

the INSURANCE FORUM®

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... for the unfettered exchange of ideas about insurance

Vol. 35, No. 1

January, 2008

OBSCENE COMMISSIONS FOR INTERMEDIARIES IN THE SECONDARY MARKET FOR LIFE INSURANCE POLICIES

Life insurance agents, agency managers, general agents, and field marketing organizations are in the business of selling life insurance. Life settlement brokers and other intermediaries in the secondary market for life insurance policies are in the business of “unselling” life insurance. Some commissions paid to life settlement brokers and other intermediaries in the secondary market are obscene, and dwarf the commissions paid to agents and others who sell life insurance.

The question of whether the secondary market is part of the business of insurance has been debated for years. Some courts have ruled that secondary market transactions do not constitute the business of insurance. However, the U.S. Court of Appeals for the Fourth Circuit recently ruled that secondary market transactions, because they significantly change the relationship between the policyholder and the insurance company, constitute the business of insurance for purposes of the McCarran-Ferguson Act. The recent decision is discussed in our July 2007 issue.

Life Partners, Inc. (Waco, TX), a secondary market intermediary that is a party in the Fourth Circuit case, has long argued that secondary market transactions do not constitute the business of insurance, and that a secondary market intermediary does not have to be licensed in a state to conduct business there. Life Partners says that efforts by state insurance departments to regulate the secondary market interfere with interstate commerce, and that secondary market intermediaries, for purposes of McCarran-Ferguson, are not engaged in the business of insurance.

Emergence of the Secondary Market

My first article about the secondary market for life insurance, entitled “A System for the Exploitation of

the Terminally Ill,” is in our March 1989 issue. I wrote about Living Benefits, Inc. of Albuquerque, New Mexico (the firm no longer exists), and their offer to buy life insurance policies from terminally ill insureds. The firm said it had raised \$102 million of capital, but it had not yet purchased its first policy. I wondered about the marketing of the firm’s “service for the terminally ill,” as the firm characterized it, and asked one of the principals whether the firm intended to compensate agents or brokers who refer terminally ill insureds to it. He said it would be inappropriate to pay compensation, and the firm did not intend to do so.

Evidence of Obscene Commissions

Today obscene commissions are sometimes paid to life settlement brokers and other intermediaries in the secondary market. I first wrote about such commissions in our June 2000 issue. Data were drawn from the financial report for 1999 filed with the Florida insurance department by Accelerated Benefits Corporation (Orlando, FL). The article includes a table showing information on each of the 75 cases listed in

CONTENTS OF THIS ISSUE

Obscene Commissions for Intermediaries in the Secondary Market for Life Insurance Policies	1
Larry King’s Lawsuit against an Insurance Agent Relating to a Pair of 2004 Transactions in the Secondary Market.....	3
The <i>National Underwriter</i> Magazine and the Secondary Market for Life Insurance Policies	6
Another Proposed Alternative to the Secondary Market for Life Insurance Policies	7
Warren Buffett’s Losing Bet against the Boston Red Sox	8

the report. Three of the cases were not completed, and no commissions were shown in four others.

In the remaining 68 cases, commissions paid to the brokers ranged from 3.0 to 10.4 percent of the *face amount*, with an unweighted average of 6.8 percent, and were 6 percent or higher in 57 cases. Expressed in another way, commissions paid to the brokers ranged from 5.9 to 70.2 percent of the *payment to the terminally ill insured*, with an unweighted average of 15.1 percent, and were 10 percent or higher in 54 cases. Many of the latter percentages would be substantially higher if expressed more logically in relation to the amount by which the payment to the insured exceeded the cash value of the policy.

I was surprised by the size of the commissions, in part because I had not seen information on commissions prior to that time, and in part because one of the principals of the first firm in the secondary market had said the payment of any compensation would be inappropriate. I said in the June 2000 article that the commissions paid to the life settlement brokers dwarfed the commissions paid to the agents who had sold the policies. I raised questions about the motivations of the brokers, and about whether terminally ill insureds were being shortchanged.

