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UK Consumer Duty Barely Impacting an Equity Release Market Desperate for Interest Rates to Fall

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Publisher
ELSA
97 Fable
261c City Road
London EC1V 1AP

+44 (0) 203 490 0271
admin@elsa-sls.org

Editorial
Managing Editor
Chris Wells
chris@elsa-sls.org

Contributing Editor
Greg Winterton
greg@liferisk.news

Contributing Editor
Aaron Woolner
aaron@liferisk.news

Editorial Assistant
Emilie Horne
emilie@liferisk.news

Editorial Enquiries
editor@liferisk.news

Design & Layout
Kieran Reilly
hello@kieranreilly.com

Editor's Letter, Volume 3, Issue 07, July 2024

Chris Wells
Managing Editor
Life Risk News

It's now a year since UK regulator the Financial Conduct Authority brought in its new Consumer Duty, a regulation requiring all financial services firms to 'act to deliver good outcomes for retail customers' for all new (and now, closed) product offerings. While there are fundamental benefits of this to the country's equity release market, it's not a needle mover in terms of greasing the wheels of supply. *Greg Winterton* spoke to **Ben Grainger**, Partner at **EY**, for his thoughts on the topic in *UK Consumer Duty Barely Impacting an Equity Release Market Desperate for Interest Rates to Fall*.

Cardiovascular disease is the world's leading cause of death, accounting for nearly 18 million lives annually, or 33% of the total, well ahead of cancers which are the second most common cause. When it comes to early onset CVD specifically, recent research by **BMC Public Health** based on data extracted from China's **Kailuan Study** shows an interesting disparity, as *Aaron Woolner* explains in *Research Demonstrates Gender Differences in Early Onset Heart Disease*.

Life settlement asset managers pay significant sums of money to keep a life insurance policy in force until the insured dies. These sums can, and very often do, stretch to millions of dollars from when they assume ownership of a policy to when it matures. But what happens if a policy they own is declared void ab initio because of a lack of insurable interest? *Greg Winterton* spoke to **Lee A. Pepper**, Partner at **ArentFox Schiff**, to learn about the impact of the recent Delaware Supreme Court ruling in Seck on the life settlement market in *Seck Affirmation Keeps Return of Premium Waters Muddy for Life Settlement Market*.

The **US Department of Labor** has concluded its review of the regulatory framework for the pension risk transfer market and decided not to take any action at the moment, but it has left the door open for future rule changes. *Aaron Woolner* takes a closer look at the DoL's recent report to the *US Congress in US Authorities Leave Pension Risk Transfer Rules Untouched*.

With around $45bn of transactions, 2023 was the second busiest year on record for PRT deals in the US, and that pace was sustained during the first quarter of 2024. But many of the deals so far have been for plans that only feature retirees. By contrast, most of the plans now coming to market have large numbers of deferred lives – employees or former employees yet to begin taking their benefits. This adds significant uncertainty for insurers, as **Caitlynn Greenfield**, Director, Insurance Consulting and Technology, **Justin Bevan**, Associate Director, Insurance Consulting and Technology, and **Stan Roberts**, Associate Director, Insurance Consulting and Technology at **WTW** explain in *Making Sense of Pension Risk Transfer Deals for Deferred Lives*, a guest article this month.

Back in April this year, the Florida Fifth Judicial Circuit Court delivered some good news to the life settlement industry. **Brian Casey**, Partner at **Locke Lord**, explains more in *Premiums Paid Offset Awarded to Investor in Florida Estate Recovery Case*, our second guest article this month.

Both LISA's and The Deal's annual life settlement provider analyses have now been published, so for our **Q&A** this month, *Greg Winterton* spoke to **Abacus Life** CEO **Jay Jackson** to get his thoughts on the current state of the life settlement landscape.

For senior living investors, the risk associated with investing in the space has typically been a real estate one – vacancy rates. Many investors and operators in the market don't focus nearly as much on longevity risk, however. *Greg Winterton* spoke to **Chris Conway**, Chief Development Officer at **ISC Services**, to get his thoughts on the benefits of longevity risk analysis for senior living investors in *Should Senior Living Investors Pay More Attention to Longevity Risk?*

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

UK Consumer Duty Barely Impacting an Equity Release Market Desperate for Interest Rates to Fall

Author:
Greg Winterton
Contributing Editor
Life Risk News

It is now a year since UK regulator the Financial Conduct Authority (FCA) brought in its new Consumer Duty (Duty), a regulation requiring all financial services firms to 'act to deliver good outcomes for retail customers' for all new product offerings. This month, the FCA closes the loop with the implementation of the duty for closed product offerings.

One of the markets that is impacted by the Duty is the country's equity release market (ERM). Participants ranging from independent financial advisors right through to the funders themselves (life insurers and pension funds, in the main) have had to get with the program, ensuring compliance at the beginning, middle and end of the customer journey.

