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MDRT – Coventry:

The Secondary Markets for Life Insurance – the Next Generation – Michael Coben

You have situations like split dollar where the situations are structured, where there is a theoretical rollout structured 15 years after the engagement of the agreement. We all know that sometimes things change, like the financial markets or the employment situation of the employee and you need to alter the plans.

One of the applications of the secondary market is to help in solving those needs. In other words, we've seen split dollar agreements being rolled out of using the market value of the policy to re-engage with the corporation to pay back their costs. We've seen key man coverage that was originally placed for coverage or buy/sell agreements placed used as an asset of corporations upon the departure of the employees. So there's been real dynamic application in the secondary market in planning, and it's not just now a transaction, it's really a planning tool.

When we first engaged in the marketplace, it was viewed as a transaction. And as we've learned over the last five to seven years, it has really morphed into a planning tool, as I said. And one of the things that has happened with how

robust the industry is, is that we've got now a tremendous amount of highlight in regulatory environment and the legislative environment. So what I would like to do today is go through where we've been in the past, where we are today and some of the hurdles that we're wrestling with today. Even relative to the financial markets as we stand in terms of the credit risk and how that's impacting our industry.

I would like you to ask questions as I go through. I know some people in this audience that have had a tremendous amount of success utilizing the tools of the secondary market. There are some people in this room that probably haven't even engaged in the marketplace. So I'm trying to cover a wide variety of knowledge.

One of the things that I saw coming in to the industry was a tremendous amount of people questioning why I was making a move from the stability of the life insurance industry to this new, at that time, emerging growth marketplace that from a carrier standpoint, was almost heresy. That was six years ago. I remember seeing a quote that our CEO has always talked about, in terms of the nature of our industry and it's a quote by Arthur Schopenhauer. And it talks about truth and truth going through stages before it's accepted.

The first stage of truth is that it's obviously, vehemently ridiculed, opposed and then becomes self-evident. We are now at the standpoint of the secondary market where it's self-evident. In other words, people really understand that there is an impact to the secondary market, in terms of a positive impact to consumers. We're seeing that in terms of carrier acceptance. We're seeing carriers now engaging the secondary market from a defensive standpoint and also from an offensive standpoint.

What I mean by defensive standpoint, they're looking at ways where they can incorporate alternatives within their own product design to combat against the secondary market. They're also investing in the secondary market themselves as a hedge to the marketplace.

We've seen robust growth, we've seen tremendous planning opportunities and we've seen, as I've said, widespread engagement in the marketplace. But we've also seen a lot of hurdles lately. And some of the hurdles stem from a new marketplace growing quickly and one of the hurdles that we're wrestling with currently is the SOLI (Stranger-Owned Life Insurance) market. I'll reference that in terms of the impact to the secondary market.

This presentation is not going to be about SOLI. This presentation is going to be about life settlements and the use of the market value of a policy to accomplish planning tools. We're not going to get into the use of the fair market value of a policy being pledged as collateral for a loan, that's something that will be outside of this conversation.

Where we are today. We believe there is close to \$23 billion of face amount that has been transacted since the true maturation of the marketplace. I think that number is actually shy; it's from Conning's Report in 2007. The reason why I think it's shy is Coventry itself has been responsible for over \$13 billion of face and we don't think we're responsible for over half of that \$23 billion. So the marketplace is probably closer to \$30 to 35 billion, in terms of transferred face amount to date.

Conning also reported that in 2007 that face amount transferred was about \$12 billion. We think that's shy as well. However, we don't think what they're projecting in terms of the annual rate of face amount being transferred is shy. They think by 2010 and 2012 the marketplace will be about \$20 to 25 billion of face amount transfer per year. And that's through the maturation of

understanding that the population is aging, that the application of the marketplace is going to be much more widespread than it is today.

Also, one of the things they're predicting which we see happening now is that the marketplace will not just be for the ultra high-net worth, that it's going to morph down more toward the middle market. We're seeing many providers in the industry now looking at policies as low as \$100,000, not just an average which we see. Our average purchase is about \$2 to 3 million per life. That is now, we're going to see that going down as we move into the future because I think there's a lot more yearning for a greater breadth of audience.

