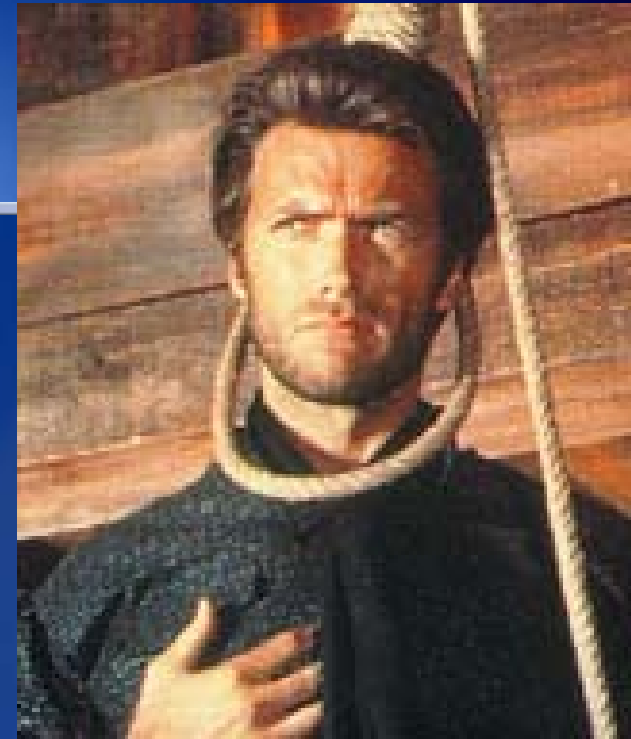
- Terminal condition
- Policy in force for many years
- Money needed for Medical Expenses
- No Beneficiaries

Obtain Higher Cash Value

Last Survivor after first death

Corporate (COLI) situations

Need proceeds for LTC needs



Bad

Recently issued policy

Smoker has non-smoker policy

Medical information inconsistent

Beneficiaries not informed

Money to be used to buy other life insurance coverage



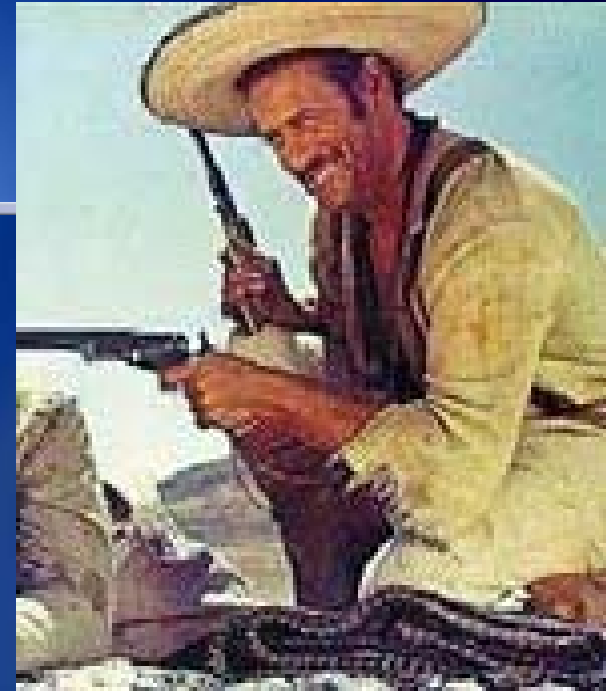
Ugly

Providing loans to purchase new policies

- Promise that they will have LS value in 2 years
- High lapses if healthy

Charitable giving schemes

Broker fee based as a % of Face Amount – not on the Economic Value



Other factors

Small restricted marketplace

High Broker charges

Reinsurance needs

GAAP Accounting concerns

Regulatory issues

Ethical issues

Life Insurance Companies' Response

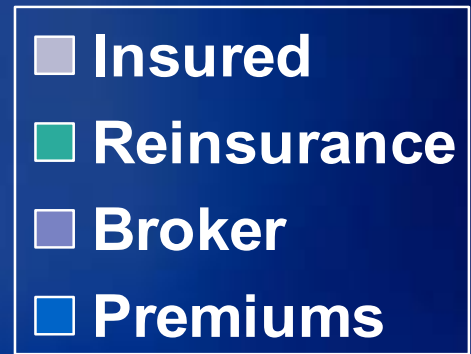
Economic Value

What is the value of a life policy?

