



SOCIETY OF ACTUARIES

Article from:

# Actuary of the Future Newsletter

October 2003 – Issue 15

# The Viatical and Life Settlement Industry: New Perspectives for Actuaries

by Teresa R. Winer

**R**ecently I surveyed professionals in the viatical and life settlement (a.k.a. secondary insurance) industry to discover how actuaries could best serve this particular business. I solicited opinions from current viatical and life settlement brokers and investment company representatives on how actuaries could add value to their industry. The survey covered areas where actuaries might be welcomed by other professionals in the industry. The full survey results and report are published on the SOA's Web site.

As a part of my research, I attended the Viatical and Life Settlement Association of America (VLSAA) meeting in November 2002 to speak to those in the industry personally. I surveyed VLSAA industry professionals about how actuaries could best provide services. Both brokers who represent the individual client/viator and investment company professionals who represent the investors participated in the survey.

The survey included 14 areas in which personal or other actuaries could serve the viatical brokerage and investor companies. The survey was intended to be general; therefore the exact nature of the actuarial work needed was not probed. Many in the

industry are not aware of specific capabilities of actuaries, but they are familiar with the broad general areas in which actuaries are typically associated. Out of approximately 28 people who attended the meeting, 22 completed surveys. In every applicable question, respondents indicated a need for actuarial help.

## Issues in the Viatical Industry

The three primary issues facing the viatical industry currently are fraud, state regulations and mortality assumptions.

In November 2002, a popular consumer advocate based in Atlanta, Clark Howard, did a segment on the local news concerning "viaticals." Howard interviewed a duped investor from Jasper, Georgia who had hoped for up to a 40 percent return on his investment in "viaticals." The company he invested with was a Florida firm that was no longer in business. Howard stated that half of "viaticals" were fraudulent, with no reference as to where such statistics were derived. Investors have filed a class action lawsuit against the investment firm, First Financial.

The book *Blue Latitudes*, by Tony Horowitz, describes an island named Tonga that invested funds in the "viatical industry." On page 268, it explains that the throne of Tonga "issued a royal decree naming as 'court jester' an American Buddhist who was also entrusted with managing the country's trust fund. The jester gambled most of the fund on America's unregulated 'viatical industry'—buying the insurance policies of elderly or terminally ill patients, in hopes they'd die while the policy was still worth more than its cost—and promptly lost \$20 million U.S., or more than half the annual budget of Tonga's government."

Concerns about fraud have caused regulators to become more active in this industry.

State regulations were a big item of discussion at the meeting. Some states do not regulate the industry at all. The National Association of Insurance Commissioners (NAIC) is drafting a model regulation for states to adopt. At their March 8, 2003 meeting in Atlanta, the NAIC Viatical Settlements



Working Group of the Life Insurance and Annuities (A) Committee addressed some of the industry concerns regarding the proposed Viatical Settlements Model Regulation. The committee is currently soliciting comments regarding the draft regulation.

The states are beginning to take note of the viatical and life settlement industry with new regulations and licensing requirements. For example, Iowa regulations establish required fiduciary duties of the brokers to the viator. The Iowa regulation specifically exempts attorneys, CPA's, accountants and nationally accredited financial planners from fiduciary requirements without mentioning actuaries. The exemptions assume certain professionals already have their own standards of practice. The omission of actuaries indicates a lack of awareness of actuarial involvement in the industry. At the other extreme, New Jersey requires that an actuary review every viatical or life settlement transaction.

Thomas Moran, who works for The Heritage Group, stated at the NAIC Viatical Settlement Working Group meeting on March 8: "The biggest problem the viatical provider companies are having is incorrect life expectancies...People are living too long...As a result the problem manifests itself in the premium reserve diminishing too fast and the money is not there to pay premiums."

Investors in the secondary insurance marketplace are relying on life expectancy calculations and assumptions about mortality that are often not reliable. The reasons include the calculation itself, the underlying standard mortality assumptions and the substandard adjustments. Current financial problems for life settlement investors could be alleviated by access to better life expectancy evaluations. Accurate life expectancy estimates are critical to the long-term success of all secondary insurance transactions.

Members of the VLSAA need more data, including updated senior mortality rates. They need mortality studies performed on their clients. Many viatical companies are willing to share their data for this purpose.

Investors in viatical and senior settlement policies need accurate mortality assumptions to make a sound investment. Mortality assumptions at older ages are often set too high, to make the policies look more attractive to the buyer. Even with factors added to a standard mortality table, such as the 75-80 Basic mortality table (which is often used) the

underlying senior age mortality assumptions may still be unreasonable.