Prior to the implementation of the Duty, one might have been forgiven for assuming that the ERM would be significantly impacted here. According to Ben Grainger, Partner at EY, however, a number of the principles of the Duty have already been in place in the ERM for some time.

> **"The Consumer Duty is an important formalisation of prioritising good outcomes for customers across the financial services sector. Looking specifically at the UK equity release market, the foundations for a lot of these practices were already in place prior to the implementation of the Duty"**
> **- Ben Garinger, EY**

"The Consumer Duty is an important formalisation of prioritising good outcomes for customers across the financial services sector. Looking specifically at the UK equity release market, the foundations for a lot of these practices were already in place prior to the implementation of the Duty," he said. "However, the Consumer Duty has introduced the need for firms to formalise and demonstrate how they are meeting its requirements. In this regard, there has still been work to do, such as firms formalising their value for money methodology."

One of the potential upsides of the Duty and the standards it mandates is in consumer perception. The 2023 Global Equity Release Survey, produced by EY and industry group the European Pensions and Property Asset Release Group (EPPARG) and published at the beginning of the year, cited customer perception as one of five main growth barriers, with 17% of survey respondents saying this was an impediment to the market kicking on.

Another question posed of the respondents was 'If you could change one thing about the equity release market in your country, what would it be?' with 'Improving customer perceptions' the joint most popular response in the resulting word cloud.

EY and EPPARG's survey was global, not UK-specific, but clearly, perception remains an issue, so arguably, anything that advances this would be welcomed by the industry.

But the 800lb gorilla in the room is still the prevailing interest rate environment.

The ERM in the UK is currently in something of a treading water mode. According to data published in April by industry group the Equity Release Council, new customers coming to the market have continued to fall quarter on quarter since Q3 2022, when nearly 14,000 Brits took the plunge; just 4,698 did so in the first quarter of this year. That decline is mitigated, to a certain extent, by the stability shown in the returning customer segment, which drove a 6% increase in drawdown activity in Q1.

The decline in new customer activity correlates highly with the upwards trajectory in interest rates in the UK, which began in late 2021. Correlation is not causation, but on the flip side, there is no smoke without fire.

Interest rates are, of course, one of the most significant influences of activity in the ERM; higher rates means that it's more expensive to buy a new mortgage and reduces the available loan amount for homeowners as well. But there is a level of anticipation that the corner might be turned sooner rather than later.

"New customer numbers are lower than last year with feedback from the market suggesting that older homeowners are adopting a more cautious approach to borrowing as there are hopes of interest rate reductions in the near future," said David Burrowes, Chair of the ERC, in a press release back in April.

> **“New customer numbers are lower than last year with feedback from the market suggesting that older homeowners are adopting a more cautious approach to borrowing as there are hopes of interest rate reductions in the near future”**
> **- David Burrowes, ERC**

Life insurers in the UK will be hoping that it does. There are very few assets available to invest in that have a duration as lengthy as a mortgage – and with a similar risk profile (a good one, incidentally). And these firms are awash with quite literally billons of pounds from their activities in the booming UK bulk purchase annuity market, all of which needs to find a home. Sadly, it’s not as if there are many other similar markets in which to park long-dated capital and even if there were, entering them would be a slow process.

“A logical step is to then look abroad to markets like Australia, Canada and some in continental Europe where there is an undersupply of funding, but many of these markets don’t have an established infrastructure to drive activity yet,” said Grainger.

“Also, while there are hurdles in the way of establishing markets, these are surmountable. It’s just that it takes insurance companies a long time to get happy investing in a new asset class. This needs to get to the top of the list before they are willing to dedicate the time to do that,” he added.

Which means that insurers are putting a good chunk of their bulk purchase annuity premiums into liquid fixed income. After all, what’s not to like about gilts at the moment, where you can get 4.37% on a 10-year, (comparatively) safe haven investment?

Until rates start to fall, it’s likely that the UK ERM will continue treading water. The Duty, while generally accepted as a positive development for the consumer, simply isn’t a significant factor in the supply of risk. But when rates do start to fall, and new customer activity starts to pick up, insurers will be poised to deploy capital.

“There is a significant gap in the UK equity release market in the sense that there is roughly $3bn of activity but more than £6bn of demand,” said Grainger.

“Strategic asset allocations haven’t changed – there will be a rebalancing when illiquid markets open up again, and, as one of the few long-dated assets available, equity release mortgages will be in high demand from insurers.”

Research Demonstrates Gender Differences in Early Onset Heart Disease

Author:
Aaron Woolner
Contributing Editor
Life Risk News

Cardiovascular disease (CVD) is the world's leading cause of death, accounting for nearly 18 million lives annually, or 33% of the total, well ahead of cancers which are the next highest cause of mortality (17%), according to Our World in Data.

