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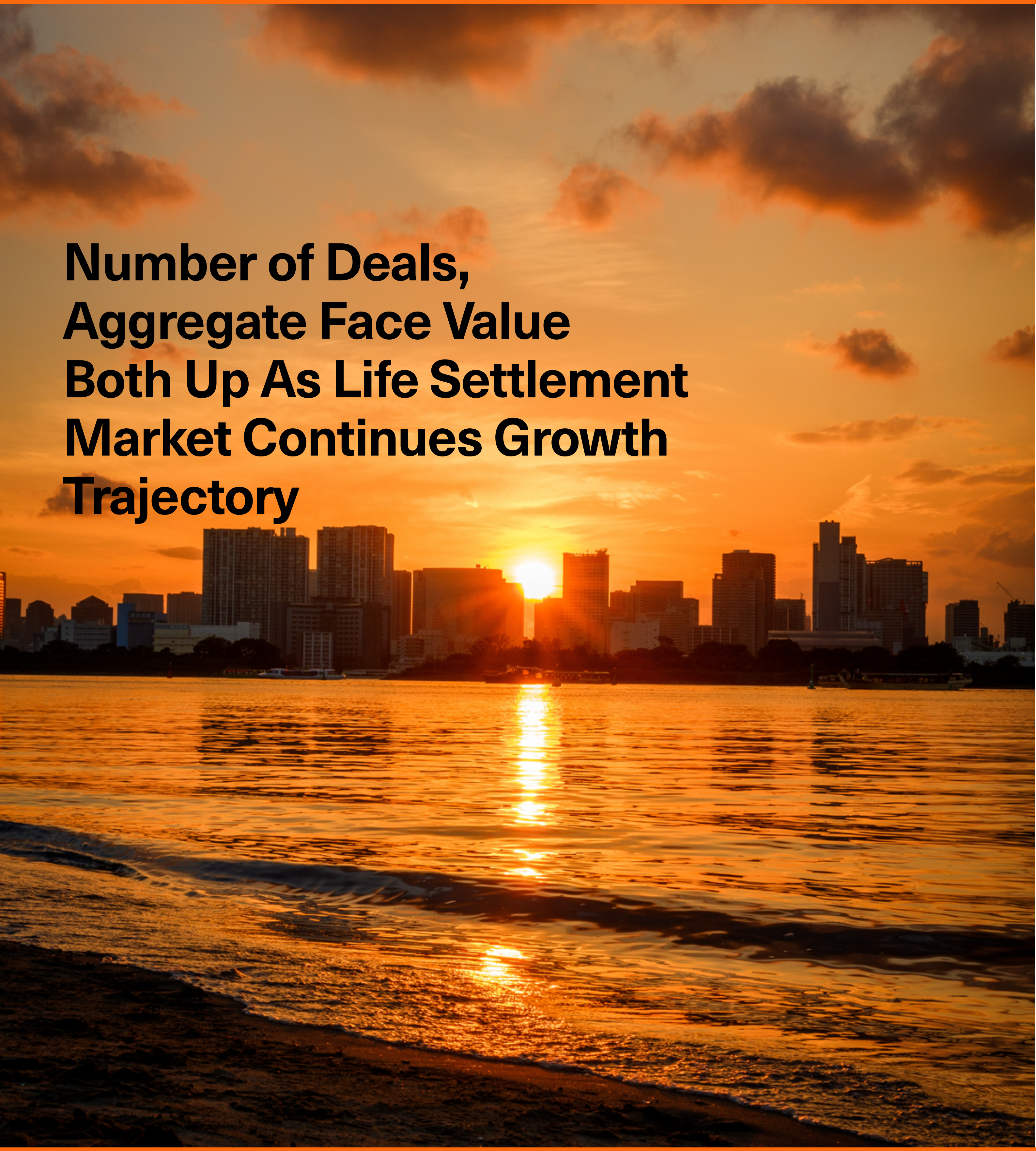
Number of Deals, Aggregate Face Value Both Up As Life Settlement Market Continues Growth Trajectory



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Editor's Letter, Volume 3, Issue 06, June 2024

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Life Risk News

Industry publication The Deal publishes an annual report that looks at the number of transactions in the life settlement industry's secondary market. This year, the headline numbers show a market in growth mode, as both the number of deals and the total value of them have increased for the third consecutive year. *Greg Winterton* spoke to **Rainer Gruenig**, CEO at **Plenum Investments**, **Rob Haynie**, Managing Director at **Life Insurance Settlements, Inc**. and **Anton Pozine**, Portfolio Manager at **Ress Capital** to get an asset manager's perspective on the state of the secondary market in *Number of Deals, Aggregate Face Value Both Up As Life Settlement Market Continues Growth Trajectory*.

The UK's **Prudential Regulation Authority** will introduce stress testing for insurers' exposure to funded reinsurance transactions for the first time in 2025. *Aaron Woolner* dissected a recent speech given by **Lisa Leaman**, Head of Insurance Supervision at the **PRA** at a recent industry conference to extract the most salient points in *Regulatory Oversight to Provide UK Bulk Purchase Annuity Market with Busy Few Years*.

In mid-May, insurance company PHL Variable and its subsidiaries entered into rehabilitation. Greg Winterton spoke to **Brian Casey**, Partner and Co-Leader of the Regulatory and Transactional Insurance Practice Group at **Locke Lord** and **Patrick McAdams**, Investment Director at **SL Investment Management** to learn more about the bigger picture in *PHL Variable Rehabilitation Emphasises Need for Prudent Counterparty Risk Management*.

Wealth has long had a high correlation with longevity – those more prosperous tend to live longer. But recent research shows that may no longer be the case. *Aaron Woolner* spoke to **Shantel Aris**, Head of Longevity Experience Studies at **Club Vita**, to learn more in *Is Education the Primary Driver of Life Expectancy?*

The risk that a life settlement provider failed to hew to the letter of the law is one which has incentivized funds to undertake careful diligence on the underlying purchase transaction to confirm that the providers they use to originate policies are compliant. **James W. Maxson**, Partner at **EM3 Law** addresses the statutory framework pursuant to which an individual with 'seller's remorse can pursue claims for violations of state life settlement statutes with the result that a transaction can be unwound or damages sought from the provider and/or ultimate fund/owner in *Do Life Settlement Statutes Create Private Rights of Action?*, a guest article.

One of the most common ills of mankind is chronic pain. However, in some cases, there is not an obvious connection between the pain and the chronic muscle spasm that was responsible for the chronic pain. In any case, treatment of chronic pain requires knowledge of its source. **Roger H. Coletti**, Medical Director at **Fasano Underwriting,** digs into a new treatment protocol, CMECD, and its potential benefits in *Innovating Beyond Cardiology: Discoveries in Acquired Chronic Muscle Spasm and Resulting Chronic Pain*, our second guest article this month.

Our *Q&A* this month features **John Kiff**, now an independent consultant and formerly of the **International Monetary Fund**. Kiff has been on top of the longevity risk transfer market for almost 20 years and offers his thoughts on the space this month.

The rising interest rate environment of the past two and a half years has had the impact of reining in deal activity in some life ILS trades, like balance sheet lending or value-in-force (VIF) deals, because rising rates make these transactions more expensive for life insurers, thus dampening demand. That is not the case in the asset-intensive corner of the life ILS market, however. *Greg Winterton* spoke to **Gokul Sudarsana**, Chief Investment Officer – Life Insurance at **Hudson Structured Capital Management Ltd.** (d/b/a HSCM Bermuda) to learn more about activity and trends in this part of the life ILS market in *Solid Outlook for Growing Asset-Intensive Life ILS Transaction Market*.

I hope you enjoy the latest issue of Life Risk News.

Number of Deals, Aggregate Face Value Both Up As Life Settlement Market Continues Growth Trajectory

Author:
Greg Winterton
Contributing Editor
Life Risk News

The life settlement industry's secondary market has grown for the third consecutive year, according to The Deal's life settlements league tables, published in early June.

The Deal collects transaction data by licensed life settlement providers via public records requests to state insurance departments. Providers are a mandatory participant in the life settlement market, so the data has become something of an annual bellwether for the health of the market overall.