The New York Attorney General's Complaint

In October 2006, Eliot Spitzer, the New York attorney general at the time, filed a complaint against Coventry First LLC (Fort Washington, PA), the largest secondary market intermediary. The complaint alleges that Coventry often engages in bid rigging by paying a life settlement broker an undisclosed "co-broker fee" to cause the broker to "sit on" or reduce a competitive bid from another potential purchaser;

often provides a broker with an undisclosed "gross offer," which is a lump sum divided between the broker and the insured at the discretion of the broker; often requires the broker to sign an agreement providing a "right of last offer" for Coventry; and in some cases generates false documents to conceal from the insured all or a portion of the broker's compensation. The complaint is discussed in our January/February 2007 issue, and a recent court ruling about the complaint is discussed in our December 2007 issue.

The New York attorney general's complaint suggests that secondary market intermediaries are paid unconscionable commissions, in at least some instances. In one case, Coventry and a broker *each* received more than the amount paid to the insured!

Developments in Florida

In the wake of the New York attorney general's complaint, the Florida office of insurance regulation (OIR) began an investigation of Coventry's practices in Florida. In May 2007, the OIR issued an order to show cause containing allegations similar to those in the New York complaint. In September 2007, the OIR issued a consent order ending the investigation. The Florida developments are discussed in our December 2007 issue.

One aspect of the Florida consent order relates to the compensation paid to secondary market brokers. Coventry agrees to pay, to all brokers involved in any single transaction, combined compensation of no more than one-third of the gross offer. Consider, for example, a case where the cash value is \$600,000 and the gross offer is \$1.2 million. Coventry agrees to pay, to all brokers in the transaction, combined compensation of no more than the unconscionable figure of \$400,000 (one-third of \$1.2 million).

When an insured surrenders a policy to the company that issued it, no one is compensated for obtaining the cash value. Thus the only "service" the secondary market provides to the insured is obtaining more than the cash value. The brokers' compensation of \$400,000 is two-thirds of the amount by which the gross offer exceeds the cash value!

Further, the insured receives \$800,000 (the gross offer of \$1.2 million minus the brokers' compensation of \$400,000), which exceeds the cash value by only \$200,000. Thus the brokers' compensation is twice the amount received by the insured in excess of the cash value!

Still further, the consent order is silent on the compensation paid to Coventry. Suppose Coventry receives what is described in the New York attorney general's complaint as a "customary" fee of \$400,000 before transmitting the \$1.2 million gross offer to the brokers; in other words, the total offer before deducting Coventry's fee is \$1.6 million. In that case, the combined compensation received by all the intermediaries is \$800,000, or four times the \$200,000 received

The Insurance Forum, an independent periodical, is published by Insurance Forum, Inc., P. O. Box 245, Ellettsville, Indiana 47429. Telephone (812) 876-6502. www.theinsuranceforum.com. ISSN 0095-2923. The subscription price is \$120 per year.

A single reprint of this 8-page January 2008 issue is \$10. Reprints are \$7.50 each for orders of at least 2 reprints sent in one shipment, \$5 each for at least 10, and \$4 each for at least 25. Further discounts apply to orders of at least 100 reprints of the issue.

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by the insured in excess of the cash value! It would be interesting to observe the insured's reaction should he or she become aware of the combined compensation received by all the intermediaries for the "service" they perform for the insured.

Conclusion

Since the secondary market for life insurance in the U.S. emerged from the shadows in 1989, it has evolved from zero compensation for intermediaries to obscene compensation for intermediaries. It is now fair to say the market is driven by the greed of intermediaries. Agents and others in the life insurance business are lured into the "unselling" of life insurance by commissions far larger than what agents receive for selling the product in the primary market. The unconscionable commissions are paid even

though it is easier to persuade an insured to dispose of a policy, receive a payment in excess of the cash value, and be relieved of future premiums, than it is to persuade a prospect to buy a policy and commit to paying future premiums.

Thus far, the most horrifying type of secondary market transaction is speculator initiated life insurance (SPINLIFE). In such a transaction, a prospective insured is bribed—with cash, free life insurance, or some other item of value—to apply for a policy where the intent is to sell the policy in the secondary market either immediately or soon after the policy is issued.