We're also seeing a growth in the marketplace through the ability for providers, like ourselves, to purchase younger lives. What I mean by that is, typically when you look at the secondary market and (you looked at it five years ago, even three years ago) people were saying you can't even look at possibly a policy for a client that may have value unless they're 75 or over, and then it went to 70 and over, then it went to 65 and over. We're now seeing value in cases where clients are in their mid-60s. Some of them have had health changes, some of them haven't. (This) depending upon the cost of the policy in terms of the efficiency of the policy. I'll talk a little bit about pricing in a little bit.

The reason for that is, investors are willing to commit capital for a longer duration. In other words, instead of wanting a return on their investment over in 8 to 10 year period, that's been historical. There are firms out there that are willing to invest 15 to 20 years out. The impact though is that there's going to be a lot more knowledge on mortality. In other words, if you have to wait as an investor, 15 to 20 years for a pool of 200 to 300 policies to come due, you're going to watch and wait your mortality every year, in terms of making sure you're on track.

I can tell you the difference, and we're going to see this in pricing: if you're using a pricing model and you're assuming your average life expectancy in the pool is 18 years and it turns out to be 22 years, that could mean an investment return going from a 12 percent down to an eight percent return in the entire portfolio. So, there is a dramatic risk involved in this business, and one of the things that's happening is the capital markets are now becoming more comfortable with that risk and understanding how to model that risk a little bit better.

The area that's interesting is the application, in terms of product line. We're now not just seeing policies that are traditional UL underfunded policies, but we're seeing obviously term policies that are convertible. We're also looking at Whole Life policies, which in the past was a little bit more difficult because of

the structured premium. You couldn't manipulate the cash flow as an investor. And we're also seeing the engagement of annuities where we're looking at, and there are firms like JG Wentworth out there that historically have purchased structured settlement annuities. But we've looked at situations where we may have had annuity arb cases where annuities were used to fund life insurance and there are loans used against it. Now, because of the economic environment, interest rate factors are such that it could be out of whack. We're looking at buying the entire package. In other words, buying both the cash flow of the annuity, plus the life insurance policy as an exit strategy. So again, another way of looking at the application of the secondary market.

I talked about the different products we're looking at now. One of the things that has really moved forward in terms of application in the advisor community is not just a cash settlement option but the application of a guaranteed paid up death benefit. What I mean by that is, there are many advisors out there that are concerned about trust owned life insurance and maybe the funding of the trust owned life insurance.

A couple of cases we've been involved in recently, is they're way above their annual exclusions and they're trying to figure out a way of cutting down premium costs. One way to do that is to lower your death benefit. Another way is try to do a replacement, to get a more efficient policy. One of the alternatives

available now in the marketplace is, instead of saying I want to cash in my policy through a life settlement, I want to have it valued for what we label a guaranteed death benefit. What that references is that carriers have reduced paid up options, whether it's extended term or a guaranteed paid up. The problem with those options is, it's based on the true guarantees of the policy. So it's based on the original guaranteed mortality rates. If we could apply someone's current health situation and the current pricing of a policy, and I'll give you an example, let's say it's a \$10 million policy, instead of offering them \$1 million of cash and maybe the cash value is \$200,000.

We may be able to look at the same life and say there's a life expectancy of 10 to 12 years, what would be the future potential value of that cash settlement? We may come up with a future value of \$3 to 4 million. That could solve the client's needs today. In other words, they may only have enough cash flow for about \$3 to 4 million and maybe what they will do is get a brand new policy for that amount and then get the guaranteed death benefit from a provider like ourselves for the balance so they now have about in that situation, family replacement insurance for \$3 million, and we're able to reduce that \$10 million policy down to \$3 million on a guaranteed basis. Now they have \$6 million of coverage for the same cash flow that they wanted for \$3 million. That transaction now is happening every day. It's a little bit different, it's almost like

the way of backdooring, in terms of problem solving. But it's a unique option, and more and more advisors are looking at that in today's environment.

One of the questions I get asked all the time is, how do providers in the secondary market come up with a value on a policy? So I thought it would be important to show you some of the important aspects in how we price a policy.

The one thing obviously is age, and that's all relative to how long a purchaser is going to intend to pay premiums on a policy and that's tied to life expectancy. Underwriting and life expectancy is critical. Those who have been engaged in the secondary market understand there is a dramatic change going on right now relative to underwriting and life expectancy assumptions. One of the major life expectancy firms out there has done some recent mortality studies and has said on all the pools that we've helped manage in terms of our pricing, we need to take a look at potentially extending life expectancies a couple of years because we were off in our assessments. That will have a dramatic impact, not only for new prices. In other words, as people who have policies coming due, you're going to see a softness in the marketplace. Those who are involved in the marketplace now understand what I mean, is that it is a lot softer. It's like the real estate marketplace where prices were up and now coming back down.