The data are also clear that CVD impacts men and women in different ways, with an overall lower prevalence of coronary disease among women, who typically develop heart problems at older ages - the average age for a first heart attack in men is 65, compared with 72 for women, according to Harvard Medical School.

The picture was more opaque when it came to early onset CVD but recent research by BMC Public Health based on data extracted from China's Kailuan Study suggests that the older age pattern is repeated with premature heart disease.

"The study highlights gender disparities in all-cause mortality among individuals with early-onset CVD, with men experiencing a higher risk of mortality compared to women.

> **"Further research is needed to develop sex-specific interventions and strategies to reduce gender-related mortality disparities in early-onset CVD"**
> **- Qi Zhang, Tangshan Gongren Hospital**

"Further research is needed to develop sex-specific interventions and strategies to reduce gender-related mortality disparities in early-onset CVD," said the study, which was led by Qi Zhang from Tangshan Gongren Hospital's Department of Cardiology.

The Kailuan Study is an ongoing prospective cohort study which started in 2006 and uses data from a community linked to the Kailuan Group coal mining firm, which is based in Tangshan - a coastal city in the North East of China.

There are 11 hospitals providing health care for the Kailuan community and from June 2006 to October 2007, 101,510 participants (81,110 men and 20,400 women; 18–98 years of age) had built up a health record in those medical facilities.

"The study conducts biennial follow-up visits and makes annual checks on cardiovascular as well as all-cause mortality. These conditions enable us to analyse factors influencing mortality following early-onset cardiovascular events in different genders," said the report.

The team of researchers at Tangshan Gongren Hospital looked at data from 3,087 individuals who developed early onset CVD between June 2006 and December 31, 2020. Premature heart disease was defined as an event which occurred before the age of 55 for men and 65 for women.

Death information was gleaned from the Kailuan social insurance system which provides medical insurance to all the group's employees.

Men made up 1,984 (70.1%) of the study group and had an average age of 49.5 versus 57 for women. Age wasn't the only difference between the two groups, with men showing higher diastolic blood pressure and eGFR (glomerular filtration rate; kidney efficiency - a higher reading is better).

More men had received higher education than the female cohort of the study, and they also had higher rates of both drinking and smoking. Interestingly, while smoking was defined as inhaling a single cigarette a day for the previous year, the bar for classifying someone as a drinker was consuming 100ml of 50% proof alcohol a day – or roughly 35 units a week.

Women were more likely to suffer from diabetes and be prescribed antidiabetic medications than men.

The differences in health between the male and female populations in the study was reflected in the period following early onset CVD, with men receiving follow-up care for a median duration of 7.54 years, during which 276 deaths were recorded.

Women had a median follow-up period of 6.45 years, and 105 deaths were recorded during this time. The data showed that adjusting for covariates in the model, men displayed a significantly increased risk of all-cause mortality compared to females.

"Individuals with hemorrhagic strokes exhibited a lower proportion of antiplatelet agent use, and upon their exclusion, men with early-onset CVD continued to manifest a higher risk of all-cause mortality compared to females," the study said.

The study concluded that the primary outcome variable was all-cause mortality, with a higher incidence in men than women within the early onset CVD group but researchers said that there are multiple factors which cause this and that these vary by gender.

"Smoking and eGFR decline can increase the risk of all-cause mortality in females with early-onset CVD. While achieving blood glucose control and using antiplatelet drugs can reduce the risk of all-cause mortality in males with early-onset CVD," the study said.

> **"Smoking and eGFR decline can increase the risk of all-cause mortality in females with early-onset CVD. While achieving blood glucose control and using antiplatelet drugs can reduce the risk of all-cause mortality in males with early-onset CVD"**
> **- Tangshan Gongren Hospital**

The Tangshan Gongren Hospital research differed from previous findings on gender disparities in all-cause mortality among CVD patients. Previous studies in China and the United States found no gender differences, while Korean researchers concluded there was a higher mortality risk for young women than men.

"In contrast to previous research, our observation pertains to early-onset CVD patients, revealing for the first time that women have a lower risk of mortality than men within the early-onset CVD population," said the study.

The researchers said that while the underlying data set allowed for what they termed 'robust' observation of the relationship between early onset CVD and mortality, it also had a number of limitations.

The paramount issue was the homogenous nature of the Kailuan community which underpinned the study. Other research has shown a pronounced difference in CVD among people from different ethnic groups, such as a 2022 study based on UK Biobank data; a large-scale biomedical database and research resource containing anonymised genetic, lifestyle and health information, and biological samples.

After researchers from the US National Institute of Health crunched the Biobank data, they found that South Asian, but not black African or Caribbean individuals, had a higher risk of CVD compared to white Europeans. Critically the higher risk in South Asians was independent of sociodemographic, lifestyle, environmental, and clinical factors.