The effect of the secondary market in general and SPINLIFE in particular is to convert life insurance into a traded commodity. As discussed in some of my earlier articles, that conversion may cause dire consequences for the life insurance business.

LARRY KING'S LAWSUIT AGAINST AN INSURANCE AGENT RELATING TO A PAIR OF 2004 TRANSACTIONS IN THE SECONDARY MARKET

Larry King, a television talk show host who lives in Los Angeles, filed a lawsuit in federal court there on October 22, 2007. The defendants are Alan L. Meltzer, an insurance agent in Bethesda, Maryland; The Meltzer Group, Inc.; and "Does 1-10." (*Larry King et al. v. Alan Meltzer et al.*, U.S. District Court, Central District of California, Case No. CV-07-6813.)

The lawsuit involves a pair of 2004 transactions in the secondary market for life insurance. One of them is speculator initiated life insurance (SPINLIFE), or stranger originated life insurance (STOLI). The lawsuit was reported in the general media and in the insurance trade press. However, the articles omit many details and do not mention some important questions raised by the case.

The Complaint

In the fall of 2002, according to the complaint, Mr. King bought three life insurance policies with a combined face amount of \$10.5 million. He "was not in optimal health at the time." The policies were placed in a 2002 trust for the benefit of family members, including his wife, who is "several years younger" than he is, and two minor children. He was "assisted" in acquiring the policies by Dennis J. Gilbert of Gilbert Krupin, a Beverly Hills, California agency of AXA Equitable Life Insurance Company. One of the policies was for \$5 million. The complaint does not identify the companies that issued the policies.

The SPINLIFE Transaction

In early 2004, according to the complaint, the defendants entered the picture without consulting Mr. Gilbert. The defendants advised Mr. King to buy a new \$10 million policy on his life and immediately resell it; thus the defendants advised a SPINLIFE

transaction. When the policy was issued, it was placed in the "LK 2004 Trust dated February 12, 2004." The complaint does not identify the insurance company that issued the policy. Within a few weeks, the defendants "advised and caused the beneficial interest in the LK 2004 Trust to be sold to a buyer named HTF Master Trust 2004-1." Mr. King received \$550,000 for selling the policy in the secondary market. According to the complaint, the defendants said that it was "a good economic and insurance decision" to sell the policy in the secondary market, and that \$550,000 was "a good price" and "the best price that could be obtained."

The complaint alleges that selling the policy in the secondary market was "disadvantageous" to Mr. King and a breach of the defendants' "fundamental fiduciary duties." Here are some points and allegations in the complaint: Mr. King's "age, health, and overall financial condition" were relevant, more could have been obtained by selling the older policies, selling the new policy caused unfavorable income tax consequences, \$550,000 was not "a good or fair sale price," the new policy had lower premiums than the older policies, there was no disclosure of the identity of the buyer of the policy, and there was no disclosure of the commissions paid to the intermediaries.

The Replacement Transaction

In late 2004, according to the complaint, the defendants advised Mr. King to dispose of the old \$5 million policy and replace it with a new \$5 million policy. The defendants arranged for a new \$5 million policy owned by Mr. King's 2002 trust. The complaint does not identify the insurance company that issued the policy. Within two weeks, the defendants arranged the sale of the old \$5 million policy in the

secondary market. Mr. King received \$850,000 for selling the old policy in the secondary market.

According to the complaint, Coventry First LLC (Fort Washington, PA), the largest secondary market intermediary, was involved in the sale of the old \$5 million policy. The complaint also mentions the New York attorney general's complaint against Coventry.

According to the complaint, the defendants said that it was "a good economic and insurance decision" to sell the old \$5 million policy, and that \$850,000 was "a good price" and "the best price that could be obtained." The complaint repeats many of the points and allegations mentioned above relating to the early 2004 SPINLIFE transaction.