According to Bragg Associates, an actuarial firm specializing in mortality tables, relatively younger ages out of the senior age group are experiencing lower mortality than many annuity tables would indicate. Jack Bragg, FSA, of Bragg Associates, asserts that the mortality slope of the 2000 Valuation Basic table (the basis of the 2000 CSO table) is too steep at senior ages, except at the very end of the table, as compared to his recent experience studies. In other words, Bragg suggests that senior mortality rates in such published tables are generally too high except at the very oldest ages at the end of the mortality table. Some table rates may be purposely set high to promote conservatism in reserve calculations for death benefits. The published table rates are not reliable for life settlement purposes.

### Opportunities and Concerns for Actuaries

Overall, actuaries are welcome in many areas. The most cited areas included working with the NAIC, life expectancies and associated risk factors, financial projections, understanding life insurance policies and reinsurance, and evaluating settlement offers arising from lawsuits. Another potential role for actuaries is working with physicians in assessing mortality implications of medical impairments.

One respondent indicated that an actuary was on retainer with the firm he/she represented, but did not elaborate as to what capacity. Actuaries have been retained by viatical investor companies to evaluate life expectancies. Actuaries could help determine a fair price in any case, where all parties could be more satisfied in the long run. To find an actuary, most would call either the Society of Actuaries or search on the Internet.

One of the concerns of those in the viatical industry regarding actuaries is that their consulting fees may be too high. New Jersey's requirements raise concerns by viatical brokers and investors that the requirement will effectively make the secondary insurance transaction too expensive.

Regardless of what opinions are about the viatical and life settlement business, it exists. Actuaries could contribute to rationalizing the determination of risk in the market, offering a more fair and equitable value for the public.

INVESTORS IN VIACIAL AND SENIOR SETTLEMENT POLICIES NEED ACCURATE MORTALITY ASSUMPTIONS TO MAKE A SOUND INVESTMENT.

continued on page 12






This study illustrates that a lot more work could be done, such as researching the viatical and life settlement industry further, educating actuaries to serve this and other areas, and educating the market and the public. Studies could delve further into specific issues in areas where actuaries should play a role. From the survey results we know that actuaries can become involved in many ways, but the issues related to the general areas need to be defined. For example, are there certain life insurance provisions that cause difficulty?

Actuaries could enter the reinsurance area by helping with mortality projections or providing a stop-loss type of reinsurance product that would protect the investor against a loss caused by the insured living beyond a certain number of years. Actuaries can provide such probability estimates as well as an analysis of deviations of actual mortality from expected. A short overview of the reinsurance needs in this marketplace and a description of the actuarial role related to reinsurance could be produced by future studies.

Actuaries can advise individuals either through brokers directly. In addition, actuaries can provide advice on tax implications, especially for very wealthy clients. An actuary could help individuals examine all of their options to make an informed decision. Research work could be undertaken to help actuaries best calculate an actuarially fair settlement and to provide ethical and professional advice to consumers as well as investors.

Involvement by actuaries could enhance the life settlement process in many ways, including: determining prices of life settlement contracts, helping individuals understand the fair value of the contract, helping brokers in assessing values of contracts, providing life expectancy education to those in the industry and the public, and working with investor companies on purchase prices and reinsurance costs. Actuaries could help analyze and correct improper life expectancy calculations being generated for the industry.

Actuarial professional associations should consider partnering efforts with viatical and life settlement industry associations. There is clearly a need for more communication between our professional associations. The American Academy of Actuaries has helped publicize the profession through its *Contingencies* magazine and other efforts. The SOA External Relations Committee is seeking to connect with other professional organizations, recognizing that the task of educating actuaries cannot be done in a vacuum. Much is being done to expand the reach of actuaries. Much more can be done to open doors in emerging markets and we need continued dedication of the actuaries that are involved in these organizations.

For more basic information on the viatical and life settlement industry, refer to the full paper online. 

## References

*Contingencies*, March/April 2000, pp 26 – 33, “Getting Personal” by Jack Bragg.

*Contingencies*, March/April 2002, pp 17-20, “A Free Market for Life Insurance” by Eric W. Sippei and Alan H. Buerger; pp 22-24, “Viatical and Life Settlement Transactions” by Joseph M. Belth.

SOA Library, [www.soa.org](http://www.soa.org), 2000, “Marketing Research: Actuaries Serving Individuals,” by Teresa R. Winer.

*Blue Latitudes*, by Tony Horowitz, page 268.



Teresa Russ Winer, FSA, MAAA, is an actuary at Chastain Financial Services in Atlanta, GA. She can be reached at [twiner@att.net](mailto:twiner@att.net).