Researchers in the Kailuan CVD study explicitly acknowledged this weakness in their results and said that it meant their analysis was unable to account for population and ethnic diversity, and validation of its finding could require its replication across multiple cohorts in various regions.

Despite this weakness, the Kailuan researchers were confident enough in the results to suggest ways that health authorities could use the information about how premature heart disease occurs differently in men and women to structure more effective policy.

"In the early-onset CVD population, the risk of mortality is higher in males than in females. Therefore, future health assessments and explorations of risk factors for early-onset CVD might need to be gender-stratified to achieve maximum cost-effectiveness."

"Simultaneously, this emphasises the need for gender-specific evaluations in the future construction of health assessment systems and clinical guidelines for individuals with early-onset CVD," the study concluded.

Seck Affirmation Keeps Return of Premium Waters Muddy for Life Settlement Market

Author:
Greg Winterton
Contributing Editor
Life Risk News

Life settlement asset managers pay significant sums of money to keep a life insurance policy in force until the insured dies. These sums can, and very often do, stretch to millions of dollars from when they assume ownership of a policy to when it matures.

But what happens if a policy they own is declared void ab initio because of a lack of insurable interest?

Under Delaware law in the US, when the present owner acquires an insurance policy, they typically also acquire all right, title, and interest in the policy - including the right to recovery of prior premiums paid, even when those premiums were paid by a completely different entity.

So, in the event of a policy being declared void *ab initio*, is the current owner entitled to a return of the premiums they have paid themselves, either in full or in part? What about those paid by the prior owner? Or is it simply a case of 'tough luck'?

These questions were at issue in *Brighthouse Life Insurance Company v Geronta Funding*, a quite remarkable saga that came to a frustrating conclusion for the life settlement industry in May.

> **"The takeaway is that the framework from the 2022 Delaware Supreme Court Seck decision remains the same, and subject to the Delaware Supreme Court's 2023 decision known as DeBourbon and Frankel, an owner may be able to obtain return of premiums paid by prior owners of the policy if the party seeking return of premium can show that those prior owner(s) are less at fault than the insurance carrier"**
> **- Lee A. Pepper, ArentFox Schiff**

Back in the summer of 2007, a life insurance policy was issued for a certain Mansour Seck by Brighthouse. The policy value was $5m, and it eventually found its way to the secondary and then tertiary life settlement market.

Except that Mansour Seck didn't exist. This was a classic case of fraud, and the perpetrator, Pape Michael Seck, went to prison in 2011.

But the saga didn't end there. The policy in question became the subject of extensive litigation; the tertiary buyer, Geronta Funding, sought to recover the premiums that both it and EEA, the secondary market buyer, paid to Brighthouse.

Following a bench trial, the Delaware Superior Court in August 2021 held that Geronta was only able to recover the premiums that it had paid after April 2017, when it notified Brighthouse that it suspected that Mansour Seck was a fictitious individual.

Geronta appealed, and the case then went to the Delaware Supreme Court, which overruled the original Superior Court's opinion in August 2022 and established a fault-based approach to determine which party is entitled to the premiums paid on an insurance policy that is found void ab initio for lack of insurable interest.

Following remand to the Superior Court, Geronta Funding was awarded all of the premiums that it paid to Brighthouse on the policy, plus interest, not only those it paid after April 2017. However, Geronta was not awarded the premiums paid by the Seck policy's previous owner, EEA. Another appeal to the Delaware Supreme Court followed and in May of 2024, the Delaware Supreme Court affirmed the Superior Court's ruling.

"The takeaway is that the framework from the 2022 Delaware Supreme Court *Seck* decision remains the same, and subject to the Delaware Supreme Court's 2023 decision known as *DeBourbon and Frankel*, an owner may be able to obtain return of premiums paid by prior owners of the policy if the party seeking return of premium can show that those prior owner(s) are less at fault than the insurance carrier," said Lee A. Pepper, Partner at ArentFox Schiff.

For the life settlement industry, however, the waters remain somewhat muddy, and it is difficult for an investor to discern what premiums that it or prior owners paid for the policy would be subject to return if a policy is declared void *ab initio* under Delaware law, as return of premium is a fact-specific inquiry.

Leadenhall Capital declined to comment; representatives from Brighthouse and EEA had not responded to an offer to provide comment by press time.

US Authorities Leave Pension Risk Transfer Rules Untouched

Author:
Aaron Woolner
Contributing Editor
Life Risk News

The US Department of Labor (DOL) has concluded its review of the regulatory framework for the pension risk transfer (PRT) market and decided not to take any action at the moment, but it has left the door open for future rule changes.

At the end of June, the DOL's Employee Benefits Security Administration (EBSA) issued a report to Congress on the thirty year old Interpretive Bulletin 95-1 (IB 95-1) in which it said it was not 'prepared at this time to propose amendments'.