The 2007 Evaluation

At a "social function" in early 2007, according to the complaint, Mr. King met Mr. Gilbert, the agent who had "assisted" in the 2002 purchases. Mr. King told Mr. Gilbert about the 2004 transactions, and Mr. Gilbert offered to review them. After doing so, he expressed concerns about their appropriateness. Mr. King then retained counsel "to provide an independent evaluation" of the 2004 transactions. In the course of the evaluation, difficulties were encountered in obtaining information supporting the defendants' recommendations. Mr. King then filed his lawsuit seeking general, special, and punitive damages, costs, and the imposition of a constructive trust.

According to the complaint, Mr. King and his attorney in 2004 were not aware of the alleged misconduct of the defendants at that time. Thus the complaint says any statute of limitations did not begin to run until the 2007 discovery of the alleged misconduct.

Commissions for Intermediaries

The complaint mentions but contains no solid information about the commissions received by the defendants and the other secondary market intermediaries involved in the 2004 transactions. The failure of the defendants to disclose the information apparently was a factor in the decision to file the lawsuit.

Commissions for secondary market intermediaries are discussed in the lead article in this issue. This case, however, involves not only a conventional secondary market sale in late 2004, but also a SPINLIFE transaction in early 2004 and the purchase of a replacement policy in late 2004. Thus the defendants received intermediary commissions in connection with secondary market sales of a new \$10 million policy and an old \$5 million policy, and also agents' commissions in connection with purchases of a new \$10 million policy and a new \$5 million policy.

Missing Details

The discussion above mentions some important details that are missing from the complaint. Many other important details are also missing from the

complaint. Among them are the types of life insurance policies involved, the cash values, if any, the dividends, if any, and the premiums, including any extra premiums charged because of Mr. King's health.

Mr. Meltzer's Statement

I wrote to Mr. Meltzer and invited him to comment on Mr. King's lawsuit. A spokeswoman said: "The litigation is completely without merit. Mr. Meltzer will defend himself vigorously and looks forward to his day in court."

Massachusetts Mutual's Statements

Mr. Meltzer is a top agent of Massachusetts Mutual Life Insurance Company, which is not a party in the lawsuit. I invited a company spokesman to comment on the lawsuit and indicate the company's views on the secondary market. He sent two statements:

- **This litigation does not involve MassMutual in any way. MassMutual is not named in the lawsuit, nor are MassMutual (or any affiliate) policies the subject of the dispute. So therefore, it would not be appropriate for us to comment. Any questions should be directed to the litigants.**
- **MassMutual strongly disapproves of Stranger Originated Life Insurance (STOLI) and will not knowingly approve or issue any life insurance application that it reasonably suspects is STOLI. What is important is that this lawsuit points to an issue—STOLI—that requires greater legislative and regulatory attention. MassMutual has been working hard on a life insurance industry effort to address STOLI abuses through legislative and regulatory action.**

National Financial Partners

National Financial Partners Corp. (NYSE: NFP), which is not a party in the lawsuit, owns several of Mr. Meltzer's firms. In its 10-K report for 2006, NFP describes itself as "a leading independent distributor of financial services products primarily to high net worth individuals and companies." The 10-K also contains this sentence:

NFP currently has relationships with many industry leading manufacturers, including, but not limited to, AIG, AIM, Allianz, Allstate, American Funds, American Skandia, Assurant, AXA Financial, Boston Mutual, Century Healthcare, Fidelity Investments, Genworth Financial, The Hartford, ING, Jackson National Life, John Hancock USA, Jefferson Pilot, Lincoln Benefit, Lincoln Financial Group, Lloyds of London, MassMutual, MetLife, Nationwide Financial, Oppenheimer Funds, Pacific Life, Phoenix Life, Principal Financial, Protective, Prudential, Securian, Standard Insurance Company, Sun Life, Transamerica, United Healthcare, UnumProvident, West Coast Life and WM Group of Funds.

I wrote to Jessica M. Bibliowicz, chairman and chief executive officer of NFP, and invited her to comment on Mr. King's lawsuit. I received no reply.

Coventry's Statement

On November 5, when articles about Mr. King's lawsuit started appearing in the press, Coventry issued a statement. Coventry said that it "did not purchase the \$10 million contract described on page 4 of the lawsuit," and that the "purchase and immediate sale of the \$10 million policy is a type of transaction that Coventry opposes." However, the complaint does not say Coventry was involved in the sale of the new \$10 million policy in the secondary market in early 2004; rather, the complaint says on page 7 that Coventry was involved in the sale of the old \$5 million policy in the secondary market in late 2004.