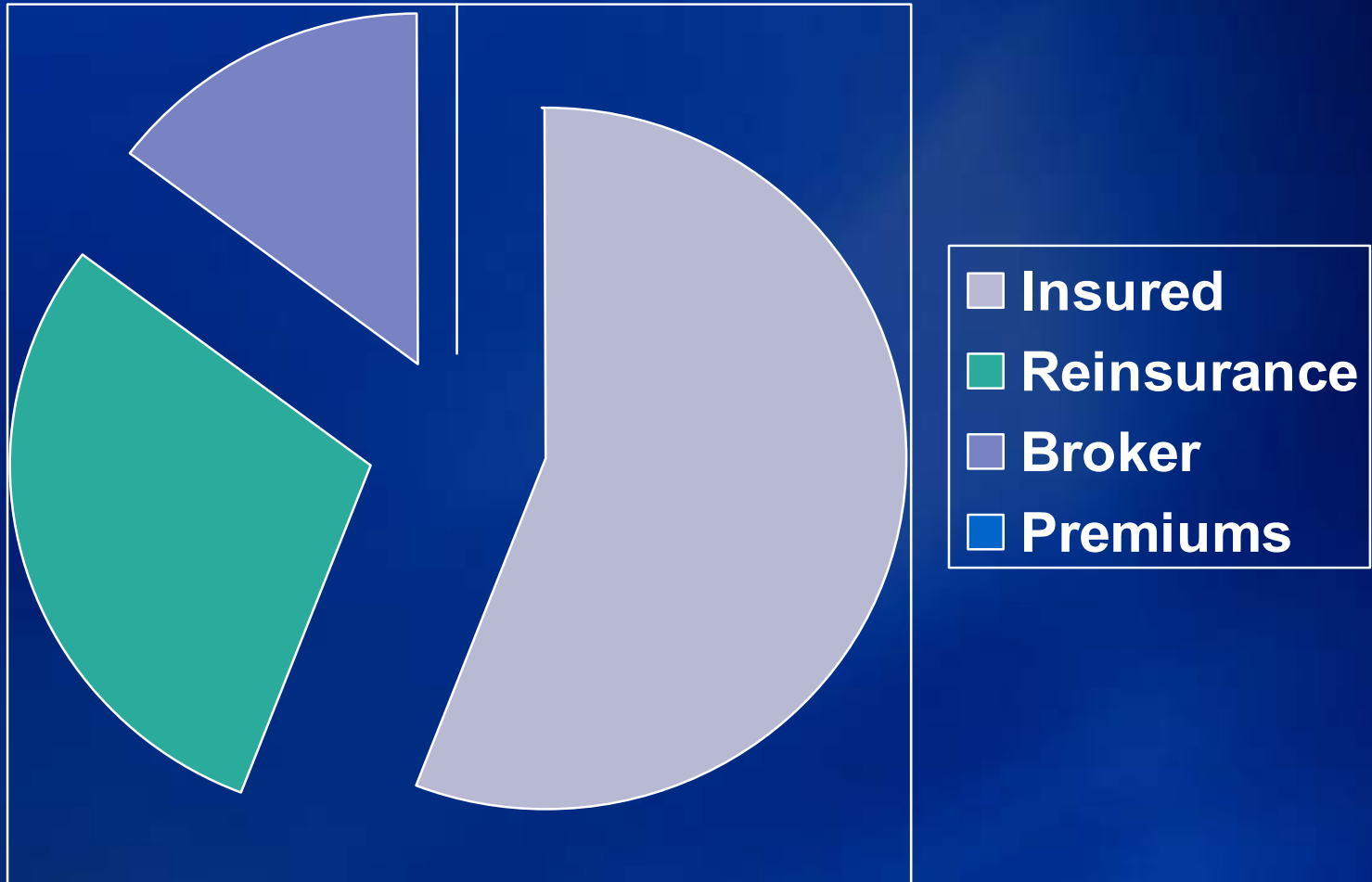
Need to understand cash flows

- Premiums
- Expenses
- Brokerage
- Reinsurance
- Other
- Death Benefit received

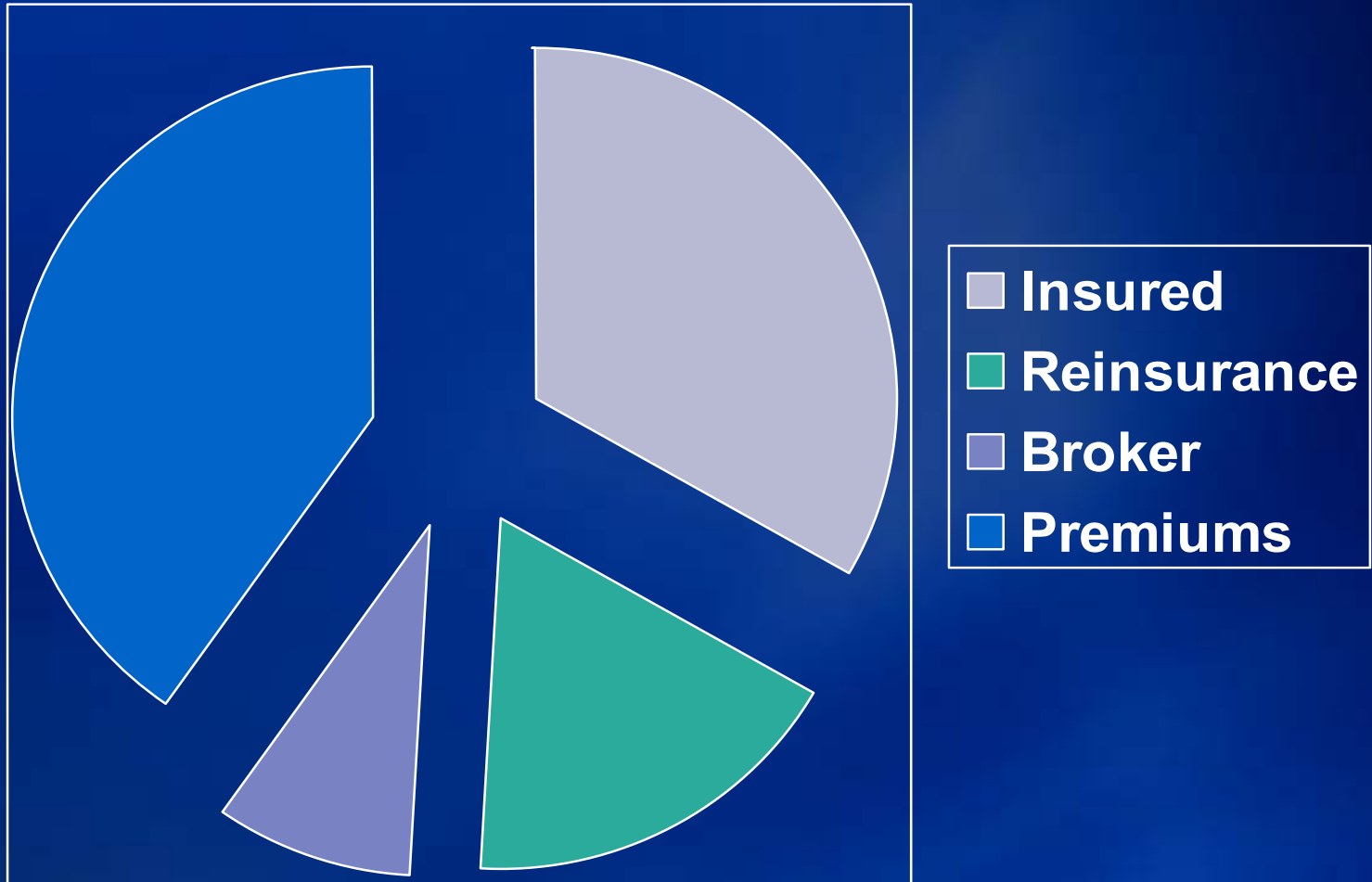
Broker Cost



Reinsurance costs – to protect against too long LE



Distribution of Funds



Life Settlement Pricing Needs

DOB, Age, Issue Date

Life Expectancy Info

- LE50 LE85

Future Cash Flow needs

- Premiums / COIs

Expenses – annual costs, fees, Brokerage

ROI needs

LE Needs

DOB, Age, Issue Date

Sex, Smoking Status

Extensive Current Medical Information

Medical Underwriting Expertise

- What u/w Manual used – current?
- How are uninsurables treated
- How is manual rating conservatism overcome

Results in LE (and rating usually)

Pricing Methods

Deterministic - All die at LE

Probabilistic – Gradual flow of deaths

Stochastic methods – multiple scenarios

Deterministic - All die at LE

Assumes all Cash Flow will be received at LE50 or LE85

Understates gains from early deaths

Overstates results from later deaths

Premium payments needed past the LE may be missed

Assumes a more certain world than actually exists

Holdover from Viatical approach

Probabilistic Method - Deaths from mortality curve

Death benefit cash flows based on mortality assumption

- What table - was 75-80, now 2001 Basic
 - Slopes very different
- Select period – when starts , how long
 - Super select in the short term?
- Accurate mortality rating
- Use of Mortality Improvements – past and future?
- Premiums usually included as a negative cash flow