The EBSA report explicitly addressed concerns from some market participants that the greater use of illiquid investments, such as private debt, by non-traditional insurers (this group holds on average 50.3% of their portfolio in corporate bonds versus 64.1% at non-private equity backed firms) was risky.

> **"Some stakeholders attributed concerns about developments in these areas to private equity firms' increased involvement in the industry. They said that private equity-affiliated insurers tend to engage in riskier practices than traditional insurers. Stakeholders were also concerned that private equity firms do not have a long track record of managing life insurance obligations and may lack a commitment to policyholder interests"**
> **- The Employee Benefits Security Administration (EBSA) Report**

"Some stakeholders attributed concerns about developments in these areas to private equity firms' increased involvement in the industry.

They said that private equity-affiliated insurers tend to engage in riskier practices than traditional insurers. Stakeholders were also concerned that private equity firms do not have a long track record of managing life insurance obligations and may lack a commitment to policyholder interests," the report said.

However, EBSA declined to propose amendments to IB 95-1 on the basis that the issues raised are 'complex' and said that a lack of consensus among stakeholders stymied potential action.

The EBSA report said that six advisory council members didn't back any changes to the bulletin, while the other nine members supported different positions on different issues.

The report also looked at the increased use of reinsurance in the life insurance sector noting that it had increased from less than $200bn in 1999 to $1.7trn in 2022. This quadrupled the share of life insurance obligations being reinsured from 6% to 24% of the total.

"A number of stakeholders raised concerns that life insurers are using reinsurance to move liabilities to less regulated reinsurers. They mentioned less stringent reserving requirements and accounting arbitrage as reasons for their concern," the report said.

The EBSA report also specifically mentioned modified coinsurance - a variant of coinsurance which sees the cedent transfer only liabilities and keeps the assets on its books, while paying a portion of the interest from the retained assets to the reinsurer.

The report cited figures from AIRT Insurance Research which said that a total of $384bn was ceded under modified coinsurance contracts to foreign domiciled reinsurers in 2021, with 86 percent ($333 bn) of those reserves being sent to Bermuda.

It also noted that a 2023 study had demonstrated that private equity-backed firms are much more likely to utilise this type of reinsurance contract.

Despite acknowledging that stakeholders had raised concerns that modified coinsurance arrangements may provide insurers with an incentive - under existing risk based capital standards - to hold on to riskier assets longer than is optimal, the EBSA report said that no recommendations for changes had been made.

The report also said that a number of respondents had pushed back against the idea that offshore insurance was inherently riskier than keeping the assets and liabilities onshore in the US.

"While recognizing that the level of regulatory oversight of offshore reinsurance differs by jurisdiction, some stakeholders argued that Bermuda is well recognized as a credentialed international reinsurance jurisdiction," the report said.

The report may have shied away from proposing changes to IB 95-1 currently, but it did not rule out making changes to the three decade old rule set in future. Instead EBSA will take further industry soundings, with a view to potentially taking action at a later date.

"Further exploration into developments in both the life insurance industry and in pension risk transfer practices is necessary to determine whether some of the [current regulations] need revision or supplementation and whether additional guidance should be developed," the EBSA report said.

> **"We look forward to further exploration of the issues and concerns raised during the process, so that we can consider what next steps may be necessary to guide fiduciaries considering a pension risk transfer for their defined benefit pension plans, so that the fiduciaries can meet their obligations to participants and beneficiaries"**
> **- Lisa M. Gomez, Employee Benefits Security**

Assistant Secretary for Employee Benefits Security Lisa M. Gomez made similar comments in the press release which accompanied the report.

"We look forward to further exploration of the issues and concerns raised during the process, so that we can consider what next steps may be necessary to guide fiduciaries considering a pension risk transfer for their defined benefit pension plans, so that the fiduciaries can meet their obligations to participants and beneficiaries."

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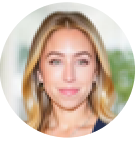
Making Sense of Pension Risk Transfer Deals for Deferred Lives



Author:
Caitlynn Greenfield
Director
WTW

Author:
Justin Bevan
Associate Director
WTW

Author:
Stan Roberts
Associate Director
WTW

The US pension risk transfer (PRT) market continues to grow. With around $45 billion of transactions, 2023 was the second busiest year on record for PRT deals, and that pace was sustained during the first quarter of 2024.[1] However, as employers have been eager to transfer pension plan liabilities to the insurance sector, most of the simple deals have been done; insurers that want to continue in this market will need to get comfortable with more complex transactions.

Facing market uncertainties

Many of the deals so far have been for plans that only feature retirees. These have been relatively straightforward to price. The acquiring insurer knows exactly how many plan participants it will need to pay benefits to and has all the details of how these benefits will change over time. It only must make assumptions about mortality rates, asset returns and its own expenses.

