

Institutions renew interest in life settlements

Recent SEC crackdown may make business stronger, observers say

By Darla Mercado

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Notwithstanding a recent crackdown by the SEC, the market for life settlements — which froze during the credit crisis — is beginning to warm up.

Credit Suisse Life Settlements is ramping up its purchase of life settlements on the secondary market, and reports greater competition from other institutional buyers.

In December, Fortress Investment Group LLC bought the U.S. life settlements portfolio of KBC Financial Products, an arm of KBC Bank NV of the Netherlands.

Also last month, Proverian Capital LLC said that it intends to build a large portfolio of life settlements. According to sources, the company is buying the policies for Cerberus Capital Management, a large hedge fund manager.

Even as the business expands, however, the Securities and Exchange Commission is taking a harder look at the life settlements market.


On Jan. 20, the SEC charged Provident Capital Indemnity Ltd., a Costa Rican provider of bonds on life settlements, with fraud. Also charged were the company's president and its outside auditor.

The commission is also investigating Life Partners Inc., a firm that sets up deals for investors to buy life insurance policies from policyholders.

The SEC's latest moves are encouraging to industry observers, who think that a cleaner image will attract more individual customers. They think that the regulatory actions likely will lead to tougher standards on the part of the Financial Industry Regulatory Authority Inc. and the SEC, give institutional investors greater confidence when they buy life settlements, and attract reputable players to the business.

“There was some bad stuff in the days before the SEC was really in it,” said Julius A.

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Rousseau III, a partner at Arent Fox LLP. “Now that this is getting regulated, we can carve off illegitimate deals.”

The SEC's focus on this market follows the release last year of a report by its life settlements task force, which recommended that the commission push Congress to expand the federal definition of “security” to apply to life settlements. The report also called on Congress and state legislators to strengthen oversight of life expectancy underwriters.

Finra already requires firms that add variable life settlements to their mix to seek approval for a material change in business and also apply best-execution, suitability and supervisory procedures.

The regulatory crackdown has broker-dealers cheering.

“I'm very pleased that the SEC is doing this, and I would like more — not less — regulation in this area,” said Jim Swink, vice president of Raymond James Insurance Group.

At Raymond James, the sale of a client's life insurance policy is a three-month process requiring the financial adviser and the firm to agree that a sale is the best course of action for the client. The process also entails the assistance of a third-party life settlements specialist and two life expectancy companies.

The sale's final stage is a bidding process in which institutional buyers, such as Credit Suisse Group AG and Berkshire Hathaway Inc., post offers for the policy, Mr. Swink said. The adviser, client and insurance experts at Raymond James are all involved in choosing the best offer.

“Because of the compliance oversight we have on these types of transactions, and because of the way we review every step of this transaction, the news doesn't affect the way we oversee our business,” Mr. Swink said.

Raymond James doesn't sell clients' policies to purchasing groups or individuals, only to institutional buyers, he said.

Another encouraging sign for institutional buyers and individual policyholders is the SEC's closer attention to life expectancy data.


Generally, investors pay a premium for policies in which insured individuals are expected to die sooner rather than later. The policy of a person who lives longer returns less to investors in life settlements, who must keep up the premiums until the person's death.

The SEC is raising questions about who holds the regulatory reins over the firms that issue life expectancy guidelines, said Caleb Callahan, vice president of investment marketing at ValMark Securities Inc.

“What's uniquely different about this business is that you don't know when life expectancies are either overstated or understated until mortality starts to happen. There is a lag in time on whether you're right or close; you won't know for a few years,” Mr. Callahan said.


“When you have a securities enforcement agency being more knowledgeable about how money is raised and spent in the secondary market, you'll have more confidence that institutional investors will be more attracted to life settlements,” he said.

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