This year, the two main points are that the number of transactions completed in the secondary market is up for the third consecutive year, and the aggregate face value of all transactions is, at $4.72bn, the highest since 2010.

The increase in the number of transactions continues the slow-but-steady upwards trend in secondary market activity of the past couple of years. Last year, 3,181 transactions were recorded; in 2022, 3,057 deals were done, and in 2021, 2,937, for an average of around 4% growth per year.

> **"A few things were different last year compared to historical trends. Notably, we saw the average age of insured tending to be younger, with higher mortality multipliers"**
> **- Rainer Gruenig, Plenum Investments**

The type of life insurance policy that accounts for these transactions most often is Universal Life. Historically, it's been the septuagenarians – and older - with a UL policy that entered the market through the broker channel who have been the mainstay of the space. That's still true, mostly, but increasingly, albeit slowly, that's changing.

"A few things were different last year compared to historical trends," said Rainer Gruenig, CEO at Zurich-based Plenum Investments.

"Notably, we saw the average age of insured tending to be younger, with higher mortality multipliers."

That's not all. Another feature of the market last year was driven by a trend that has been establishing itself significantly in the secondary market in recent times.

"We saw more smaller face value policies in the secondary market last year," said Anton Pozine, Portfolio Manager at Ress Capital.

"This was mainly due to the direct-to-consumer efforts by several providers in the market."

The aggregate face value of transactions in the secondary market last year was, at $4.7bn, the highest level since 2010, when $8bn of transactions were concluded. Those days, however, were when premium financed policies, where policyholders borrowed funds to pay the premiums to keep the policies in force, were popular.

Legal risk – the life settlement industry has been on the wrong end of a few court decisions that declared premium financed policies as lacking an insurable interest in the past decade - has had the effect of reducing the amount of these types of policies that entered the market and although some still remain in the tertiary space, in the last decade, a more stable secondary market has emerged.

Since the aggregate annual face amount hit a low of $1.3bn in 2011, only twice has the secondary market shrunk, in 2014 and 2021. Rob Haynie, Managing Director at Life Insurance Settlements Inc., puts that down largely to market awareness.

"Growing the secondary market has been a slow process. And it continues to be slow. But there are plenty of efforts by industry groups to raise awareness, and media advertising by some providers has certainly had an impact. Also, the RIA channel continues to evolve and learn about our market. It's made a notable difference," he said.

In some private market segments, large deals can occasionally distort the market; indeed, Legal and General Retirement of America's quarterly pension risk transfer monitor recorded an estimated $15bn of deals in the US PRT market in the first quarter of this year, $11bn of which was accounted for by just two deals. It is a similar story in the life insurance Insurtech space, where in 2023, 19 deals were completed in North America worth $326.5m, with just one of these, Devoted Health's Series E round, accounting for $175m of that.

Not so with life settlements. While there is a wide range in policy size, they need to be large enough to make the numbers work for investors. And, when compared to the two markets above, there is a much higher frequency of transactions. But in order to get the attention of investors the way that other private markets do, Pozine says that more significant movements are required.

> **“It is of course positive that the number of transactions increased last year, but you could argue that the market size is still rather small in absolute terms. It would make much more of a difference if we saw some larger increases over a number of years”**
> **- Anton Pozine, Ress Capital**

“It is of course positive that the number of transactions increased last year, but you could argue that the market size is still rather small in absolute terms,” he said.

“It would make much more of a difference if we saw some larger increases over a number of years.”

Still, the market shows few signs of slowing down. The drivers of supply in the life settlement market - the insured senior simply doesn’t feel that they need the policy anymore – perhaps their children have left home, and their mortgage is paid off, for example, the need for cash to help with personal bills, such as healthcare-related expenses and senior living costs, or that they simply can’t afford the premiums anymore – are ever-present, and, according to Gruenig, driving activity this year as well.

“The first half of this year has been even busier for us. We have been offered hundreds of policies,” he said. “I think that there are lots of policies being marketed where the current owner can’t afford or doesn’t want to pay the premiums anymore. Cash definitely has become a value – so instead of paying premiums, the policy owners prefer to sell the policies and get some cash at hand. And there is enough demand to clear the secondary market supply,” he said.

Anecdotal evidence suggests that tertiary market activity has been slower in the past twelve months or so, driving asset managers that play in both sandpits to the secondary market to flesh out their portfolios.

Whether the tertiary market experiences a renaissance this year or not; whether aggregate face values exceed $5bn for the first time since 2010 or not; and whether the number of transactions increases or not, remains to be seen. But the general trend is, for Haynie, encouraging.

“You can’t expect the numbers to go up every year – you never know if there will be an extraordinary situation like Covid, for example, that might impact the space. What’s most important is that the general trend is up over time, both in terms of the number of policies transacted in the secondary market and the aggregate face value. The data coming out of The Deal this year, and LISA’s own member data published in May, show that we have a growing market. We continue to see encouraging data and trends in our industry.”

Regulatory Oversight to Provide UK Bulk Purchase Annuity Market with Busy Few Years

Author:
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Life Risk News

The UK's Prudential Regulation Authority (PRA) will introduce stress testing for insurers' exposure to funded reinsurance (funded re) transactions for the first time in 2025. The UK regulator first signaled its concerns over the use of this type of reinsurance treaty in June 2023 when it warned this structure could leave carriers exposed in stressed markets.

Speaking at an industry conference in April, Lisa Leaman, Head of Insurance Supervision at the PRA, said that the 2025 Life Insurance Stress Test (LIST), due to be published in June, would outline the proposed funded re stress tests.

Funded re is the transfer of all the material risks of a bulk purchase annuity (BPA) transaction – both investment and insurance – to counterparties, which are sometimes based outside the UK.

An example of this type of transaction is when a book of in-force annuities moved from an unnamed UK insurer to Bermuda-based Resolution Re in February 2024 in a deal worth £2.5bn.

While German authorities quashed a deal between Zurich and life backbook specialist Viridium in January, UK regulators have not publicly stopped any similar deals despite a backdrop of the significant increase in funded re-linked BPA activity in recent years.

> **"Our stress test will assess the ability of firms to measure the risks associated with the recapture of a Funded Re arrangement in stressed conditions"**
> **- Lisa Leaman, The UK's Prudential Regulation Authority (PRA)**

Leaman, however, made clear that the UK prudential regulator was watching the sector closely.

"One motivation for these transactions is to invest in a wider range of assets, which may not be eligible for MA [Matching Adjustment}. This creates potential risks and capital strain on recapture if the collateral is not eligible for the MA," she said.

Leaman said that this strain was increasing.

Citing a 2018 PRA speech titled: 'An annuity is a very serious business', given by the regulator's then Executive Director of Insurance Supervision David Rule, she said transactions in the UK BPA market have increased from roughly £10bn a year in 2018 to over £50bn in 2023 and she predicted activity would double in size over the next decade.

This increase in BPA activity, and the increased use of funded re, has prompted an evolution in regulator's perception of the main risks facing BPA insurers.

Rule's 2018 speech cited data due diligence, longevity, and asset selection as the three biggest risks facing the sector. Six years later, in Leaman's talk to the same audience, she spoke about 'recapture risk' – that is, when insurers are left holding a pool of non-MA eligible assets in the event of taking back a book of business if a counterparty defaults – but the regulator also has other concerns.

"Our stress test will assess the ability of firms to measure the risks associated with the recapture of a Funded Re arrangement in stressed conditions," says Leaman

There is also additional risk if reinsurers in these transactions have large, concentrated exposures similar to those of the insurer ceding the risk.

This in turn has led to what Leaman termed an 'emerging risk' from the increased use of Funded Re by UK insurers.

Leaman stressed that the regulator is currently in the exploratory stage of understanding the industry's exposure to funded re; the conclusions of the stress tests will only be published at the sector, not company, level.

"We will continue to monitor the volume and the increase in complexity of Funded Re arrangements, as the product develops. This will inform our views on the publication of individual firm-level results of the Funded Re stress in future LIST exercises," says Leaman.

Another topic of relevance to the life insurance industry that Leaman mentioned at the conference is that of Solvency UK – the local iteration of the EU standard. The PRA will outline the next steps this month and Leaman said that the revised MA is the most relevant change for BPA players.