By contrast, most of the plans now coming to market have large numbers of deferred lives – employees or former employees yet to begin taking their benefits. This adds significant uncertainty for insurers. They can't be sure when deferred lives will start drawing their pensions; some may retire early or late. This can affect the size of the benefit. Nor do insurers know what type of annuity deferred lives will choose. They may not even have the basic demographic details of the dependents of the deferred lives who may be entitled to benefits from the plan.

With so many unknowns, pricing a PRT deal that includes significant numbers of deferred lives is challenging. Some insurers have simply opted to steer clear of such transactions. In the future, however, almost every PRT transaction coming to market is likely to pose this problem.

Dealing with the unknowns

The good news is that a PRT deal that includes deferred lives is not a complete leap of faith; several sources of data can help insurers move forward with greater confidence.

For example, the sponsoring employer likely has good data on the decisions made by previous generations of deferred lives. WTW's surveys reveal that insurers have made use of data from DOL Form 5500 Schedule SB filings (which pension plan sponsors must submit annually) that include documentation of this experience data. The census data of current retiree records for the plan, usually included in the deal, are another rich source, as the data include granular information such as commencement ages and form of payment. Finally, insurers may already have done similar deals; the experience of how these transactions played out is one more source of insight.

Using these data, insurers can begin to model the likely outturns for deferred lives of an individual plan in each of the areas where they are grappling with uncertainty:

Commencement age

Insurers can make an educated assessment of when each cohort of deferred lives, grouped by current age, is likely to begin taking benefits. There are some common spikes for retirement age – 62 and 65 given the connection to social security and Medicare.

"WTW's surveys reveal that insurers have made use of data from DOL Form 5500 Schedule SB filings (which pension plan sponsors must submit annually) that include documentation of this experience data"

Commencement type

Insurers will also need to model for both active participants of the plan and deferred vested participants (those no longer working at the employer in question). The former may leave employment to retire, but they may also leave for other employment, in which case they may not begin drawing benefits. Another group may leave due to ill health or disability and therefore be entitled to specific benefits from the plan. Some may even die.

Type of annuity

The type of annuity deferred lives will eventually choose is another key factor; joint and single-life contracts, for example, carry very different liabilities. The current marital status and family circumstances of deferred lives can add granularity to the model here, though these may change before the participant reaches retirement.

Lump sum take-up rate

Where plans offer participants the option of taking a lump sum instead of some or all of their income entitlement, this will be a material consideration. This may affect the duration of insurer's cash flows – and therefore asset allocation – and will necessitate an assessment of interest rate risk. Take-up rates are not easy to estimate; WTW's experience suggests these vary from below 50% to more than 90%, depending on the terms of the lump sum alternative on offer.

Spouse and dependents

Where plans offer dependents' benefits, insurers will need to build an assessment of the cost of these into their models. This will depend on both the value of those benefits and the proportion of deferred lives to whom they are relevant (and likely to become relevant in the future).

Market-related assumptions

Deferred lives also bring complexities around market-related factors, particularly around assumptions about future interest rates and inflation. Plans may include future benefit increases related to the cost of living, for example.

> **"In an ideal world, standardized assumptions would help insurers model for deferred lives in each of these areas. But because every plan offers different benefits and has participants with distinctive characteristics on gender, age, professional status and more, this simply isn't possible. Both plan design and demographics have a huge impact"**

Adjusting for difference

In an ideal world, standardized assumptions would help insurers model for deferred lives in each of these areas. But because every plan offers different benefits and has participants with distinctive characteristics on gender, age, professional status and more, this simply isn't possible. Both plan design and demographics have a huge impact. Early retirement subsidies, for example, will skew commencement ages; lump sum options are often popular. Men are more likely than women to select joint-life annuities. There may also be more than one population of participants to consider – where plans have evolved over decades of mergers and acquisitions. It is even possible that participants' behavior will change as a direct result of the PRT transaction, as participants move away from a plan sponsored by an employer with which they feel comfortable.

For all these reasons, modeling individually for each deal therefore produces a more accurate assessment of future liabilities. It is also important to build a degree of sensitivity into these models – and to increase tolerance levels where larger numbers of deferred lives are younger, since this will increase uncertainty. New technologies will play a role, as some of the current limitations of software will be overcome, making it easier to model multiple forms of payment, to develop multiple decrement models and to forecast with more accuracy. Finally, the rapid evolution of predictive analytics tools also provides reason for optimism.

