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STATEMENT OF THE ACLI REGARDING SECURITIZATION OF LIFE SETTLEMENTS

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The American Council of Life Insurers (ACLI) recommends that the securitization of life settlements be prohibited by legislation or regulation.

Securitization may encourage promoters of these packages to prey upon senior citizens urging seniors to settle their life insurance policies even if a settlement is not in their economic best interests.

Insurers are also concerned about public policy implications of stranger-originated life insurance (STOLI), where promoters of life settlements induce seniors to buy life insurance policies that they would not otherwise purchase in anticipation of profit from the sale of the policy to investors at the end of the policy contestability period. Since there are only a limited number of insured individuals who want or need to sell their existing insurance policies and are of an age and expected mortality profile to be of interest to settlement providers, promoters of life settlement artificially manufacture new life insurance sales to generate an inventory of policies for investors. Seniors are offered a variety of inducements, including cash payments and promises of "free insurance" obtained through the use of forgivable premium financing, to participate in the fraudulent origination of policies.

Securitization of life settlements will exacerbate the STOLI problem. Securitization is a very effective means of market-making and encouraging rapid expansion of a "product", in this case, life settlement contracts. Promoters will use capital generated from securitization to create larger inventories of life settlement contracts which, in turn, will fuel more securitizations and more STOLI.

Life settlement securitization also poses risks for the investors purchasing settlement securities, sometimes referred to as "death bonds", "blood pools" and "collaterized death obligations". This is true for at least two reasons.

First, securitization divorces the life settlement provider from the ultimate risk associated with the purchase. The provider which purchases a senior's policy should be responsible for accurate settlement risk assessment and not insulated by securitization from such responsibility. This is comparable to what happened with the mortgage securitization market, which facilitated and fueled the proliferation of subprime and "no-doc" mortgages. The ultimate risk to life settlement investors is that the senior will live longer than expected and hence "ruin" the investment return.

- Investing in a life settlement contract only makes economic sense when the insured person has a relatively predictable -- and shortened -- life span. The life settlement investors must pay premiums to keep the policy in force until the pay-day death of the insured. This cost, combined with the amount paid to acquire the rights to the death benefit and related broker fees, can exceed the death benefit if the insured lives "too long." Medical innovation, cures for disease and better elder care are detrimental to the value of the investment.

- Unlike the residential mortgage market, where there was a credible argument that securitization of mortgages freed capital for additional consumer lending, there is no capacity issue when it comes to the resale of existing life insurance policies. In fact, even without securitization, some promoters of life settlements have created artificial insurance transactions (STOLI) in order to fuel the demand for life settlement contracts. Investors in life settlement securitizations will have no hard assets as security for the inevitable default and fraud losses that attach to these investments with alarming regularity. This is unlike mortgage securitizations, where there is at least some tangible asset base guaranteeing some value.

- Rating agency experts advise that there is no standard method and no common set of assumptions used by life settlement providers to predict the life expectancies of the insured seniors whose policies are being purchased, either at the time of the elderly owner's entry into the life settlement contract or at the time of a contract resale. They advise that, if there are no restrictions on the pooling and securitization of life settlement contracts, there is little incentive for life settlement providers to "get it right" in terms of medical underwriting and respect for insurable interest requirements.

Second, there is a lack of transparency for investors in the securitization since they are not permitted to perform due diligence by examining the settlement underwriting files. While protection of the personal medical information about the person whose life is insured is important, other details about individually settled policies and the senior lives which are insured are needed by investors for risk evaluation. This information includes the current age of each insured and his/her life expectancy, the amount paid to the policy owner for purchase of the life policy, future annual premium amounts, the date of each policy's issuance and when it was transferred (sold) to the life settlement provider. The amount and quality of information that will be made available to investors in life settlement securitizations is insufficient for any respectable securitization. This was a factor in some rating agencies declining the opportunity to rate life settlement pools.

In summary, securitization of life settlements presents dangers to the insured public and to the investors who buy the securities. The only constituencies without risk on securitization will be the life settlement brokers and providers, security underwriters and middlemen lawyers, accountants and rating agencies who will enjoy fee income. Inevitably, life settlement-backed securities will be contaminated with STOLI policies, which will then be passed on to unsuspecting pension funds and other far-removed investors. Since STOLI is prohibited or statutorily restricted in over half the states and violates state insurable interest laws, these securities may be subject to regulatory enforcement actions or lengthy and costly litigation. The fact that there are now over 200 lawsuits involving life settlements – many filed by disgruntled investors – sounds a warning.

Securitization of life settlement contracts does not satisfy any consumer or societal need. Securitization will foster the proliferation of STOLI which undermines long-standing public policy that life insurance policies be supported by insurable interest at their inception. For these reasons, ACLI recommends that the securitization of life settlements be prohibited by law.