The MA gives an uplift to the risk-free rate when insurers match long term liabilities with similarly dated assets and is intended to reduce capital volatility for long term, buy and hold investors.

Leaman said there were a number of misconceptions circulating in the market around the potential changes to the MA regime and she made it clear that the PRA will not require firms to reapply for permission to apply MA status to an asset portfolio if it already has this under the existing Solvency II regime.

> **"The PRA will communicate, as part of the policy statement, the date(s) on which new requirements will take effect, and whether early adoption will be possible on a voluntary basis"**
> **- Lisa Leaman, The UK's Prudential Regulation Authority (PRA)**

She also said that reform of the MA was intended to broaden the pool of available assets and not exclude ones already permitted for MA calculation.

"Finally, we understand that the implementation date of 30 June 2024 for the MA reforms may pose practical challenges to firms in some areas. The PRA will communicate, as part of the policy statement, the date(s) on which new requirements will take effect, and whether early adoption will be possible on a voluntary basis," she says.

Leaman also said that the PRA is considering introducing MA 'sandboxes' - that is experimental environments to develop MA eligible assets which can then be granted regulatory approval.

She said that the regulator's immediate priority was to implement the current proposed set of reforms but that MA sandboxes could be included in the future.

"We are open to new ideas, and we agree that it is important to think about how we could bridge any gap that might emerge in future between what is allowed by the form of prudential regulation, and those financing needs of the UK economy that can best be met from the life insurance sector," says Leaman.

Leaman said that UK life insurers currently hold around £250bn in assets to back their long-term liabilities and by broadening the pool of assets that can be MA eligible would have major benefits for the UK economy.

Leaman also said that the government intended to review the impact of Solvency UK in five years' time to assess their impact, but she was bullish about the potential positive impact of the changes.

"What will the BPA sector look like in five years' time? I anticipate several positive developments. A far larger sector with insurers providing sound, efficient and effective management of defined benefit liabilities as they run off.

"More transparency, as market discipline will be enhanced by the disclosures from our Life Insurance Stress Tests. Enhanced accountability, with firms taking greater responsibility for the prudence of the MA through the new attestations that they will make," she says.

PHL Variable Rehabilitation Emphasises Need for Prudent Counterparty Risk Management

Author:
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Life Risk News

In mid-May, Connecticut Insurance Commissioner Andrew N. Mais filed a 'Petition for Rehabilitation and Appointment of the Commissioner as Rehabilitator of PHL Variable Insurance Company (PHL)' and its subsidiaries, Concord Re, Inc. and Palisado Re, Inc., in the Connecticut Superior Court.

"Today's filing underscores the Department's commitment to protecting consumers and ensuring the availability of a financially sound insurance industry in Connecticut," said Commissioner Mais in a press release.

"This action is a critical first step for the Department to begin developing and implementing a plan of rehabilitation that both maximizes the value of the Companies' assets and equitably administers PHL's business for the benefit of all policy and annuity holders," he added.

The Connecticut Insurance Department (CID) filed the petition after determining that the companies are in a hazardous financial condition and that "other alternatives have been thoroughly explored".

> **"Life insurance company rehabilitations are complex and lengthy. It's difficult to predict right now what will happen with PHL"**
> **- Brian Casey, Locke Lord**

Commissioner Mais, as Rehabilitator, expects to develop a plan of rehabilitation for the companies over the next 12 months.

There could be a significant impact on life settlement asset managers that own PHL policies in their portfolios here. The CID has issued a temporary moratorium order, which limits the payout of a claim for death benefits to $300,000 (until further notice), ostensibly until a Plan of Rehabilitation is developed.

This is significantly lower than the average death benefit in the life settlement market; recent data published by industry group the Life Insurance Settlement Association suggests that in 2023, the mean face value purchased in the industry's secondary market works out to approximately $1.45m.

Many policies transacted in the marketplace have a death benefit far north of that figure, however; there is a lot of variance in the range of death benefit size in the life settlement market. But regardless of whether an investor owns a $600,000 policy or a $5m policy, any maturations in the next year or so will yield only $300,000 while the rehabilitation process plays out. In the event of a liquidation, PHL policyowners looking to recover additional death benefit payouts will become claimants in the liquidation.

Those investors will, of course, be hoping that the plan of rehabilitation includes the payment of the full death benefit for in-force policies. The CID will try and find a white knight to absorb PHL, which could be another insurance company or even a buyer like a large private equity firm. But, according to Brian Casey, Partner and Co-Leader of the Regulatory and Transactional Insurance Practice Group at Locke Lord, it's not always clear and won't be for at least another year.

"Life insurance company rehabilitations are complex and lengthy," he said. "It's difficult to predict right now what will happen with PHL."

Whatever happens to PHL, and investors holding its policies, this news story brings into focus the topic of counterparty risk in the life settlement industry.

The worst-case scenario here is that PHL's rehabilitation is unsuccessful such that the company transitions from a rehabilitation into a liquidation proceeding. While solvency risk is a significant risk, it is also, comparatively, an infrequent one; there are only one or two life and health insurer failures each year. In 2022, there were more than 700 life insurers active in the US, so if one fails, plenty remain to support not only the American consumer but capital markets investors in the life insurance industry as well.

Instead, it is Cost of Insurance risk that is a much more frequently experienced carrier-related risk in the life settlement market. Life insurers are permitted to raise the cost of insurance on certain policies in situations where they need to raise capital, but they must apply to the state regulator to do so. That hasn't stopped multiple life insurers from doing so in the past decade, but subsequent class action lawsuits have been filed by policyholders against life insurers that raised the CoI which were 'won' by the plaintiffs, resulting in the return of excess payments to policyholders.

That doesn't mean that CoI risk should be underestimated, of course. But, according to Patrick McAdams, Investment Manager at SL Investment Management, a prudent life settlement investor has plenty of tools available through which they can mitigate their risk.

> **"Credit risk is pretty standard practice in our industry – you have credit rating limits, where you don't have exposure to a carrier that has a poor credit rating, for example, or at least, you keep that exposure to a minimum and cap max exposure to any one life insurance company"**
> **- Patrick McAdams, SL Investment Management**

"Most well managed life settlement portfolios have limits on concentrations in different factors, such as the age of the insured, gender, their life expectancies, policy size, carriers, and even medical conditions – you want to, say, cap exposure to insureds whose primary medical issue is diabetes. Credit risk is pretty standard practice in our industry – you have credit rating limits, where you don't have exposure to a carrier that has a poor credit rating, for example, or at least, you keep that exposure to a minimum and cap max exposure to any one life insurance company," he said.

The full extent of the impact on the life settlement market of PHL being placed into rehabilitation will not be known for many years. It's certainly not a good news story for the industry – PHL was exposed significantly to Universal Life policies, the type favoured by the life settlement market - so asset managers with PHL policies in their portfolios could be in for a tough time.

But investors with life settlements allocations should feel a touch reassured about the bigger picture. So far, there hasn't been a contagion effect in markets – the SPDR S&P Insurance ETF (KIE), while being down a dollar since the news broke, is up around 11% year to date at the time of publishing. According to Casey, the PHL situation, while not good, is not reflective of the US life insurance company industry at large.

"This is not a systemic issue for the life settlement market. This issue involved one life insurance company. The credit rating for life insurers in the US is generally strong, as is the regulatory environment under which they operate. It remains a benefit to the life settlement market that life insurers are the main counterparty in the space."

The Connecticut Insurance Department did not respond to a request for comment by press time.

Education the Primary Driver of Life Expectancy?

Author:
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Life Risk News

The UK's Institute and Faculty of Actuaries includes data from as far back as 1825 when calculating its life expectancy tables. Fundamental to those estimations is the importance of the correlation between income and life expectancy.

The effects of this relationship are still apparent today. Research by the McKinsey Global Institute shows that the GDP per capita in the Polish IT hub Wroclaw increased from $23,000 in 2000 to $55,000 two decades later.

Wroclaw's citizens saw their average life expectancy increase by 4.9 years in tandem with the influx of high paying jobs from tech giants such as Alphabet and IBM over the same period.

A change has occurred in the key drivers of living a longer, healthier life says Steve Prince, President of the Canadian Institute of Actuaries (CIA).