Stochastic Methods – from multiple scenarios

Projections produce mean results

Also give deviations of results

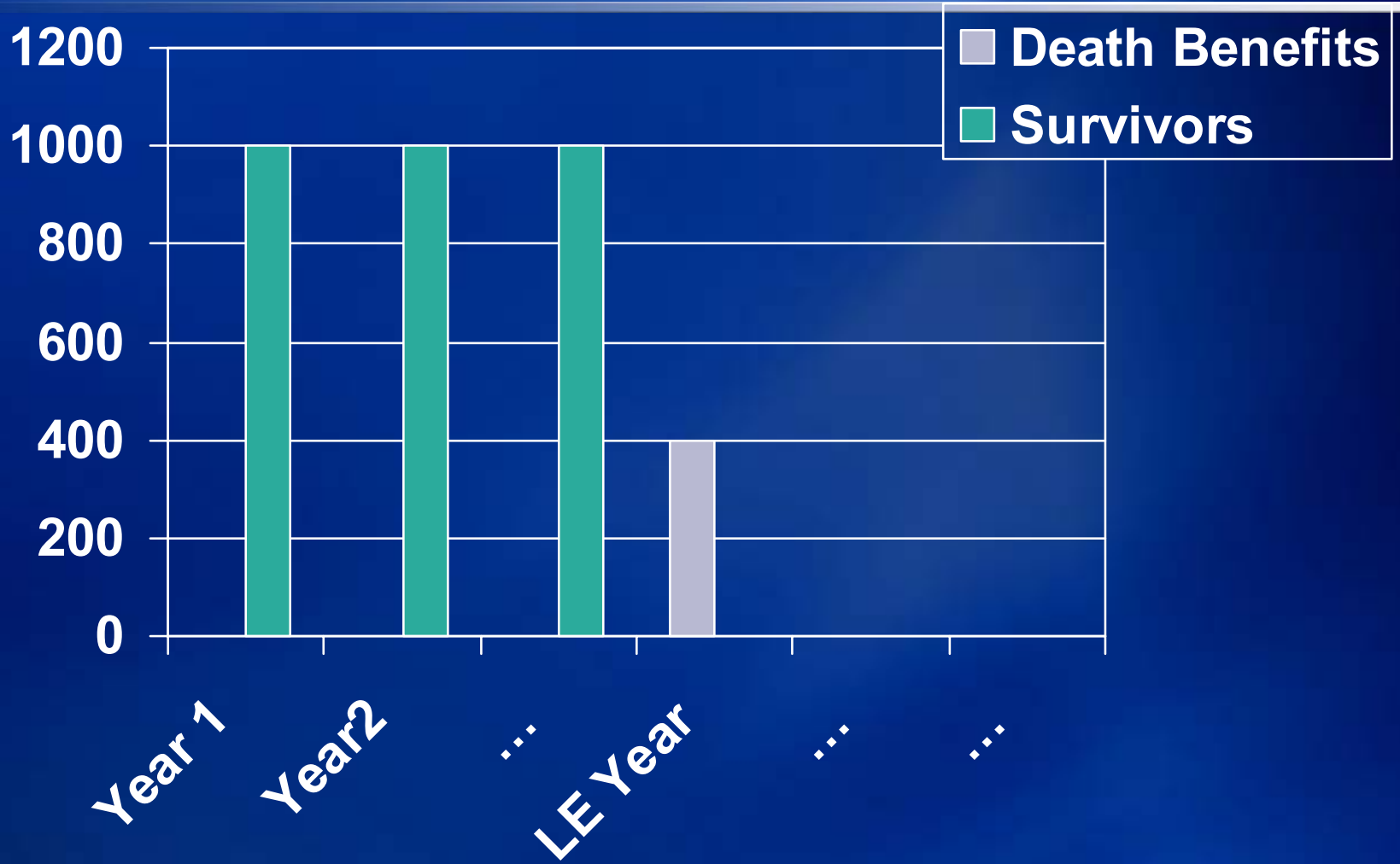
Larger deviations = more risk

More deviations/risk with:

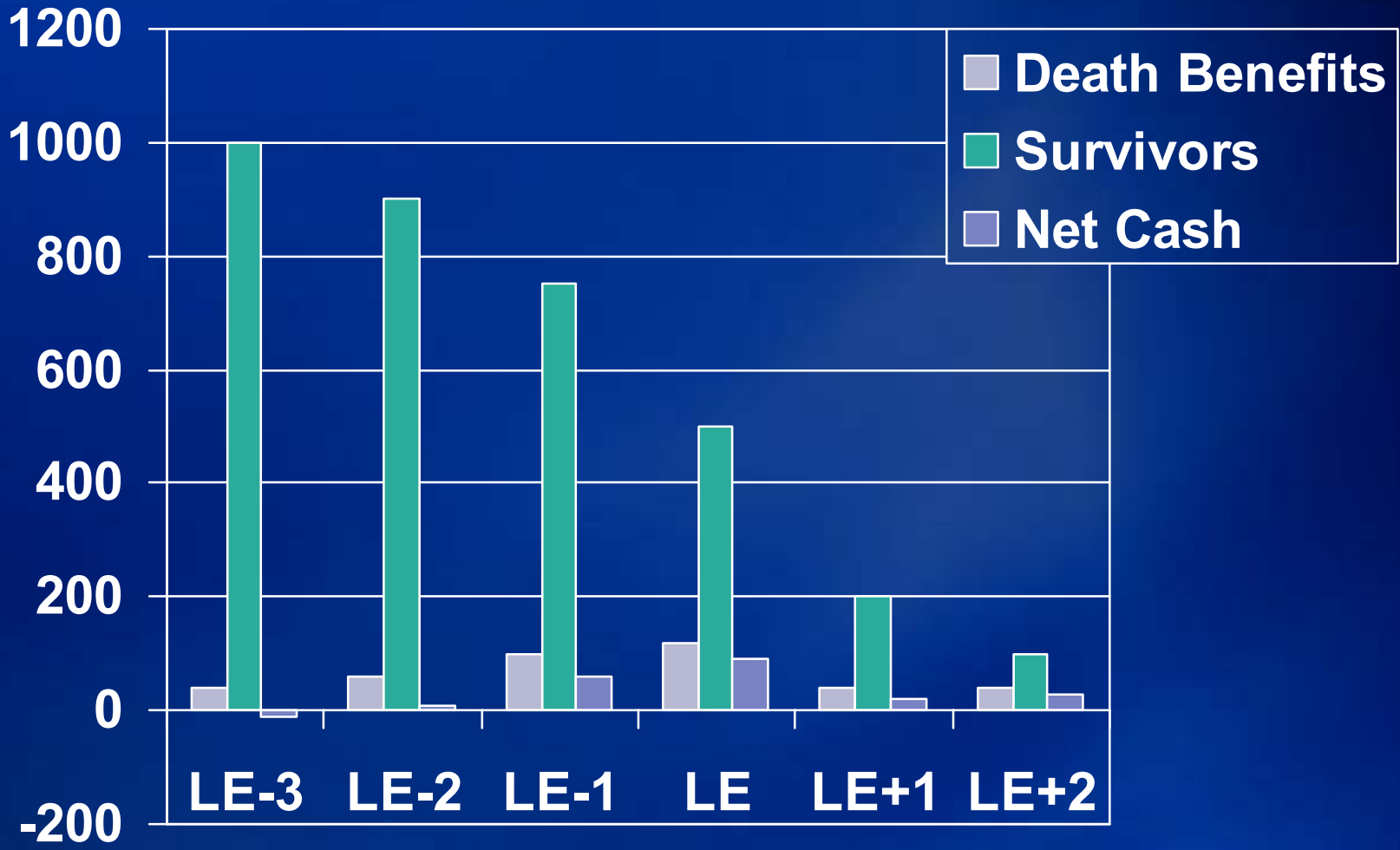
- Smaller number of policies
- Disparate size of benefits
- Premium cost