In its statement, Coventry avoids mentioning the secondary market transaction in late 2004. It is reasonable to conclude that Coventry was involved in that transaction, as the complaint asserts.

Some Important Unanswered Questions

The complaint mentions Mr. King's health. Did the insurance companies follow appropriate underwriting procedures in connection with the three policies totaling \$10.5 million of life insurance issued in 2002, the \$10 million policy issued in early 2004, and the \$5 million policy issued in late 2004?

When the \$10 million policy was issued in early 2004, presumably the "LK 2004 Trust" was designated the owner to conceal from the insurance company that the policy was part of a SPINLIFE transaction, and that there was no insurable interest. Who paid the first premium? When the ownership was changed to the "HTF Master Trust 2004-1" within a few weeks after the policy was issued, did the company try to rescind it based on intentional concealment of the lack of insurable interest?

How much did each of the defendants and other intermediaries receive in commissions relating to the 2004 transactions? If the combined commissions exceed the before-tax cash of \$1.4 million Mr. King received (\$550,000 from the secondary market sale of the \$10 million policy and \$850,000 from the secondary market sale of the old \$5 million policy), was the primary purpose of all the 2004 transactions to improve his financial situation, or was the primary purpose to generate commissions?

The Defendants' Motion

On November 9, the defendants filed a motion to dismiss and requested an award of attorneys' fees and expenses. The "preliminary statement" included in the defendants' motion is in the box below.

The defendants take the position that Mr. King's advisors were responsible for the actions taken, and that they rejected many suggestions the defendants made. The defendants deny many of the allegations, "are without knowledge or information sufficient to form a belief as to the truth or falsity" of many of the allegations, and admit a few minor points.

The motion identifies attorney Mark Barondess, Mr. King's personal and business advisor; Gregory M. Bell, Mr. Barondess's brother-in-law; John B. O'Grady, Mr. King's estate planning attorney; David Blouin and Robert Cinelli, Mr. King's business managers; consultant Jerri Turley; and insurance agents Mr. Gilbert and Michael Krupin. The motion, like the complaint, does not identify the companies that issued the policies.

Conclusion

Before the 2004 transactions, Mr. King had \$10.5 million of life insurance. After the transactions, he still had \$10.5 million of life insurance, and also had the before-tax cash of \$1.4 million. Whether his financial position was improved or worsened by the

PRELIMINARY STATEMENT IN DEFENDANTS' MOTION IN THE LARRY KING CASE

(November 9, 2007)

Larry King's Complaint is fraught with misstatements of fact and law. First, Larry King pretends that Defendants were his "trusted insurance agent engaged to protect him and his family," when, in fact, Larry King had virtually no contact with Defendants and consistently relied upon a team of independent professionals and financial advisors who not only approved the transactions Larry King complains of, but issued opinion letters confirming the validity and legality of the transactions. In fact, Larry King expressly represented that Larry King and his trust have "consulted with and received advice from attorneys, accountants and/or financial advisors of their choosing to the extent they have deemed such advice necessary in order to satisfy

themselves that . . . consummating the transactions contemplated . . . is in their best interest."

Second, Larry King pretends that he was interested in purchasing additional life insurance. In fact, and as the evidence will prove, Larry King was unwilling to spend money to purchase additional life insurance beyond his initial purchase in 2002. During each of the transactions complained of, Defendants expressly told Larry King's advisors that Larry King was better off keeping the new insurance rather than selling. But Larry King refused to assume the cost of more insurance premiums. Larry King was, however, very interested in selling his insurance on the marketplace at a substantial profit. This is what happened.

transactions can be determined only by a thorough analysis of the price structure of all the policies, including those he sold in the secondary market.

In addition to the \$10.5 million of life insurance Mr. King still has, two policies totaling \$15 million of life insurance are in the hands of speculators who want him dead. Whether that concerns him, and whether the \$1.4 million is adequate compensation for any such concerns, are difficult questions.