"Previous studies said that wealth was the major driver. But recent studies say that education is now a bigger factor than wealth," said Prince.

Prince's comments followed the publication of the CIA's Education and Longevity insight by Shantel Aris, Peter Gorham, and Jie Ji, in March this year. The paper looked at a literature review by actuary Robert Brown, on behalf of the institute.

> **"Previous studies said that wealth was the major driver. But recent studies say that education is now a bigger factor than wealth" - Steve Prince, Canadian Institute of Actuaries (CIA)**

While wealth has historically been believed to be the primary driver of life expectancy and longevity, the research review by the CIA showed that it is increasingly likely that educational attainment is the primary driver of differences in both wealth and longevity.

The studies, which were examined by the CIA, produced consistent results according to Aris, Head of Longevity Experience Studies at Club Vita – the more education people have, the longer they live.

"The studies have brought forward the thinking that now education is a primary driver for both wealth and longevity," she says.

"One of the challenges for the insurance industry is how to incorporate this research into life expectancy tables. At the moment education data is collected at an aggregate, not an individual, level by the industry."

Aris says that while the insurance industry currently relies on postcodes as a proxy form of data for wealth this doesn't allow for any degree of granularity over the level of education that an individual has.

"We work with postal code indicators and in those measures there is some element of the educational attainment of that area. But on an individual basis the datasets don't have an indicator that this person achieved a university degree versus a person that didn't complete high school."

Aris says that while on an individual level education is not being used vary widely by the insurance industry it is being incorporated more and more at an aggregate level."

"There's an increasing amount of research into the idea that education is a primary driver of longevity," she says.

But why is education potentially a better proxy for life expectancy than wealth? Smoking is the single most important factor. According to the CIA paper, smoking rates were almost four times higher among Canadians who didn't complete high school compared with university graduates.

The same trend was apparent outside of Canada with the CIA research saying that smoking explains half of the recent widening of the educational difference in life expectancy in several European countries, with the trend especially notable for women.

"This is not a purely Canadian phenomenon. In our paper, we saw a significant gap between the life expectancy of the lowest and highest education groups which is consistent across multiple countries.

"There are differences between countries over what is classified as low versus high education but it was consistent that we saw a difference across multiple countries," Aris says.

Strikingly, even among smokers, there are different life expectancy outcomes depending on the education level of the cigarette user. Aris says that this differential is potentially explained by higher levels of education leading to healthier lifestyle choices.

So, not only was there a greater percentage of smokers among lower education groups, they also experienced a higher level of mortality than their more educated peers.

Aris says that a plausible explanation for this difference is that better educated groups adopt otherwise more healthy lifestyles than their lower educated smoking peers.

> **"You see a trend where those with a higher education adopt healthier lifestyles, have better employment, and improved access to health care. Those are some of the drivers that we suspect explain the different outcomes for the same diseases between different social groups"**
> **- Shantel Aris, Club Vita**

"You see a trend where those with a higher education adopt healthier lifestyles and have improved access to health care. Those are some of the drivers that could explain the different outcomes for the same diseases between different social groups."

Another intriguing aspect of the CIA paper is that spending on healthcare may have a bigger longer term impact on improving life expectancy than directly increasing healthcare funding.

"Improved education is a preventive measure – possibly suggesting that increased spending on schools might, to some degree, be a better expenditure than increasing spending on health care, especially high-tech and expensive health care.

"Certainly, it appears that increases in education can double as investments in long-term health," said the CIA report.

A US study mentioned in the CIA report compared the effect of Americans achieving a college degree with advances made in biomedicine between 1996 and 2002.

According to the US study, more lives would have been extended from the increase in education than from the medical advances.

There are further potential longevity-linked benefits from increased education spending.

Statistics Canada looked at the relationship between income and education on life expectancy as well as on health adjusted life expectancy and found that not only did individuals with higher levels of education live longer, they also had more years of good health than lower education groups.

"Higher income leads to a longer life in good health. Lower income leads to a longer end of life period in poor health. More income or more wealth provides the means for better health care and better lifestyle, both of which can lead to better longevity," said the report.

Causation and correlation are, of course, two different things.

And while the current research into the relationship between education and longevity suggests that wealth may be superseded as the primary driver of life expectancy calculations, Aris says that it is not clear whether the data indicates causation or correlation.

"To say there is a direct cause-effect relationship between education and longevity is a stretch based on the research studies explored in the original literature review. However, while education may not cause longevity directly, it drives longevity through its connection to better employment, income generation and information gathering.

"Higher education not only leads to longer life, but it also leads to longer life in good health. Given this benefit of higher educational attainment, further research on how investment in education can lead to a healthier society is a good next step."

Secondary Life Markets Conference

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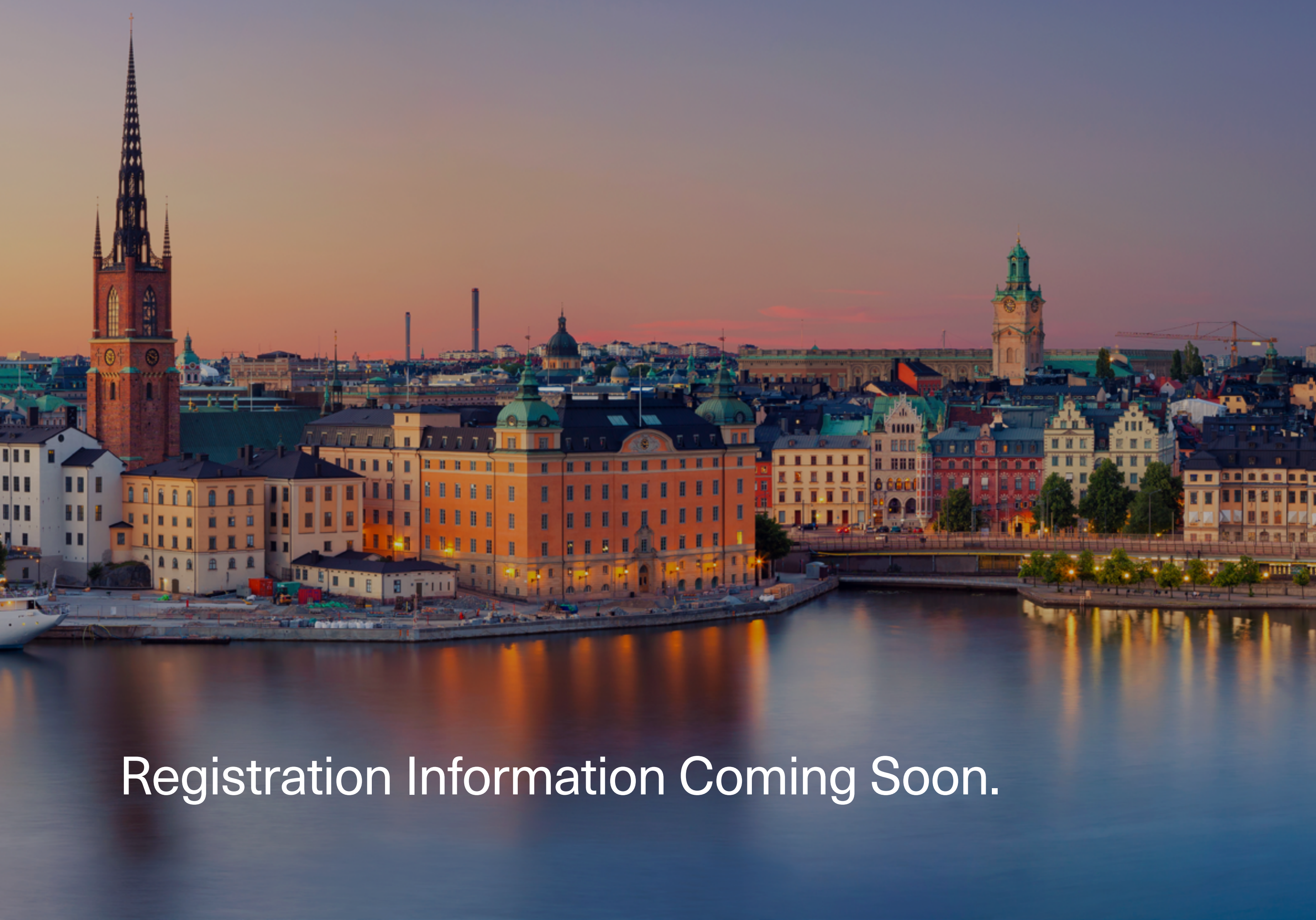

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Do Life Settlement Statutes Create Private Rights of Action?