Risk/reward relationship can be examined

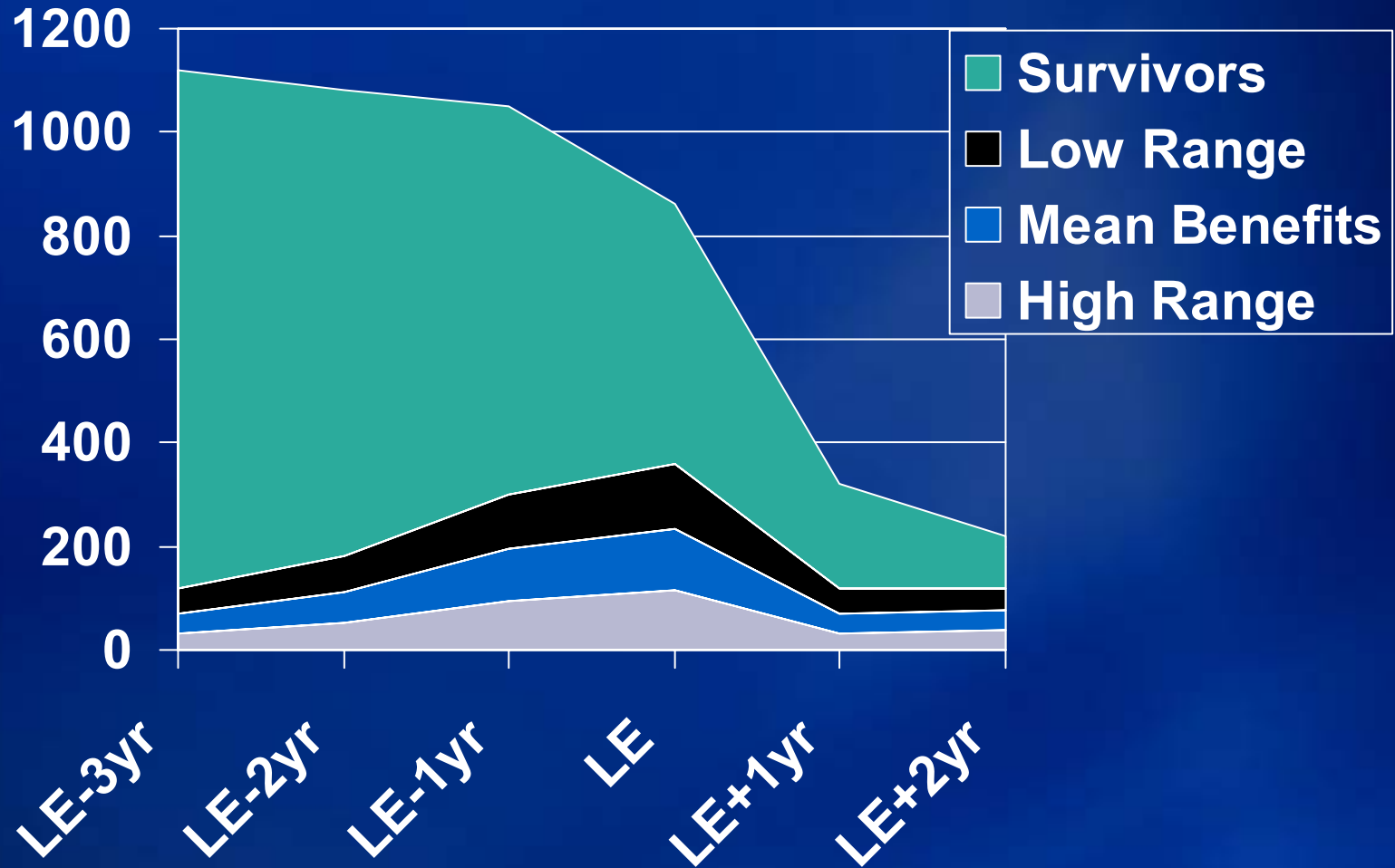
Graph of Results - LE



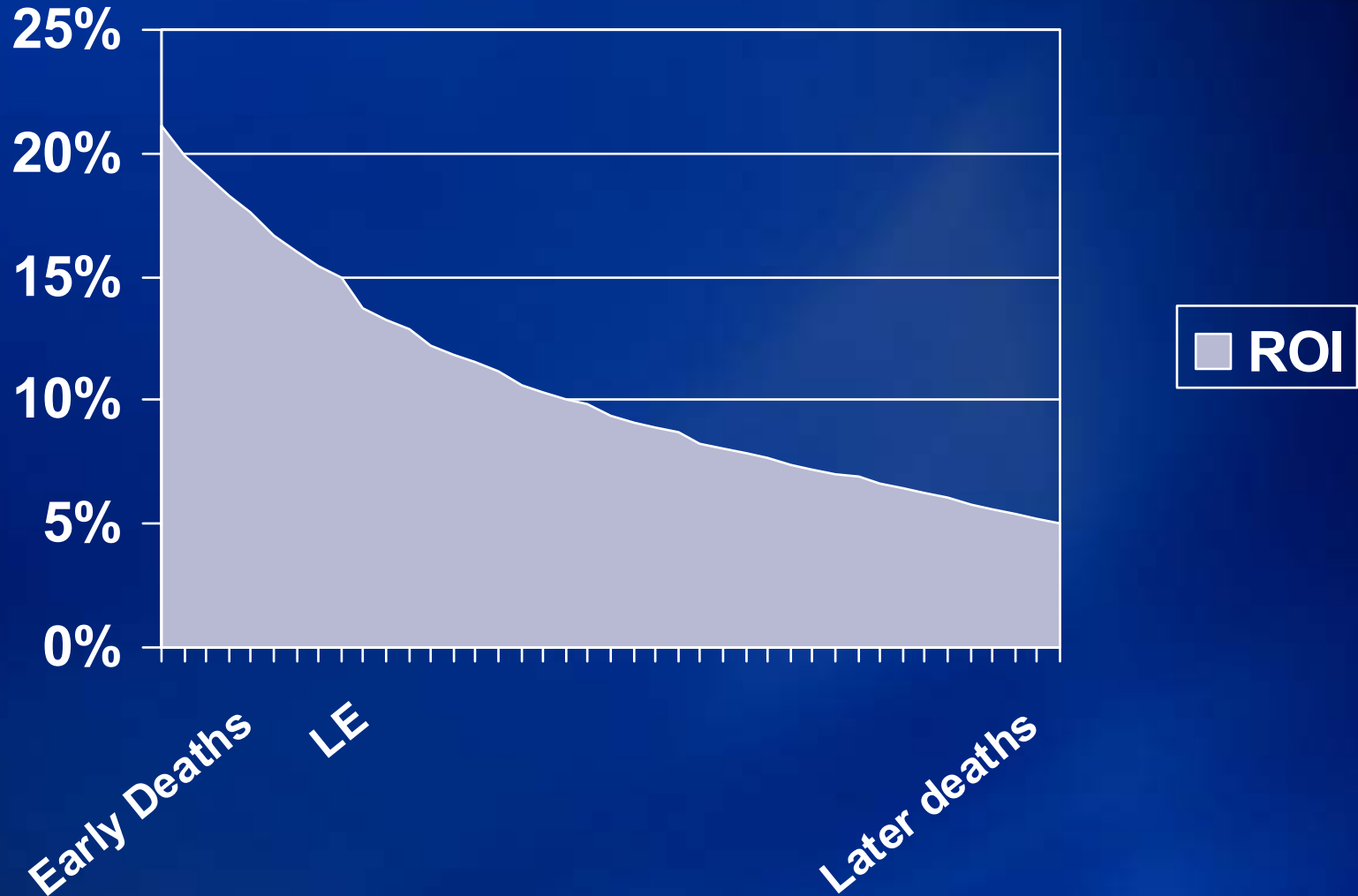
Graph of Results - DM



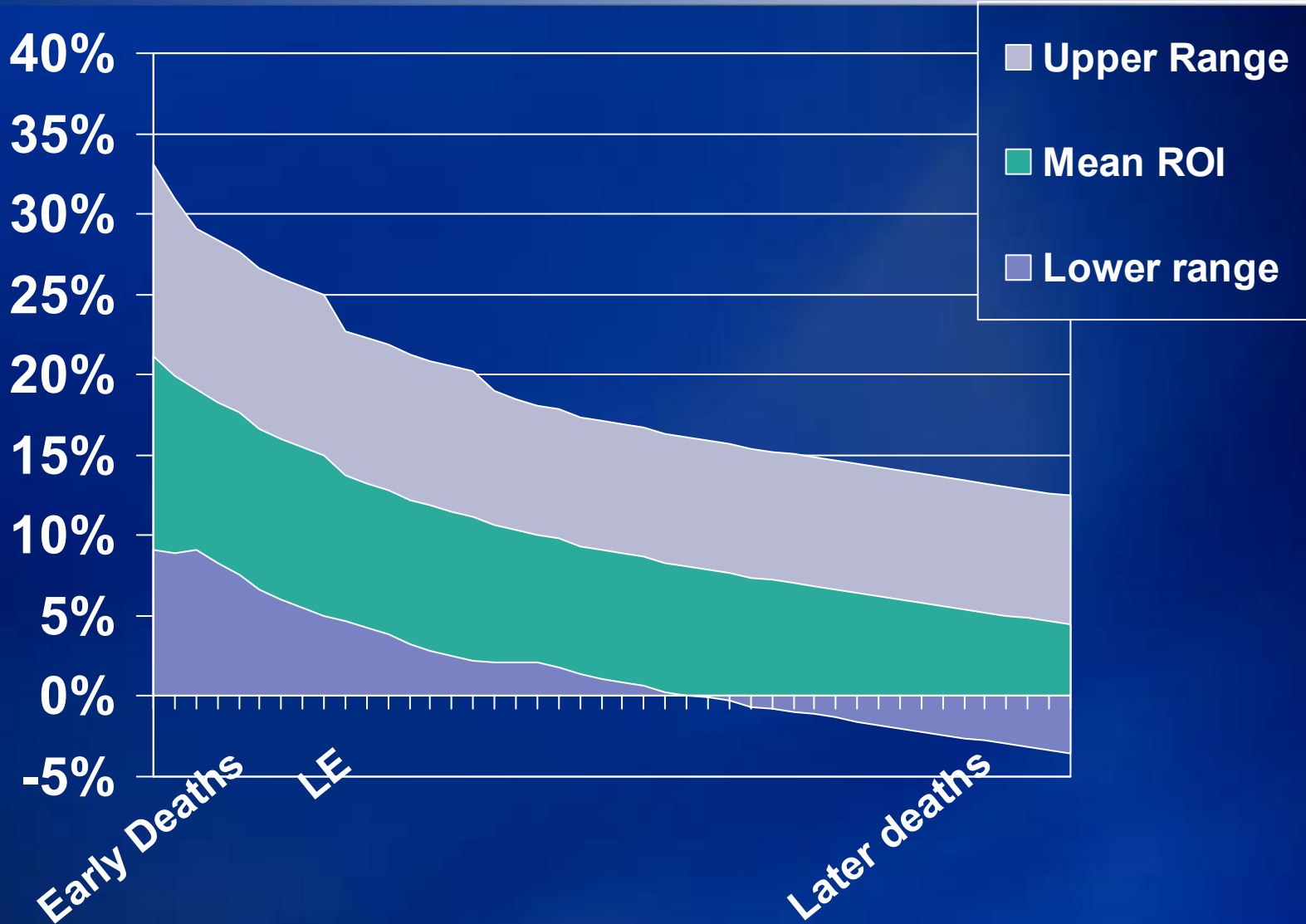
Graph of Results - SM



ROI Results (DM)– by quarter



ROI Results(SM)– by quarter