I can't tell you if we're going to go back up. Because I think what's happening is that firms are really looking at true mortality experience now and they're not getting what they originally expected. They're requiring obviously either a higher return or they're requiring a longer period of time in terms of the investment period, which requires obviously more capital commitment.

Q. What made them get off about 30 percent from their original projection, they discovered that?

A. They looked at some of the original pools that they priced dating back four or five years and saw that they were off. Also there was a recent mortality study, it's the study which basically said that people are living longer than anticipated. What we found is firms aren't using the actual new study, they're using a percentage in new study. Which is still longer than what they originally projected. I can tell you also from observation, there are a lot of firms out there that were using aggressive mortality because they were attracting capital. They were showing a model that looked really nice because the mortality assumptions were really aggressive. But if you applied a little bit more conservative assumptions then the return wouldn't be as significant and the capital may not be as willing to enter into the marketplace. And we did see that a lot.

Our firm has been in and out in terms of how competitive we are in cases. As a matter of fact, I label it very much like the substandard life market where you've got to go out and shop a case to multiple providers, multiple carriers. Because you don't know how one company is going to do a particular case. That's our marketplace and you have to be comfortable with that process because it's no longer as it was 10 years ago, one or two players. There are many players in the marketplace that weave in and out. In the capital, United States base, the capital is European based.

So you never know on a given case who's going to be more competitive but I can tell you that we have always had capital commitments and we always have had tremendous experience in terms of closing cases. We've never stopped buying in the marketplace. We've ebbed and flowed and right now, we're from what we're hearing, there are four active funders in the marketplace that are active. (This means) currently engaged without withdrawing and stop and starting over a period of time. We're obviously one of them. We're benefitting from that at this point.

Cost of policy is important. Obviously if you're a 90-year-old client and the policy cost 12 to 15 percent of face, that's something that the marketplace is

not going to be willing to look at. But if you're in your 60s or 70s and you have a policy that prices anywhere from 4 to 6 percent of face, that may be very attractive. The reason for it is as an investor you don't want to put too much money into a policy where there's a point in time where your return has been diluted.

I think the biggest thing we're seeing in terms of the impact outside of underwriting right now, is carrier ratings. What I mean by that is, you think about the credit markets. One of the things the investors are doing now is they're looking at the quality of the insurance carriers that they're purchasing and they're discounting for that. I can tell you right now there is some discounting going on for some carriers that have had some negative press lately and have had some downgrading. The reason for it is that we want to make sure that when these policies mature, when the claims come in, that the claims are going to come in as expected. They're not going to be impaired in any way because of forfeitures of the carriers. We've had a couple experiences where that has happened.

Impact of underwriting. I referenced earlier that underwriting makes the biggest difference in a case in terms of what a funder like ourselves can offer. This is an example of a 70-year-old who was issued a standard policy, hypothetically three years ago. So they were 67 and now they are 70 years old.

We're assuming it's a quality carrier, an A rated carrier. The cash value is \$137,000 and the current premium is about \$150,000. If we looked at that client today at age 70 and we assume that client was standard. A standard risk with the mortality is probably anywhere from 15 to 16 years in terms of life expectancy. We would value that policy to be about \$445,000.

If we looked at the same life and said this client is a Table B, in our industry that would reference that that client would probably move down to a 12-year life expectancy. That's the kind of impact you would see in the offer. The offer would go up to \$760,000.

Now, people ask, how does that happen? Because we always get cross-eyed when someone says, how did your offer move from \$400,000 to \$500,000 or \$600,000 overnight? The reason for it is, think about the negotiations you do with your underwriters on substandard life cases, where you have three or four companies looking at a case and you have a Table 1 here, you have a standard here, and you are preferred here. What's the premium difference between all that? Pretty dramatic in some situations.