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Lawyers whose clients participate in the life settlements industry devote significant time to ensuring that their clients strictly adhere to the requirements contained in life settlement laws. For life settlement providers, the rationale is that they do not want to put their licenses at risk and invite regulatory action, as well as not leaving open the possibility of challenges from sellers or their families who might regret having sold the policy. For the funds that purchase and aggregate life settlements, the first rationale is not applicable, but the risk that the provider failed to hew to the letter of the law, thus creating an opening to challenge the fund's clear title to the policy, is one which has incentivized funds to undertake careful diligence on the underlying purchase transaction to confirm that the providers they use to originate policies are compliant.

This article addresses the statutory framework pursuant to which an individual with "seller's remorse" can pursue claims for violations, technical or otherwise, of state life settlement statutes with the result that a transaction can be unwound or damages sought from the provider and/or ultimate fund/owner.

What is a Private Right of Action?

Before proceeding further, it is necessary to understand what is meant by a "private right" or "private cause" of action. A private right of action allows an individual or organization to bring a lawsuit in court based on an alleged violation of a law and to seek relief to remedy that alleged violation. If there is no private right of action, only the pertinent government actor (the US Department of Justice (DOJ), state attorneys general, state regulators, etc.) can initiate an action seeking to enforce a given statute, restricting who can sue under it. In the context of life settlements, if the pertinent state regulatory schema does not allow a private right of action, then a regulator such as an insurance department could bring an action to enforce a violation of a settlement law or regulation, but not an aggrieved seller or their family.

> "A private right of action can either be express or implied. Legislators create an express private right of action when the law explicitly defines that private individuals and groups can file lawsuits pertaining to the legislation at hand"

A private right of action can either be express or implied. Legislators create an express private right of action when the law explicitly defines that private individuals and groups can file lawsuits pertaining to the legislation at hand.

An implied private right of action is defined by courts rather than the legislators if the law itself is silent on the right of an individual to pursue an action under it. If the legislature does not explicitly spell out who or how individuals can bring lawsuits to enforce the law at hand, it is up to the court system to determine if the pertinent legislators intended for a non-governmental individual or entity to have the ability to pursue relief via the courts. For example, the US Supreme Court recognized that "an implied private right of action" exists under *Title VI* of the *Civil Rights Act of 1964* (prohibiting discrimination under any program receiving federal funds), leaving it "beyond dispute that private individuals may sue" to address allegations of intentional discrimination. *Barnes v. Gorman, 536 U.S. 181, 185 (2002).*

The NAIC and NCOIL Model Acts

Because life settlements are regulated on a state-by-state basis, whether life settlement statutes create a private right of action must be looked at in the context of each state's life settlement statute and the pertinent legislature's intent in enacting it. There are two model acts setting forth a framework for life settlement regulation, The Nation Association of Insurance Commissioners (NAIC) Viatical Settlements Model Act, and the National Conference of Insurance Legislators (NCOIL) Life Settlements Model Act (each, a 'Model

“Assuming a state legislature has adopted one of the Model Acts largely verbatim, it seems likely that such law does grant an explicit private right of action by individuals harmed by violations ”

Act’). Because almost all state life settlement regulation is based, in greater or lesser part, on one of the Model Acts, it is worthwhile to see whether this issue is addressed therein. In fact, each of the Model Acts contains language that would appear to create an explicit private right of action by individuals harmed by a violation of such act.

The NAIC Model Act contains the following language:

Section 15 B. “Any person damaged by the acts of a person in violation of this Act may bring a civil action against the person committing the violation in a court of competent jurisdiction.”

And, the NCOIL Model Act provider as follows:

Section 15 B. “Any Person damaged by the acts of another Person in violation of this Act or any rule or regulation implementing this Act, may bring a civil action for damages against the Person committing the violation in a court of competent jurisdiction.”

While, as discussed below, it is not without doubt, the language in these two Model Acts would seem to be an explicit manifestation that “any person” and not just a regulator, can bring an action to seek redress for a violation of the law. Hence, assuming a state legislature has adopted one of the Model Acts largely verbatim, it seems likely that such law does grant an explicit private right of action by individuals harmed by violations thereof.

State Laws

Regulation of the life settlements market is, perhaps, most consistent in its inconsistency. When the laws of the twenty-six most populous US states that regulate life settlements are reviewed, eighteen states have adopted some form of the language from the NAIC or NCOIL Model Act noted above[1], while eight have not.[2]

The fact that neither California’s nor Texas’ settlement law contains the language explicitly permitting a private right of action is remarkable given that they are the two most populous states in the country, and it would be fair to wonder if a court might read an implicit right of action into the statute. As it turns out, the answer is no.

California

In the case of *KKMB v. Khader, 2018 WL 6012225 (C.D. California 2018)*, at issue was a dispute regarding a policy in the amount of $5,000,000 taken out on the life of Noura Shoubash. The Plaintiff alleged that Jason Boutrous, Shoubash’s physician, intentionally gave Shoubash a false diagnosis of Chondrosarcoma and advanced coronary artery disease in order to shorten her life expectancy. The plaintiff purchased the Policy, relying on allegedly false medical records and life expectancy estimates.

There were a number of arguments made by the parties, but most pertinent for this discussion was the defendant’s assertion that the claim for “fraudulent life settlement acts” in violation of California Insurance Code §§ 10113 et seq. should be dismissed because there is no private right of action under California’s life settlement statute.

The court initially noted that there did not appear to be any precedent directly addressing whether a private cause of action exists to challenge a fraudulent life settlement act under the *California Insurance Code §§ 10113, et al.* (the California Act). It then set out the analytical framework for determining if a statute creates as private of action under the California Act. The court stated that the first step is to look at the language of the statute itself to see if there is a clear indication of an explicit private right of action. If not, then the legislative intent behind the statute must be reviewed to determine if the “[l]egislature has ‘manifested an intent to create such a private cause of action’ under the statute.” *Khader, 2018 WL 6012225 at *7 (quoting, Lu v. Hawaiian Gardens Casino, Inc., 50 Cal. 4th 592, 596 (2010))*.

> **"The court stated that the first step is to look at the language of the statute itself to see if there is a clear indication of an explicit private right of action. If not, then the legislative intent behind the statute must be reviewed"**

In support of its position that there was an explicit private right of action, the plaintiff cited two provisions of the California Act. First, the requirements that contracts and applications for life settlements must "contain the following statement or a substantially similar statement: 'Any person who knowingly presents false information in an application for insurance or for a life settlement contract may be subject to criminal or civil liability.'" *Cal. Ins. Code § 10113.3(t).* Second, the plaintiff referenced one of the enforcement provisions of the Act: "The commissioner may, after notice and a hearing at which it is determined that a licensee has violated this section or Section 10113.3 or any order issued pursuant to this section, order the licensee to pay a monetary penalty of up to ten thousand dollars ($10,000), which may be recovered in a civil action." *Cal. Ins. Code § 10113.2(n).*

The Court did not find either of these two provisions from the Act persuasive. It noted that the first statement recognizes the potential for civil liability, but fails to describe the mechanism for the liability, and whether an individual is entitled to an action to seek this redress, or if it was the province of the insurance commissioner. Id. The court found the second statement even less persuasive noting that, "if anything, [it] cuts against Plaintiff's argument in that it gives the commissioner authority to recover a monetary penalty against a licensee in a civil action; it says nothing about a private action by an aggrieved party." *Id.*

Not finding a specific right to a private action in the plain language of the statute, the court then determined that it had to examine the California Act's legislative history to seek evidence of the legislature's intent. In this inquiry, the Court noted "that the legislature seemed focused on creating a "regulatory framework," including the establishment of licensing requirements for those operating in the industry. [citation omitted]. The Bill Analyses do not mention private civil actions." *Id. at *8.*

Ultimately, the Khader court dismissed the claims asserted under the Act, concluding that "[i]n light of (1) the lack of cases establishing a private right of action, (2) a dearth of guidance on a seemingly silent legislative history, and (3) the equivocal nature of the statutory language, the Court is skeptical that the California legislature intended to create a private right of action to enforce *California Insurance Code § 10113.1 et seq." Id.*

Texas

Utilizing essentially the same analysis as the Khader court, the court in *Brighthouse Life Insurance Company v. Daboub, 577. F. Supp.3d 504 (N.D.TX 2021)*, reached a similar conclusion.

