The Economist

Reprinted from the issue of May 17, 2003.
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Finance and economics

Insurance

New lease on life

NEW YORK

The secondary market in life-insurance policies is good for consumers

AFTER savings accounts and government bonds, life insurance may be the most respectable of investments. It was not always so. Until the British parliament passed the Gambling Act in 1774, which banned policyholders from insuring the lives of people with whom they had no documented connection, many life policies were straight bets on whether somebody-a member of the royal family, say-would would live or die.

Now, in a faint echo of those times, a secondary market in life-insurance policies is going rapidly in the United States. Firms buy policies, mainly from older people, at discounts to their face value. They pay all subsequent premiums and collect the proceeds on the death of the insured or the maturity of the policy.Such "life-settlement" firms bought $2 billion-worth of policies (by face value) last year, ten times as much as they acquired in 1998. The industry's potential-Americans aged over 65 have life cover with perhaps $500 billion-has attracted such investors as General Re, a subsidiary of Warren Buffett's Berkshire Hathaway.

Hitherto, elderly American with policies they do not need or cannot afford to keep up have had little option but to let the policies lapse or sell them back to their insurers. Plenty seem glad to have an alternative buyer. No wonder, when on average they can get three times as much from life-settlement firms as they can from their original insurers.

However, the life-settlement business still has to overcome several obstacles. One problem is that its reputation is tainted by association with the viatical industry, which bought the life-insurance policies of the terminally ill, usually with AIDS, and in which fraud was common.

In addition, some like insurers see the life-settlement business as a direct threat. Should the secondary market expand, the proportion of policies that lapse - and on which insurers pay no claims - would drop. Insurers would then have to pay more out. Their profits would hall and premiums would probably rise. So a handful of life-insurance firms are trying to hamper the life-settlement firms' growth by prohibiting their insurance agents from discussing them with clients and by making policies non-transferable.

The legality of such moves is not clear. It is not certain, says Rick Cortese of National Regulatory Services, a consulting firm, that insurance agents have a fiduciary duty to their clients, as brokers selling securities do - or, if they have such a duty, whether it obliges them to discuss life settlements. New rules being drafted by state insurance regulators would explicitly allow agents to talk to clients about life settlements but would not insist on it. On the transferability question, some states permit insurers to write policies that cannot be sold on. Others, such as North Carolina, Florida and Louisiana, do not.

The economic argument, however, is plain. Before the life-settlement industry grew, life-insurance companies were the sole buyers of unwanted policies. Now consumers have a choice, and the chance to get more if they cash their policies in. And so what if the life-settlement firms profit from their death? Unlike their 18th-century forebears, the policies' buyers have at least asked permission. ■

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