Impact on Direct Companies

Lapse Assumption Changes

- If lapse supported – profits may not realized
- Usually lapses are bad but ...
- Last Survivor Policies

Long term mortality assumptions

- Worse lives will persist – overall mortality worsens

Counter Measures

Future Developments

Reporting Issues

Licensing Requirements

LE Validation

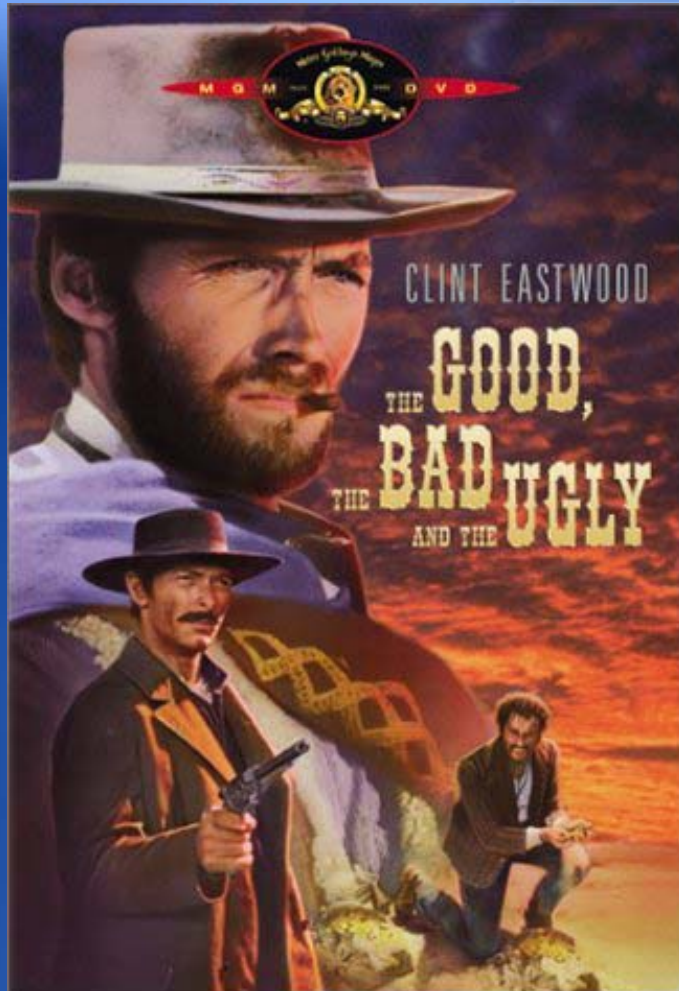
Market Tightening?

Broker Compensation

Market Availability

Life Companies' Reaction

Spitzer Action



Life Settlements

Questions?

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