The issue came before the court in the context of a Motion to Dismiss Crossclaims filed by Cross-Defendant Coventry First, LLC. The claim against Coventry First alleged it and Wells Fargo violated the Texas Life Settlements Act (the Texas Act) by engaging in fraudulent life settlement acts, prohibited practices, and failing to provide disclosures required under *§§ 1111A.012, .014*, and *.017* of the Texas Act.

Coventry First and Wells Fargo both argued that the Texas Act does not provide a private right of action. The Daboub court noted that, "[u]nder Texas law, a statute creates a private cause of action "only when a legislative intent to do so appears in the statute as written." Daboub, 577 F.Supp. at 525 (citing *Brown v. De La Cruz, 156 S.W.3d 560, 567 (Tex. 2004)*). In granting the motion to dismiss, the court looked at other, non-life settlement, provisions of the Texas Insurance Code that do expressly grant a private of action, and then concluded "[t]he Texas Life Settlements Act does not contain a private right of action. See Tex. Ins. Code §§ 1111a.001–.026. At most, the statute provides that the Texas Insurance Commissioner may seek civil remedies of injunctions or cease and desist orders to address violations of the Act. Id. § 1111a.023." *Id.*

Other Cases

There is very little case law that specifically addresses situations in which a private action was found, explicitly or implicitly, under a life settlement

> **"There is very little case law that specifically addresses situations in which a private action was found, explicitly or implicitly, under a life settlement statute"**

statute. Although not specifically discussed, in the case *Consolidated Wealth Management, LLC v. Short, 414 F.Supp.3d 1011 (S.D. Tex. 2019)* it is clear the court, applying West Virginia law, did believe that a private right of action existed.

The court was presented with the following facts: In January 2014, James Short, a resident of West Virginia, entered into a Senior Facilitation Agreement (SFA) with an individual employee of Montage Financial Group (Montage). Montage played no role in the transaction with Mr. Short and was not a party to the SFA. Under the terms of the SFA, Mr. Short agreed to assign his interest interests in the policy for a payment of $25,016. Three days after entering the SFA with Mr. Short, the individual assigned his entire interest in the policy to Consolidated Wealth Management (CWM) for a payment of $37,700.

When Mr. Short passed away several years later, Mrs. Short and CWM made competing claims to the death benefit. As a result, the carrier filed an interpleader action and deposited the death benefit with the court.

Mrs. Short argued that the sale of her husband's policy violated West Virginia's viatical settlement law, and was, therefore, unlawful and void.[3] Whereas, CWM argued that under the "natural person" exemption in West Virginia's law, the individual who purchased the policy was not a "viatical settlement provider" when he entered into the SFA and therefore the SFA was not a "viatical settlement contract" under West Virginia law.

The Court did not discuss whether a private right of action was created under West Virgnia's Viatical Settlement Act,[4] but ultimately the court rejected CWM's arguments finding that the natural person exemption was not applicable under the facts in front of it and concluded that the sale of the policy violated the West Virginia viatical settlements act. As a result, the court effectively unwound the sale transaction and awarded the entire death benefit to Mrs. Short. Short, 414 F.Supp.3d at 1019.

An example of a case in which a court did not recognize a private right of action for a claim even where the state's life settlement did contain the pertinent language from the NAIC Model Act is *Southwestern Life Ins. Group v. Morehead, 245 Fed.Appx. 304 (4th Cir. 2007).* Here, the court was presented with a situation in which the Morehead's, rather than allow the policy on Mr. Morehead's life to lapse, engaged the Medical Escrow Society, a viatical settlement broker, which solicited bids to sell the policy for cash to an investor. Ultimately, the Robin Hood Group made the Morehead's an offer of $21,000 for the sale of the policy. After Mr. Morehead passed, Ms. Morehead filed a competing claim for the death benefit, which prompted the carrier to seek a declaratory judgment. After a bench trial, the court declared that the ultimate purchaser of the policy was the rightful owner of the death benefit.

Ms. Morehead appealed to the Fourth Circuit Court of appeals, which found: 1) that the offer by Robin Hood was the highest offer made by any viatical company for the sale of the policy; and 2) the Morehead's decided to sell the policy, and executed a purchase and sale agreement with Robin Hood; 3) the viatical settlement was fully and satisfactorily performed as contemplated by all parties; and 4) neither of the Morehead's complained about the terms of the transaction prior to the institution of the litigation.

Looking at the facts as determined by the trial court, the appeals court concluded that "[a]t all times relevant to the viatical settlement transaction, neither Robin Hood nor [the management company] were licensed to conduct business in North Carolina as viatical settlement providers pursuant to N.C. Gen.Stat. § 58-58-210(a) (2002) Also, Robin Hood failed to provide Mr. Morehead with a brochure describing the process of viatical settlements as required by N.C. Gen.Stat. § 58-58-245(a)(8), and failed to use contracts in execution of the viatical settlement that had been approved by the Commissioner of Insurance, as required by N.C. Gen.Stat. § 58-58-220." *Morehead, 245 Fed.Appx at 306*.

"The court presented the question in front of it as, "whether, under North Carolina law, a party to a fully executed contract may rescind it on the basis of the other contracting party's failure to comply with licensing and similar regulatory statutes, which statutes do not expressly create such a private right of action"

The court presented the question in front of it as, "whether, under North Carolina law, a party to a fully executed contract may rescind it on the basis of the other contracting party's failure to comply with licensing and similar regulatory statutes, which statutes do not expressly create such a private right of action." Morehead, 245 Fed.Appx. at 306 (emphasis added). After considering the facts and the law, the Fourth Circuit concluded that "North Carolina case law clearly and directly answers the posited question in the negative." *Id.* (citing *Hawkins v. Holland, 97 N.C.App. 291, 388 S.E.2d 221, 223 (1990)*).

In light of the provisions of *N.C.G.S.A. § 58-58-290(b)*, "Any person damaged by the acts of a person in violation of this Part may bring a civil action against the person committing the violation in a court of competent jurisdiction," one might think the court would have reached the opposite conclusion, and determine that a private right of action did exist under North Carolina law in this instance.

To reach its conclusion, rather than focus on the general question of whether a private right of action exists under the North Carolina Settlements Act, the court focused instead on the specific claim made by Mrs. Morehead, which the court characterized as, "attempting to recover moneys still owing to them under the tainted agreement...Morehead is trying to recover back the consideration she and her late husband voluntarily parted with as part of their performance under the Viatical Settlement Agreement, after receiving the full benefit of their bargain." *Id.*

Because of the nature of the claim asserted by Ms. Morehead, the court determined that notwithstanding that "the relevant regulatory enactment provides for ample penalties and enforcement mechanisms, that "not one of [those remedies] is a private right of action for annulment and avoidance of a concluded transaction...In sum, we conclude that appellees' technical violations of North Carolina's Viatical Settlement Act neither entitle Morehead to unwind the viatical transaction after it has been fully executed and satisfactorily performed, nor give rise to a claim at law where she can prove no actual injury." *Id. at 307*.

Conclusion

While there is a paucity of case law directly addressing the issue, what precedent there is suggests that courts are more likely to find a private right of action exists under a life settlements statute where language, such as that contained in the Model Acts, explicitly permits "any person" to seek redress for a violation of the act. As shown by the Morehead decision, however, even when the pertinent language is contained in the statute, the plaintiff still must articulate a claim that is sufficiently specific that it falls within a violation of the statute that has a direct connection to the injury alleged to have been suffered.

In sum, in light of the distinct possibility of that an aggrieved seller could seek to unwind a sale transaction on the basis of a violation of the underlying statute, it is prudent that the funds that aggregate life settlements continue to insist that the providers they use strictly follow the provisions of the pertinent life settlements law, or potentially suffer the consequences for their failure to do so.