For us, in this situation, if we were able to be "beat an underwriter up" from standard to Table B, in other words, we said the client was actually worse off

than they were, that reduces the life expectancy which ends up popping potentially how much we're willing to pay for that policy. That type of negotiation happens infrequently, but does happen. What happens more frequently is our underwriters may look at the case and say it's Table B and XYZ funder underwriter looks at it and says it's Table 1 or standard, and that can create the difference. Then what happens is, if we were the standard and we're trying to fight the Table B, the only thing we can do is reduce our rate of return on the investment. In other words, maybe we're pricing to a 12 percent return. The only way to get to the \$760,000 is maybe we were pushed down to a 10 percent or a nine percent return.

We may sometimes do that for a business decision depending on who the source of business is, and this is something that's happening right now, do we need more of one particular policy type in our portfolio, do we need more of one particular age grouping, more of one particular carrier in our portfolio? That happens a lot and we may have the same life, same situation, same life expectancy and in one scenario we're very aggressive and six months later we can come back and be not as aggressive. The reason for it is we may have too much of that life. We may have a concentration risk in the portfolio. We may have too much of a particular carrier in our portfolio which could dilute our ability to take that case.

I thought that would be interesting in terms of sharing with you the real impact that underwriting has in the industry.

What I'm going to do now is go through several case studies that we find prevalent in our business that are somewhat different than the historical case studies that people have looked at in our industry. One of the things that we're seeing that we're labeling as a movement toward healthier lives and when we mean healthier lives, we're talking about younger lives that have either fairly healthy in terms of being issued a standard policy instead of a preferred policy relative to the past where we needed a fairly dramatic change in health.

One of the things we're finding is that the application is more prevalent in the replacement market than ever before. Or, the application of someone thinking that this policy, traditionally, I would not think of a life settlement and now we're finding value in that policy where we had not before.

This is a case we're involved in with business insurance; there are two \$5 million UL policies, a total of \$10 million. The case value is \$1.2 million. The policies were purchased for \$1.4 million. That may not seem dramatic compared to what historically we've seen in valuation for life settlements. When people think about life settlements they think about three, four, five times cash

value, but what we're seeing as a relevant change is that if we're able to look at younger life like a 65-year-old who is standard in our underwriting, that \$200,000 is still a value available and whether the owner of the business wants to capture that value or not, it's really up to him. One of the things we're trying to make sure everyone understands is provide that information. In other words, at least give that information to your client so they can make an educated decision on the asset versus an uneducated decision.

For those who have been through the process, all the client would have to do is sign an authorization and we collect five year's worth of APS's and we look at an in-force illustration and we model to see the value of the policy. If we model it and you're doing your client review in terms of reviewing their assts, their insurance, if you say part of that process was valuing their insurance and you found \$200,000 excess above cash value available in the secondary market, they may say we're going to take that \$200,000 because we were going to drop the policy anyway.

Another event that's happening in the marketplace is a tremendous amount of term insurance is being sold. It's typically convertible term. We're seeing it in a couple of scenarios.

This is a scenario obviously that the policy was no longer needed and this client actually had a slight impairment from inception and on the \$7 million policy we saw a value of over \$500,000.

One of the scenarios we're seeing a lot more is if a client is looking to convert a policy, what they'll do through the advisor is to see if they are healthy enough to buy a new policy without converting, in other words, going in full underwriting in the marketplace. If they are able to, then they're going to compare that cost to the converted policy. And one of the things we're finding is even if the new issue is a little bit more expensive than the converted policy because maybe they were issued originally preferred but the new issue is standard, that the excess capital, in other words, this \$525,000 if this was a replacement, could be used to help bring down the cost of the new policy potentially way below the converted premium. That transaction is happening every day.

The other transaction which we're finding out is happening every day as well is when someone has term insurance and they're replacing it for new term insurance. Let's say they're 69 years old and they're in a 20-year term policy and they realize their convertibility period is going to expire. They may want to keep a term policy, why not look at buying a new policy, maybe a 10-year term but a guarantee period that is going to last longer than the original period. Sell

the old policy, have the proceeds, if it's business owned, go back into the corporation and reissue a brand new term policy.

From an advisor's perspective it's a tremendous opportunity because you have multiple revenue opportunities for yourself. Compensation for the term that is going to be converted and also compensation for the new policy being issued.

I referenced death benefit option earlier, and as I said, this is probably becoming a hot topic of discussion in the estate planning community relative to what's happening in the marketplace today. A lot of people didn't realize that the transaction in the secondary market can be morphed into not just a cash option but a death benefit option. I verbally demonstrated the scenario where we used it as a replacement situation, but I wanted to show it in a slide format.