The two policies totaling \$15 million of life insurance in the hands of speculators reduce Mr. King's

capacity to buy life insurance in the future. Whether that is a significant consideration cannot be determined without careful consideration of his health and a thorough analysis of his finances.

The complaint refers repeatedly to the fiduciary obligations of the defendants. Courts have often ruled that a life insurance agent does not have fiduciary obligations to his or her prospects and policyholders. Thus it may be difficult for Mr. King to establish that the defendants breached their "fundamental fiduciary duties" to him.

THE NATIONAL UNDERWRITER MAGAZINE AND THE SECONDARY MARKET FOR LIFE INSURANCE POLICIES

National Underwriter is a weekly insurance trade magazine that has been published continuously for more than a century. The content of a recent issue shows that the young secondary market for life insurance has become a major focus of the magazine.

The Advertisements

National Underwriter publishes prominent advertisements for many intermediaries in the secondary market for life insurance. For example, six such advertisements are in the October 8, 2007 issue of the

magazine's life/health edition. Their purpose is to lure agents into the lucrative secondary market. The advertisements are listed in the box below.

The Editorial

Steve Piontek is editor-in-chief of the magazine. His editorial occupies two-thirds of page 4 of the October 8 issue. He discusses the "fascinating" life settlement business and calls attention to what was then the upcoming October 11 "life settlement roundtable" in the Bahamas sponsored by *National*

NATIONAL UNDERWRITER ADVERTISEMENTS FOR SECONDARY MARKET INTERMEDIARIES

(Page references are to the October 8, 2007 issue of the life/health edition of *National Underwriter*)

Coventry First LLC (Fort Washington, PA)

The inside front cover is a full-page advertisement.

The Lifeline Program (Atlanta, GA)

Page 5 is a full-page advertisement. The firm, also known as Wm. Page & Associates, Inc., was formerly in Fort Lauderdale, Florida. The advertisement features a photograph of Scott Page, founder and president, and actress Betty White. The firm's website says it is "not to be viewed by Texas or Florida residents." The advertisement does not contain that language. *Texas*: In December 2003, the insurance department fined the firm \$40,000 for operating without a license. *Florida*: In January 2003, the insurance department filed an administrative complaint containing serious allegations against the firm. In May 2003, the department issued a consent order; the firm denied the allegations, paid restitution, paid a \$25,000 fine, paid \$9,200 of examination expenses, agreed to change its procedures, and was placed on two years' probation. In March 2005, the firm surrendered its Florida license, agreed not to advertise to Florida residents, and moved to Georgia.

Legacy Benefits Corporation (New York, NY)

Page 27 is a full-page advertisement. It says the firm "can help you reap the rewards" and create "a significant source of revenue for your business." A footnote says:

"This notice is not intended for use by consumers who are interested in selling their life insurance policies." The footnote also says the firm is not able to conduct business in all states, and offers upon request a list of the states where it is authorized. The firm's website says the firm is not yet approved by the Texas insurance department. The advertisement does not contain that language.

Life Equity LLC (Hudson, OH)

Page 30 is a half-page advertisement. It reads in part: "In the secondary life insurance market this year an estimated \$20 billion of life insurance policies will change hands. Gain your client's share."

Abacus Settlements, LLC (New York, NY)

Page 33 is a full-page advertisement.

Life Insurance Settlements, Inc. (Fort Lauderdale, FL)

The back cover (page 44) is a full-page advertisement. It says the firm helps "our partners build a significant profit center." The advertisement lists 35 jurisdictions—including Oklahoma—where the firm is licensed, and 13 other jurisdictions where the firm can do business because licensing is not required. However, the advertisement says the advertisement is not approved in Oklahoma, and the firm's website says the website is not approved in Oklahoma.

Underwriter. He also mentions the magazine's sponsorship of two earlier such roundtables—October 4, 2006 and March 23, 2007—that were featured in special supplements to the magazine.