Any views expressed in this article are those of the author(s) and do not necessarily reflect the views of Life Risk News or its publisher, the European Life Settlement Association.

[1]By population: FL: (F.S.A. § 626.9927(3)); NY: (NY INS § 7816(e)); PA: (40 P.S. § 626.12(b)); IL: (25 ILCS § 701(b)); OH: (O.R.C. § 3916(B); GA: (O.C.G.A. § 33-59-15(b)); NC: (N.C.G.S.A. § 58-58-290(b)); NJ: (N.J.S.A. § 17B:308-13(b)); VA: (V.C.A. § 38.2-6012(A)); AZ: (A.R.S. § 20-3214(B)); TN: (T.C.A. § 56-50-115(b)); MA: (M.G.L.A. 175 § 223C(b); WI: (WI. ST. § 63299(18)); CO: (C.R.S.A. § 10-7-613(2)); LA: (L.R.S. § 22:198(8)); KY: (K.R.S. § 304-15-709)); CT: (C.G.S.A. § 38a-465k(b); IA: (I.C.A. 508E.16(s)).

[2]California; Texas; Washington; Indiana; Maryland; Minnesota; Oregon; Utah

[3]Mrs. Short argued in the alternative that the SFA did not cover replacement policies, and that the policy at issue replaced the one sold. The court also found in favor of Mrs. Short on this argument.

[4]This may be because court assume under § 33-13C-15(b) of the West Virginia Act, which states, "Any person damaged by the acts of a person in violation of this article may bring a civil action against the person committing the violation in a court of competent jurisdiction," that such a private right of action existed.

Innovating Beyond Cardiology: Discoveries in Acquired Chronic Muscle Spasm and Resulting Chronic Pain

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Medical Director
Fasano Underwirting

One of the most common ills of mankind is chronic pain. In some cases, the associated chronic muscle spasm is known to be the culprit.

However, in some cases there is not an obvious connection between the pain and the chronic muscle spasm that was responsible for the chronic pain. In any case, treatment of chronic pain requires knowledge of its source. If chronic muscle spasm is indeed the source, then it is necessary to have a diagnostic tool to identify the muscle or muscles in chronic spasm.

Ultimately, a treatment that specifically targets chronic muscle spasm is then needed to successfully treat the chronic pain.

What is not generally known is that muscles in chronic spasm are very electrically active. Use of an EMG device, that is essentially an EKG for muscle, is all that is needed to identify a muscle in chronic spasm. Unlike EKG devices, a needle must be inserted into the muscle to record the electrical activity.

Surface recordings of EMG are possible but only tell of generalised electrical activity and do not identify specific muscles. When treatment of muscles in chronic spasm involves an injection technique, not only the specific muscle but all segments of the muscle demonstrating enhanced electrical activity need to be identified.

Successful treatment by injection will result in elimination of the enhanced electrical activity. Medications such as Botox have a slow onset and the results peak at about two weeks. Medication combinations such as Lidocaine/Phenoxybenzamine have an initial immediate effect of resolution of the enhanced electrical activity and a secondary effect that can last for months.

> “When Lidocaine is utilised, it is possible to map the entire muscle and verify that all parts of the muscle that demonstrated enhanced electrical activity have been treated and adequately suppressed”

When Lidocaine is utilised, it is possible to map the entire muscle and verify that all parts of the muscle that demonstrated enhanced electrical activity have been treated and adequately suppressed.

Getting back to basics, muscles in chronic spasm can cause pain at a distance. One of the most obvious examples is a condition called IT band syndrome which causes knee pain. The muscle that is responsible is the tensor fascia lata, which is a relatively small muscle in the upper anterior thigh.

Resolution of spasm of that muscle results in near immediate relief of the knee pain. On the other hand, pain resulting from some muscles in chronic spasm results in local pain such as in shin splints that are caused by muscles in the anterior leg below the knee.

There has been significant controversy regarding the origin of the enhanced electrical activity in various states of muscle activity. However, relative to identification and treatment, the exact origin is of little consequence.

Prolonged elimination of the enhanced electrical activity, that is identified in the scientific literature as Spontaneous Electrical Activity or SEA, results in resolution of the chronic spasm and sustained relief of chronic pain if it was secondary to the chronic muscle spasm.

If it can be identified that a muscle is in chronic spasm and appears to be the source of chronic pain, then treatment of the chronic muscle spasm and not suppression of the chronic pain with pain medications such as opioids should be focus of treatment. A treatment protocol named Coletti Method

Emg ChemoDenervation (CMECD) has been shown in somewhat limited but statistically significant clinical setting to relieve chronic pain by prolonged suppression of the SEA.

Fortunately, when this protocol is utilised, the SEA does not return, nor does the muscle spasm or the resulting chronic pain.

The question remains: how does the muscle go into chronic spasm in the first place?

What I have postulated is that what is seen in cardiac muscle during a state of contraction is that the contraction of the muscle limits the blood supply that is needed for relaxation of the muscle. It turns out that the muscle needs more blood supply and therefore energy to relax than to contract. It is like a mouse trap, much more effort to set the trap than to set it off.

Normally, a muscle in spasm does not stay in spasm long enough to limit the energy supply to relax. But if an acquired muscle spasm from an overuse injury is not attended to, then the spasm sets off a chain of events that leads not only to chronic spasm but a degeneration of the muscle with loss of mitochondria and muscle fibers.

> "Recovery requires significant time with unimpeded blood supply for new mitochondria to emerge and repair of the muscle fibres. Short-term relief of chronic muscle spasm does not suffice and thus a therapy that has a long-term solution is necessary"

Recovery requires significant time with unimpeded blood supply for new mitochondria to emerge and repair of the muscle fibres. Short-term relief of chronic muscle spasm does not suffice and thus a therapy that has a long-term solution is necessary.

Alternatively, a therapy performed on a daily basis for months may be sufficient. It is likely that there are a number of therapies that may suffice but will require very frequent applications for at least two-three months depending upon the degree of injury and loss of cellular elements resulting from the prolonged ischemia, ie: poor blood supply.

I had done research during my cardiology followship that unfortunately was not reported. The findings were that the blood flow during cardiac contraction that is known to be less than during cardiac relaxation can be altered by medications that limit the force of cardiac contraction.

At a certain point of suppression of cardiac contraction, the predominant cardiac blood supply to the cardiac tissue is predominantly in a state of cardiac contraction. This demonstrates that muscle contraction limits the blood supply.

Now to the question of the SEA. Where did that come from?

Let's first look at the cardiac situation. When there is poor blood supply, we get cardiac arrhythmias. The skeletal muscle is no different. The technical issues are a matter of future research, but the end result is the SEA not only identifies the presence of chronic muscle spasm but is actually the ongoing cause of the chronic spasm. The SEA is like an electrical stimulator, constantly depolarising the skeletal muscle and keeping it in a state of constant contraction, limiting its blood supply and resulting in an unending state of contraction. I call it the black hole of muscle pathophysiology.

So, what does this newfound knowledge do for us? To start with, it provides us with a method of identifying muscle in true chronic spasm. With that knowledge, we are able to seek alternative treatments to resolve the chronic spasm and we have the means to verify success or failure of those treatments.

The CMECE procedure is one proven way to treat chronic muscle spasm and resultant chronic pain secondary to chronic muscles spasm. It can be performed by any medical professional that is allowed to do intramuscular injections and has minimal risk. Cost is also relatively minimal with a one-time procedure, all that is necessary, likely to be under $500 for all costs incurred.

Other procedures should be able to be developed given the understanding of the cause of chronic muscle spasm and may not require injection of any medication. Hopefully, these treatments will emerge. In the meantime, the CMECD procedure is available to be performed worldwide and holds the opportunity to relieve chronic pain in a large portion of those with chronic pain.

Q&A

John Kiff
CEO, Kiffmeister Consulting

The remarkable growth in the pension risk transfer market in the past few years has caught the eye of the trade media, investors – and regulators. But the transferring of longevity risk from pension funds was discussed long before it became a 'thing'. Greg Winterton spoke to John Kiff, formerly of the International Monetary Fund, and now an independent consultant, to get his views on how the industry has evolved since he first started discussing it in the mid-2000s.