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

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[1]Record-breaking year for Pension Risk Transfer market in 2023: Legal & General

Premiums Paid Offset Awarded to Investor in Florida Estate Recovery Case

Author:
Brian Casey
Partner
Locke Lord

In an important decision issued in April 2024, the Florida Fifth Judicial Circuit Court, applying Delaware law, granted summary judgement to Viva Capital 3, L.P. awarding it the right to offset the amount of insurance premiums it had paid for a $10m life insurance policy issued in 2006, which Viva had purchased in a tertiary life settlement policy purchase transaction, against the death benefit to which the insured's estate was entitled to recover from Viva under Delaware's insurable interest statute.

Viva received payment of the policy's death benefit in May 2017, after having owned the policy for only about six months. Nearly three years later, Mr. Albart's estate sued Viva to recover the entire death benefit.

Earlier in this case, in October 2023, the court granted summary judgement to Mr. Albart's estate, finding that the life insurance policy was issued without the requisite insurance interest under a non-recourse premium finance loan where the insured had not paid any portion of the premiums for the policy, and following a 2021 Florida federal court case, *Estate of Malkin v. Wells Fargo Bank*, which involved a life insurance policy originated under the same financing program and a claim by the insured's estate to recover the dearth benefit that had been paid to investor that owned the policy when the insured passed.

The Malkin case did not definitively decide the question of whether the investor was entitled to offset the insurance premiums it had paid for the policy against its death benefit that the insured's estate was able to obtain from the investor, saying only that a policyholder might be able to offset premiums it had paid if it could demonstrate a "viable legal theory" therefor.

The court in the Albart case found that Delaware's estate recovery statute codified, prior long-standing case law, derived from Warnock v. Davis, an 1881 case, that allowed a life insurance policyholder that had applied for and purchased a life insurance policy on the life of Warnock in which the policyholder did not have an insurance interest to retain from the policy's death benefits the amount of premiums that had been paid for the policy, leaving the insured's estate's recovery of the policy's death benefit net of these premiums paid.

> "The court went further, however, holding in dicta that Viva's offset claim would have prevailed based on its unjust enrichment claim even if the Warnock decision were not baked into Delaware's estate recovery statute"

The court went further, however, holding in dicta that Viva's offset claim would have prevailed based on its unjust enrichment claim even if the Warnock decision were not baked into Delaware's estate recovery statute. As a result, this case tempers the Delaware case law that has found that a life insurance policy issued through the payment of premiums by a person other than the insured is prima facie without a valid insurable interest by reducing the amount that an insured's estate can obtain under Delaware's estate recovery statute.

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Q&A

Jay Jackson
CEO, Abacus Life Settlements

Author:
Greg Winterton
Contributing Editor
Life Risk News

Life settlement provider Abacus Life listed on the Nasdaq a year ago, a rarity in the life settlement market. Greg Winterton spoke to Jay Jackson, Founder and CEO at Abacus Life, to get his thoughts on a range of topics in the life settlement market.

GW: Jay, we're into the second half of 2024 now, and both LISA and The Deal have published their annual data insights into activity in the secondary market. What are your thoughts on the results at an industry level?

JJ: Overall, I thought the results were encouraging for our industry. The life settlement market had a strong year in 2023 in both number of policies purchased, and total capital deployed. The growth can be attributed to an increase in awareness driven by not only television and digital marketing but also financial professional outreach.

GW: It's approximately a year since Abacus listed on the Nasdaq. What are some of the lessons you've learned after being a public company for a year?

JJ: The challenges of being a public company are the demands related to reporting. Historically, we would prepare for audits and reviews annually – now that occurs every 90 days. The markets are not only learning about our industry more frequently but are also scrutinizing the results every quarter. This level of scrutiny requires a higher level of accountability, transparency and operations. In addition, becoming a public company created additional transparency and regulatory review of not just our company but the industry, which has had a positive impact on the overall optics of our industry.

GW: Back to transactions now. The direct-to-consumer market, in which Abacus participates, has been growing generally in the past few years. Is this trend one that is something of a paradigm shift in the life settlement market, in the sense that the secondary market will increasingly see deal flow from this segment?

JJ: Our industry has been built on education. The challenge is the education can take significant time before an impact is made. The direct-to-consumer market is not different. It requires significant resources in both operations and capital to be successful. The benefit of direct-to-consumer education can be materialized through all origination channels. As companies continue to invest in education then there will be a positive impact for the entire industry.

GW: What about policy type and features – are you seeing more seasoned policies, or younger people looking to sell their policy, for example? Anything interesting at the type and insured level?

JJ: We have seen a significant increase in the volume of larger face value contracts. We believe a cause for this shift is awareness from financial professionals as they are now communicating the benefits to their client's estate. The optic of the transaction is shifting from a one-off small transaction for seniors who are in financial need to an estate planning tool used by high-net-worth households.

GW: Finally, Jay, back to the aforementioned secondary market activity data. What would you say is the main puzzle that needs to be solved in order to really get the life settlement industry moving in terms of secondary market deal flow?