The Articles

Page 7 of the issue contains a major news article about Coventry First LLC (Fort Washington, PA), the largest secondary market intermediary. (The inside front cover of the issue is a full-page advertisement for Coventry.) The article discusses a consent order issued by the Florida office of insurance regulation and a court ruling about former New York Attorney General Eliot Spitzer's complaint against Coventry. The article, a page long, is entitled "Florida Settles with Coventry as New York Judge Cuts Charges in Spitzer Suit." The article is under the byline of Trevor Thomas, a senior editor of the magazine. The article quotes extensively from Coventry's self-serving press releases, and is slanted in Coventry's favor. The Florida consent order and the New York court ruling are discussed in our December 2007 issue.

Page 31 of the issue contains a major article by Scott Page, president and chief executive officer of The Lifeline Program (Atlanta, GA), which is also known as Wm. Page & Associates, Inc. (Page 5 of the issue is a full-page advertisement for Lifeline.) The article, a page long, is entitled "A Primer for Agents Considering Life Settlements."

Previous issues carried many favorable articles about the secondary market. Some were by staff members of the magazine, and some were by officials of secondary market intermediaries. I do not recall the magazine publishing any articles critical of the secondary market.

ANOTHER PROPOSED ALTERNATIVE TO THE SECONDARY MARKET FOR LIFE INSURANCE POLICIES

As an alternative to the secondary market for life insurance policies, I discussed in our August 2006 issue the concept of a program under which a life insurance company buys out policies that are no longer desired by the company's policyholders. Later I asked 20 companies to comment on the concept of a buyout program. I received three responses; they are in our March/April 2007 issue.

One of the responses was from New York Life Insurance Company, which prefers a "policy preservation program" to help policyholders keep their policies in force. At the time, the company did not provide details, but said it was working on the program. When details of the company's "Access Plus" program became available, I wrote about it in our November 2007 issue.

Larry E. Fondren, CLU, ChFC, FLMI, president of Entre Global Services Inc. (Malvern, PA), recently

General Observations

Some long-time subscribers may recall that *The Insurance Forum* began in large part because of censorship by the insurance trade press. Here are two of 31 incidents I experienced over a period of 12 years. Both involved *National Underwriter*. The individuals' and companies' names are omitted because the incidents occurred about 40 years ago.

National Underwriter published a full-page advertisement for an insurance company. The advertisement was deceptive. I wrote a letter to the editor explaining why the advertisement was deceptive and how to remove the deception. The editor refused to print the letter, citing a "wall" between advertising and editorial/news content.

National Underwriter later published an article written by an insurance agent. He described a technique he was using in sales work, speeches to agent groups, and articles in sales magazines. The technique was deceptive. I wrote a letter to the editor explaining why the technique was deceptive and how to remove the deception. The editor refused to print the letter, citing a need to avoid antagonizing the agent's company.

I believe that officials of the companies involved in these incidents were not aware of the censorship. If they had known, and if they were concerned about the welfare of the business, they would have been angry rather than grateful that the magazine had suppressed discussion of deceptive practices.

We never accept advertising; instead, we rely on subscription and reprint revenue. That is why I refer to *The Insurance Forum* as an "independent periodical," bristle when it is referred to as part of the trade press, and ask readers to buy reprints rather than violate our copyright with unauthorized copies.

wrote to senior officials of numerous life insurance companies about another alternative to the secondary market. The subject of the letter is "New Policyowner Alternative to Life Settlement and STOLI Transactions." The program, called "LegacyLoan," is similar in some respects to New York Life's Access Plus.

LegacyLoan

LegacyLoan involves a loan from a premium finance company. The only collateral is 90 percent of the policy's death benefit. The policyholder receives a lump sum larger than the cash value. The lender also pays all future premiums and adds them to the loan. The policyholder retains ownership of the policy. The loan carries a guaranteed, fixed interest rate (9 percent at present), and no prepayment penalties. The premium finance company transfers the loan to a trust, which works with investment banks to securitize

pools of such loans into “collateralized insurer obligation” (CIO) securities. When an insured dies, the death benefit is used to pay off the loan, including accrued interest. The balance, which is guaranteed to be not less than 10 percent of the death benefit, goes to the beneficiary of the policy.