So this client is a young client, 67, was looking at the amount of insurance he had. They knew they needed to keep \$5.5 million but they only had a premium tolerance of \$120,000. Unfortunately because of declining interest rates, premium was almost getting to double that amount. The first thing they thought about in their planning was should I do a 1035? Unfortunately because of the change in health, it didn't make sense. The new premium on the

new policy with just the cash value just didn't economically make sense for replacement.

Next thought of process, for traditionally thinking about it, is look at a life settlement. We valued the policy to be \$1.6 million and unfortunately that still wasn't enough to make the new policy more efficient than the existing policy. Remember, the client has \$120,000 premium tolerance and the premium now based on current rates is well in excess of \$200,000. So what do we do? Well, we looked at the policy and said if we offer a guaranteed death benefit, we can offer \$3.6 million on that original face amount. Now what do we do?

I only know one or two firms in the marketplace that offer this option, and we're probably the one that is transacting the option, not just sharing the option with an advisor. We'll take ownership of the policy. We'll take on premium responsibility and we'll share the death benefit on an irrevocable basis with the original beneficiary. So ABC Trust owns the policy. ABC Trust will be an irrevocable beneficiary for \$3.6 million. Coventry would be the beneficiary for the balance. When the proceeds come in through a death claim, the carrier automatically splits the proceeds into two pieces.

However, the client still needs \$5.5 million of insurance. So \$3.6 million is fine but how do we look at getting additional insurance? We know that in every case there are some carriers that want business. And in this particular case one of the carriers said they would be willing to offer \$2.3 million of coverage on a preferred to standard basis for the client. Everybody else was heavily rated. There is one carrier that is willing to do a table shaving to get it down on a standard/preferred basis. We helped the advisor back in and say what would \$120,000 buy? It happened to buy obviously, \$2.3 million.

Now think about this. The client's cash flow is \$120,000 because on the \$3.6 million, they're not paying any premium on anymore; we're paying the premium. They're paying a premium for \$2.3 million. We now accomplish the issue of how do we get someone's premium tolerance down to \$120,000 from a current premium basis in excess of \$200,000? This option would not have been available five years ago. We've talked about it over the last couple of years and when I go in front of estate planning councils, CPA councils, they are very interested in this because of the uncertainty of the marketplace relative to their clients' ability to continue gifting and the ability to change the situation to fit their needs.

Q. Just from a mechanical standpoint, what do you guys do with all that money when ... leave it in the policy or ...

A very good question. We think we can do better with the funds than the carriers can in their fixed accounts and their UL rates so we'll take the money out and put it in our own accounts. We'll actually model these policies, like term policies, so we'll leave enough to help pay the bare minimum premium throughout. Typically we'll try to take out as much. A lot of the policies restrict you for how much you can take out of the policy. That's why whole life is so hard to purchase because we can't withdraw the cash out of a whole life policy without actually taking a loan, which ends up reducing the net amount at risk, which depletes our investment.

Q. You talk about buying additional insurance without being sold the first policy. A lot of carriers have that question on their policy within the last two or three years. In your opinion, how does that affect the insurability of the person as far as new security?

A. I think it's carrier by carrier. I was actually in conversation with someone this week at a big producer group meeting. They said that right now they're writing very effective cover letters explaining the transaction to the underwriter. They're finding that the more upfront they are in explaining the transaction and that this person doesn't have a history of this type of engagement, that it's

strictly for this transaction, the carrier is more comfortable. But it's carrier specific. I know some carriers that don't even ask the question, I know some carriers that do ask the question, and they'll have offline conversations with you. I just know from my past the more upfront you are with an underwriter in detail cover letter, the better you are in terms of them feeling comfortable proceeding on the case.

Q. The next topic, not trying to say it's different, but if you're doing a swap like this, you're actually buying the new policy before you get to sell the old one. So technically the answer is no. You wouldn't enter the swap until you knew you had the \$2.3 million, so the answer is no, you didn't sell it yet.

A. Where we're finding some of that friction is an alternative to the 1035 on the cash side. As I said, if you're upfront and the carrier doesn't see a high propensity of that type of behavior in the past, that they'll be more comfortable moving forward.