GW: John, you were discussing the longevity risk transfer market back in 2006 when you worked at the IMF. Go back to that time. Did you ever think that the market would be as large and active as it is now?

JK: I thought it would be larger and more active than it is now. In particular, I thought that by now there would be more longevity risk transfer to capital markets, as opposed to those just between (re)insurers. I was encouraged by the 2012 €12 billion longevity swap between Dutch insurer Aegon and Deutsche Bank that used standard ISDA documentation and was targeted specifically at institutional investors, and the similar 2013 Aegon €1.4 billion deal structured by Société Générale. All payments were based on longevity indices based on publicly available data, rather than the actual longevity experience of Aegon's annuity book. And the deals had 20-year maturities with close-out mechanisms that determined final payment. However, although there continue to be large transfers into (re)insurance markets, there haven't been any further attempts to transfer longevity risk to capital markets.

GW: You co-authored a paper, The Limits of Market-Based Risk Transfer and Implications for Managing Systemic Risks, in 2006. What's your view on the regulatory environment in terms of how, and/or if, it has evolved to support the space?

JK: I don't think much has changed at all. In most jurisdictions, only traditional reinsurance transactions, where cash flows are based on the cedant's actual longevity experience, may provide a primary longevity risk insurer with regulatory relief. This makes risk transfers based on longevity indices, like the Aegon transactions, unlikely to get traction, at least in the current regulatory regime. There will need to be something specific that happens for capital market participation in longevity risk transfer to really get moving.

GW: The International Monetary Fund staff called attention to concentration risk in UK pension scheme buy-out markets in their 2024 Article IV mission concluding statement. Where on the spectrum of concern are we in terms of this pile of longevity risk accumulating at the reinsurance level?

JK: Concentration risk is certainly something that bears watching. Since 2009, about 80% of completed UK longevity risk transactions have been concentrated in just four (re)insurers. However, this is not an extraordinary degree of concentration in wholesale capital markets, for example over-the-counter derivatives markets. Nevertheless, it takes us back to a need for the development of ways for (re)insurers to share these risks, ideally outside the (re)insurance sector. And as we said in that 2006 paper, there are capital markets players that take longer-term investment positions that would make ideal counterparties for such transfers, like private equity firms and sovereign wealth funds.

Continued on next page...

GW: What's something that you personally would like to see change in the longevity risk transfer market, and why?

JK: I would like to see longevity risk become tradeable – which is what I thought was going to happen when I was looking at this space nearly twenty years ago – but the obstacles seem to be manifold. (Re)insurers get little to no regulatory relief for risk transfers outside the (re) insurance industry, maybe there's simply no capital markets appetite for it, or the right transfer instrument design hasn't been discovered/developed yet.

GW: Finally, John: Looking ahead five years or so. What do you think – hope – the longevity risk transfer market will look like?

JK: I suspect, sadly, that things won't be much different at all. There will still be plenty of pension scheme to insurance company transfers in the bulk annuity market, except that maybe the appetite for these deals will begin to peter out somewhat. As I've said, there doesn't seem to be much in the way of regulatory action to support the involvement of the capital markets and so I think that the status quo will remain. I hope I'm wrong.

Solid Outlook for Growing Asset-Intensive Life ILS Transaction Market

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Life Risk News

The rising interest rate environment of the past two and a half years has had the impact of reining in deal activity in some life ILS trades, such as commission financing or value-in-force (VIF) deals, because rising rates make these transactions more expensive for life insurers, thus dampening demand, as well as being challenged by rate-driven lapsation.

That is not the case in the asset-intensive corner of the life ILS market, however. These deals – whereby the investor(s) assume both the liability and asset risk associated with a block of insurance-linked policies, like annuities, for example – benefit from a rising interest rate environment.

"In asset-intensive deals, you are primarily investing in the spread between asset and liability performance. On the liabilities side of the trade, your cost of funding is largely fixed at the time of pricing. But on the asset side, as rates rise, you're earning more as you reinvest cash flows, thus benefiting from a wider spread," says Gokul Sudarsana, Chief Investment Officer – Life Insurance at Hudson Structured Capital Management Ltd. (d/b/a HSCM Bermuda).

**"In asset-intensive deals, you are primarily investing in the spread between asset and liability performance. On the liabilities side of the trade, your cost of funding is largely fixed at the time of pricing. But on the asset side, as rates rise, you're earning more as you reinvest cash flows, thus benefiting from a wider spread"
- Gokul Sudarsana, Hudson Structured Capital Management Ltd.**

"While some liabilities may experience higher lapses as rates rise, this is offset by the asset side," Sudarsana added.

The outlook for interest rates in the short term is uncertain. If rates start coming down again, it follows, other things being equal, that commission financing and VIF transactions would become more interesting to life insurers, given both the cost of capital and the stability of collateral.

But falling rates doesn't mean that asset-intensive trades would see a reduction in the spread. Similar to how many defined-benefit pension plans are buying interest rate hedges to maintain their newly fully-funded status, insurers take steps to create and preserve value through the economic cycle.

"Unlike some trades in the life space, asset-intensive deals give you more flexibility in managing both sides of the balance sheet. Generally, the capital markets risk is muted to begin with as you are matching stable, predictable liabilities with all-weather, investment grade assets. But it is important to have a good feel for where we are in the prevailing interest rate cycle, which will inform pricing, hedging, and rebalancing decisions to tactically optimize the business," said Sudarsana.

In March, industry group LIMRA published data suggesting that annuity sales in the US in 2023 came in at their highest ever total, $385.4bn. Then in April, it followed that up with a press release stating that the first quarter of this year was the best ever quarter at $113.5bn.

Annuities are a good example of products that work well as the basis for an asset-intensive life ILS trade as many of them have a specific term, meaning that the liabilities are fixed and known. And while the apparent boom in annuity sales has motivated a large number of asset managers to rush in and try to take a slice of this growing pie, the moats in the space are formidable.

First and foremost, certain expertise is required to execute these deals effectively.

"The actual underwriting of the risk requires significant actuarial, investment, and regulatory expertise. The assets and liabilities are not necessarily going to run off the way you model them, and the ongoing operational and governance requirements are complex, so insurers need a partner that has the requisite expertise and credibility," said Sudarsana.

Additionally, what also impedes the ability of others to enter the space is the good, old-fashioned network.

"These deals are often bilateral, and you need relationships at the executive level at life insurance companies, which take years to develop," Sudarsana added.

"Asset-intensive trades are as much strategic partnerships as they are transactions. The whole project, from the ideation stage through to completion, regularly takes well over a year."

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Finally, asset-intensive trades are often hundreds of millions of dollars – sometimes, billions of dollars – in size, which requires access to large pools of long-term capital. That requires thoughtful structuring to fit fund mandates and robust institutional distribution capabilities.

Asset-intensive deals aren't all about annuity-backed business. In a low-rate environment, annuity-backed trades work well because buyers need cheaper liabilities because their asset returns are lower. But in a higher rate regime, buyers can pay more because their returns will be higher, which brings into play liabilities that are higher cost and more complex, like certain life insurance products. The pension risk transfer market, for example, has, in the past couple of years, seen significant growth in activity as defined benefit pension schemes generally have become fully funded; both the UK and the US market delivered approximately £50bn and $50bn of transactions value in 2023.

Good news for those in the space, indeed. And more is on the way – at current interest rate levels, activity in the asset intensive space should keep growing.

"There is a need for capital for life insurers globally to support the strong demand for savings, retirement, and life insurance products. It's a virtuous cycle; the growth exists because rising rates make annuities more attractive to consumers, and so more capital is needed to support this demand," said Sudarsana.

"We participate in in-force block transactions that provide capital relief to insurers so they can redeploy into new business, as well as supporting new business flows.

"The growth at the front end is driving the demand for capital which is driving the opportunity for the capital markets to participate in the risk. These transactions are actually well insulated from capital markets risk because of strong credit quality and tight asset-liability management. Consequently, there is growing interest from long term institutional capital, like pension plans, sovereign wealth funds, etc. that value the stable, uncorrelated cash flow profile that asset-intensive life ILS transactions can provide," he added.

The views expressed in this article are those of the individuals

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