There is no medical underwriting at the time of the loan. The life expectancy estimate is based only on the insured’s age at the time of the loan and the underwriting classification of the policy when it was issued. The face amount, the future premiums, and the type of policy are taken into account. Built into the calculations is a “risk premium” equal to 15 or 20 percent of the face amount for a reinsurer or financial guarantor to cover the risk of the insured living longer than his or her life expectancy. Also, the premium finance company charges an “origination fee” of 2 percent of the face amount, half of which is for the agent or broker.

To be eligible for the LegacyLoan program, a policy must have a face amount of at least \$1 million, and the insured must be at least aged 75. Any type of policy is eligible: traditional whole life, universal life, variable life, or term life. However, the policy must be at least two years old.

Similarities and Differences

LegacyLoan and Access Plus both involve loans, keep policies in force, and guarantee some death benefits for the beneficiaries. In LegacyLoan, a premium finance company makes the loans; in Access Plus, New York Life makes the loans. LegacyLoan involves risk premiums and origination fees; Access Plus involves neither of those items. LegacyLoan involves any type of policy, a minimum policy of \$1 million,

a minimum age of 75, and no health factors other than the policy’s classification; Access Plus involves only traditional cash-value policies, a minimum policy of \$250,000, a minimum age of 65, and significant deterioration in the insured’s health subsequent to the issuance of the policy.

Conclusion

LegacyLoan is in the public interest because it eliminates the insurable interest problems associated with secondary market transactions, and because it provides greater benefits to policyholders than secondary market transactions. The primary reason for the financial advantage of the program is its elimination of almost all the compensation paid to intermediaries in the secondary market.

Nonetheless, LegacyLoan may not achieve widespread acceptance by life insurance companies for at least four reasons. First, most life insurance companies use lapse-supported pricing; thus they may not embrace a program that eliminates lapses, despite the fact that the program provides greater value for policyholders than is provided by secondary market transactions. Second, the \$1 million minimum face amount narrows applicability of the program; lowering the minimum face amount would necessitate larger origination fees. Third, the minimum age of 75 narrows applicability of the program; lowering the minimum age would necessitate larger risk premiums and perhaps medical underwriting. Fourth, a fee of 1 percent of the face amount for an agent or broker may create conflicts of interest even though it is significantly smaller than the commissions typically paid to secondary market intermediaries.

WARREN BUFFETT’S LOSING BET AGAINST THE BOSTON RED SOX

Warren E. Buffett is chairman and chief executive officer of Berkshire Hathaway Inc. (Omaha, NE). Berkshire owns many insurers, reinsurers, and other firms. Jordan’s Furniture, Inc., which Berkshire acquired in 1999, is a large retail furniture company with several stores in the Boston area.

In early 2007, Jordan’s announced a potential furniture giveaway as part of a “Monster Deal” promotion. It said anyone who bought furniture between March 7 and April 16, and took delivery by July 10, would receive a full refund of the cost of the furniture if the Boston Red Sox should win the 2007 World Series. The Red Sox did so, and customers are cashing in on the promotion.

According to press reports, Jordan’s says it acquired \$20 million of “insurance.” Executives of the firm did not reveal details, but some Berkshire subsidiary probably is involved. I asked a Berkshire spokeswoman one question: “Which of Berkshire’s

insurers wrote the policy for Jordan’s?” She replied: “I checked around and I am unable to get you a response to your question about Jordan’s Furniture.”

Such an arrangement seems to be gambling rather than insurance. The “premium” must be based heavily on odds provided by Las Vegas bookies. I have not asked major league baseball whether a hypothetical Red Sox recruit who moved to the Boston area in time for the promotion and furnished his home with Jordan’s furniture would be subject to disciplinary action for gambling on baseball.

According to press reports, Jordan’s will send 1099s to its customers. It is my understanding that a rebate is viewed as a reduction in price and not taxable, but a giveaway is taxable like a lottery jackpot.

Since one of Mr. Buffett’s companies probably is involved, it may be said he placed a losing bet against the Red Sox. Perhaps he hedged by also betting against the New York Yankees.