One of the innovations in our marketplace, as I referenced earlier, is the expansion of the business in terms of just moving from the affluent marketplace down to more of a middle market. We entered a program called Simplified Underwriting Life Settlements where we'll look at a case with a

minimum face amount of \$100,000. Why were firms like ourselves not willing to do that in the past?

For us, the cost of underwriting a case when you look at the time our underwriters review a case, the financial engineering that has to be done in pricing a case, it's not a magic wand that happens. They spend hours looking at a policy and trying to figure out the most efficient way for paying for it. They're looking at the probability of someone passing away in 10 years and then they're saying based on that person's life expectancy, age, type of health, what's the probability of them living one or two more years past that. If that's a heavy probability then they have to back in based on that. That process takes a while. As a matter of fact, our financial underwriters and our engineers could take 3-5 days to actually model a policy to see if we're willing to offer on it. That's money. That costs us about \$4,000 in terms of APS work, underwriter time and the modeling of the time.

If a \$10 million costs us \$4,000, and a \$100,000 case costs us \$4,000, then why do you think firms like ourselves had a very high threshold in terms of what types of cases we would look for? That's why, because of the efficiency. We came out with an idea through one of our partners where we would look at a case on a nonmed basis. What I mean by nonmed basis, think about the cases that you've written in the past where you just used the nonmed on an

insurance application. Off of that an underwriter would make a decision without ordering APS's. That's our simplified program. We have an application that has a non-med piece to it and we ask the advisor and the client to sign off to their health history.

There are a variety of questions you would normally see in a nonmed and based on that we will do underwriting off of a modified schedule, so we're not engaging in ordering APS's, we're not doing some of the financial engineering that we typically would do in a policy. We're able to be involved in much smaller cases. From an efficiency standpoint one of the things we're finding is that when you're dealing with business owners, even individuals, in planning they may have some policies that historically you didn't think about in terms of having value. It wasn't worth your time, just like it wasn't worth our time.

The process of underwriting and providing offers, etc., has been expedited to the point where once we get an application in and we review it, within 2-3 days we have an offer out for you. That process could take months through traditional underwriting. Typically then we've seen a closing period within 30 days which is a big acceleration in the life cycle of the case compared to our traditional cases. Again, it's just a new innovation because of our understanding of the marketplace. Others are now getting involved in small faces as well. And the reason for it is efficiency more so than anything else.

I referenced growing pains in the industry. I'll position this by saying that Coventry is obviously not a supporter of SOLI. We were involved in a premium finance program through the relationship we had with LaSalle Bank which was a nonrecourse program but from everything that we saw in the marketplace and what we're seeing now in terms of the carrier reaction, was the type of program that was not problematic relative to some of the programs that were being positioned and sold in the past and are currently being sold. The big issue is, was there a prearranged agreement from the inception of that sale in terms of contractually. Did that lender or provider make the client commit from the inception that they had to sell a policy within a couple of years?

Programs like ourselves, and I'm not saying we were the only program, provided an option. In other words, we provided the capital for someone who wanted a short term financing and if for some reason they didn't want to keep the policy, they had the ability to sell the policy on an unrestricted basis. Many of the programs out there were not structured like that. People were given incentives for inducements to get into financing arrangements or even if they weren't, there are such restrictions on their ability to get out of those programs that it's almost like the whole purpose of setting this up was to sell the policy and have the original lender keep the policy.

What has happened is the reaction in the regulatory community and the legislative community is that they're lumping life settlements in together with SOLI. That's a very dangerous conversation because when people that are misinformed about the marketplace bring the two together and start restricting property rights for your clients, it's going to restrict your planning abilities as well. What we're trying to do is make sure that the two are separate. In other words, traditional life settlements are totally separate from the concerns of the SOLI market.

And what are the concerns of the SOLI market? Part of it is there are two models of regulation out there. One we believe will restrict the ability for you to work with a client. What I mean by that is if you have a client that bought a policy and within five years they decided they wanted to make a change to that policy, whether they wanted to find a new efficient policy or it just didn't fit their needs. According to Limer 44 percent of all new issues lapse in the first five years. Why? Because of buyer's remorse. They can't afford it, they don't want. That alone will impede our marketplace dramatically and your ability to work with clients. That's encapsulated in the NAIC model act and a lot of people don't realize that.