JJ: Education and operations related to the documents used in acquisition. We as an industry should spend more time educating the states on a more streamlined document process. This is one piece of the puzzle that would have a significant impact on increased deal flow.

Should Senior Living Investors Pay More Attention to Longevity Risk?

Author:
Greg Winterton
Contributing Editor
Life Risk News

Investors in the senior living market in the US are typically more active in assisted living facilities, as opposed to a nursing home. The two are very different stateside and provide different levels of care.

But regardless, for senior living investors, the risk associated with investing in the space has typically been a real estate one – vacancy rates. Every unoccupied bedroom is missing rental income that could be going into the bank account of the investor.

But as far as risks go, that's arguably a small one, with the industry recently seeing occupancy rates increase for the 11th consecutive quarter to stand at 85.6% in the first quarter of this year. Whilst occupancy still lags the pre-pandemic high of 87.1% in Q1 2020, the market expects this to return to normal this year.

> **"The continued upward climb of occupancy along with strong absorption levels supports the NIC forecast of returning to and surpassing the pre-pandemic occupancy levels sometime in 2024" - Lisa McCracken, National Investment Center for Seniors Housing & Care**

"The continued upward climb of occupancy along with strong absorption levels supports the NIC forecast of returning to and surpassing the pre-pandemic occupancy levels sometime in 2024," said the National Investment Center for Seniors Housing & Care's (NIC) Head of Research & Analytics, Lisa McCracken in a press release in April.

Good news for those investors with retirement communities in their portfolios. And, given the slow pace of new developments - the rolling four-quarter average for construction starts sits at 1.37% of total inventory, the lowest level since first quarter 2010, according to the NIC – tailwinds exist to support higher occupancy data.

"With little change in access to capital and in borrowing costs, particularly for new projects, we continue to see depressed levels of construction starts," said Caroline Clapp, senior principal with NIC, in the same release. "We expect this trend to continue until financing conditions ease."

That all sounds great for those private equity real estate folks. And if someone doesn't pay, then they can just be kicked out, because unlike a typical landlord / tenant relationship, most states permit eviction in instances of non-payment of rent and sell the spot to the next person in line.

Said rent has been, historically, calculated using a combination of a spread over the mortgage and other costs, with a consideration to what the local market might bear and any competitive pressures. But with residents potentially staying longer due to increased lifespans, senior living facilities might benefit from a more nuanced approach.

That's according to Chris Conway, Chief Development Officer at life expectancy underwriting firm, ISC Services.

"Senior living investors and operators obviously tend to price using a real estate approach," says Chris Conway, Chief Development Officer at life expectancy underwriting firm, ISC Services. "But they're not necessarily looking at how long they might need the kinds of services they deliver for a particular resident. The length of supply can impact the margin to the investor."

A range of benefits can be had to the investor by taking a longevity modelling approach, beginning with increased accuracy in terms of cost projections. Taking into account resident demographics, health history, and projected lifespans allows for a more accurate prediction of future costs associated with each resident, including care needs and potential length of stay.

"Longevity modelling allows investors to set sustainable rent structures; by understanding the long-term care needs of residents, investors can price rents that factor in the increasing cost of care over time which ensures financial stability and prevents unsustainable rent hikes later. Furthermore, they can allocate resources efficiently; knowing the future needs of residents allows for proactive resource allocation. Staffing levels, medical equipment, and activity programs can be tailored to the evolving needs of the resident population, leading to cost optimization," said Conway.

Other areas of application of longevity modelling to the senior living market include mitigating risk, for example, diversifying care options within the facility, offering flexible financial plans for residents, or partnering with long-term care insurance provider; this would also be a selling point for capital raising for any future developments.

Whether or not the senior living market pays more attention to life expectancy modelling and underwriting as an input into the pricing model remains to be seen. If it ain't broke, don't fix it, after all. And with the fundamentals in the market currently – an ageing population and not enough development of new facilities to absorb the demand – pointing to a solid outlook for investors, perhaps adoption will be a slower burn.

> **"Often, senior living facilities operate with fixed costs per resident. If residents stay longer than anticipated, it could strain their financial resources or those of the facility. A greater understanding individual life expectancy – micro-longevity – is a logical next step for a senior living investment firm to help them increase the returns on their investments"**
> **- Chris Conway, ISC Services**

Still, for Conway, there is an air of inevitability about this.

"There are many reasons why senior living investors should consider using longevity risk as a consideration in their costs and revenue modelling," he said. "Often, senior living facilities operate with fixed costs per resident. If residents stay longer than anticipated, it could strain their financial resources or those of the facility. A greater understanding individual life expectancy – micro-longevity – is a logical next step for a senior living investment firm to help them increase the returns on their investments."

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Editorial Enquiries
editor@liferisk.news
+44 (0) 20 3490 0271