The Enquil Act which is really more of an attempt to go after the pure definition of stranger owned life insurance from the inception. They're looking at the pure

definition of what I referenced earlier, was there a contract at inception, was there inducement at inception, and it doesn't use the five year hurdle as a litmus test. We think that's much more pro-consumer. You're seeing many of your states that you reside in adopt the Enquil Act because of the efforts that our industry is having in terms of educating legislature.

As I said earlier, we are anti-SOLI, we think it's bad for the industry. We have actually taken a hiatus from the premium finance world because we're looking at the reaction of the marketplace more so than anything else. Those of you who have financed cases in the past, are probably seeing a real softness in the market should a client want to sell those financed policies. The reason for it is providers like ourselves are very concerned about if we purchase a policy, is that policy tainted? Would a carrier down the road have the ability to rescind that policy? If they did, obviously we bought an investment that we're not going to see a return on. That's happening a lot. You'll see right now that there's a dramatic shift in the willingness of the providers in the marketplace to purchase these policies.

That has actually impacted the whole market itself because you think about inventory, there's a lot of inventory out there of policies that have been "manufactured" and the industry is now staying away from that, meaning the secondary market because it's tainted. We're getting back to basics. We're

getting back to using what I talked about throughout the whole presentation, of the marketplace being used as a problem-solving tool more so than anything else.

I will tell you that coming from the insurance roots, we believe in insurance. When someone has a policy that they need and it's efficient, we believe they should retain it. We find situations where clients are very unhealthy and we make recommendations for them to retain the insurance, but obviously clients will do what they want to do and we want to be able to provide the options for them.

We've been responsible for purchasing close to \$13 billion of insurance for consumers. The one thing that we're most proud of is out of the \$13 billion of face amount, we provided over \$2 billion of capital above cash value to those clients. To me that's where the value is. It's the value that we're providing back to your clients in terms of the excess capital that you can utilize for planning.

Q. Is everyone familiar with the tax ramifications to the trust or policy owner during this transaction?

A. There are varying opinions. Obviously we're not tax advisors by any means. In the traditional life settlement where you're selling a policy for cash, typically advisors look at it as a three-prong approach. They'll look at their basis as a push. If the cash value is above the basis, that's ordinary income. If their purchase price, if our purchase price is above surrender value which it has to be to be meaningful, then advisors are looking at that as a long term capital gain. So it's a three tier process. But again, we're not tax consultants. Many of our cases are actually return of basis because of how poorly performing the policies were originally especially on replacements.

Q. For a whole life policy, is it kind of a rule of thumb that you're just not interested at all?

A. No, we are. You're just not going to find the same kind of value in those policies traditionally that you will with UL. The reason for it is you think about UL in the structure. We can figure it out and we'll reengineer a policy to figure out how to pay the bare minimum premium. Mock it like a term policy. You can't do that with a whole life policy. The structured guaranteed premium, and because of that it requires a higher outlay. Many of them are rich with cash. Look at the policies in the marketplace that are very good whole life policies, the Northwestern and Mutual policies. We can't beat cash anyway because the cash in the policy is so high relative to the death benefit. But there are policies

out there that we purchase on a whole life basis that we were able to beat the cash.

As a matter of fact the biggest case I worked on my first couple of years at Coventry was a case where it was a business owner who owned about five or six different whole life policies, some were term blended, some weren't. They wanted to transfer the business to their children. They didn't want to wait until the succession plan kicked in which was when they passed away the policy proceeds would help the children buy back into the business. They ended up selling those policies. It was a total of \$52 million of insurance. I think the cash value if I remember the case was about \$17 million and we ended up buying the policies for about \$24 million. That was used to start the succession plan today rather than later.

Q. On a whole life, would it be better if it's blended versus

A. Sure, because it would be mocked like a UL. The only issue would be the, and I've been involved in a lot of term blends through my career, would be the volatility of the term rates escalating. The typical term blends that are structured well, that have paid up additions flooded in with them to help usually price well.

Q. I would think an annualized premier product might be a good one to look at, net pay versus

A. It's funny you say that because there are a lot of cases I remember working on in my past that are coming in the door, and they are the term blend cases from life. Not picking on the company, but they had what was called the life plus riders, life plus one, life plus two, which really mocked a paid up addition term blend scenario and it makes it look like a UL policy. We definitely will look at those policies.

Q. Explain a little more the term conversion and how that works.

We don't. Some do.

Thank you very much.