

Death's Aftermarket

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Wall Street's fascination with the workings of chance has found a morbid outlet in the exploding market for wagers on how long rich people with big life insurance policies will live.

Wall Street's biggest-money players are vying for a piece of what's estimated to be the \$4-billion-a-year business of life settlements, in which traders snap up unwanted life insurance policies taken out by the wealthy and by corporations on former executives. In this field of high finance, investors hope a policyholder dies before premiums eat up too much of the final payout.

The life settlement's business is a close cousin to the much-maligned viaticals industry, which specializes in buying life insurance policies from the terminally ill at deeply discounted prices. That practice got a bad name in the 1990s, when a number of firms engaged in unscrupulous tactics and were accused of taking unfair advantage of the infirm.

To distinguish themselves from the viaticals crowd, life settlement buyers mainly target wealthy individuals over 65 years old with insurance policies that carry high premiums. Buyers pay an upfront lump sum for these potentially lucrative policies, which the insured might otherwise have allowed to lapse or have sold back to the insurance company for a modest sum.

Some of the big investors in this little-known market are **American International Group** ([AIG:NYSE](#) - [news](#) - [research](#)), **Merrill Lynch** ([MER:NYSE](#) - [news](#) - [research](#)) and **HBK Investments**, a \$5 billion Dallas hedge fund. Others also said to be eyeing the market include billionaire investor George Soros, **Citigroup** ([C:NYSE](#) - [news](#) - [research](#)), **Credit Suisse First Boston** ([CSR:NYSE](#) - [news](#) - [research](#)) and **Millennium Partners**, a New York hedge fund.

While the life settlements market is less ghoulish than the one for viaticals, the risk and reward for investors is much the same. Buyers are betting that in picking up the cost of the premiums, they can outfox the grim reaper and score a big profit. The buyers win if the insured dies sooner rather than later, enabling them to cash in the death benefit.

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Buyers typically focus on policies with death benefits that range between \$250,000 and \$5 million. Investors generally prefer policies that have been in effect for at least two years, covering someone with a life expectancy of fewer than 12 years from the time of purchase.

"The new interest in this is amongst some of the hedge funds that see it as an attractive asset class," says Neil Doherty, a professor at The Wharton School of the University of Pennsylvania, who has studied the life settlements and viaticals market. "The risk levels are partly controllable ... through careful medical screening."

There's so much interest amongst hedge funds that a number have contacted Doherty in recent months about the possibility of serving as a consultant. The professor hasn't accepted any offers yet, but says he's keeping his options open.

Most hedge funds and Wall Street firms don't directly invest in life settlements or get themselves involved in the negotiations with policyholders. Rather, they are the behind-the-scenes financiers for more than a dozen firms that specialize in buying life settlements and viaticals.

People familiar with the business say AIG is one of the main financial backers of **Coventry First**, a Philadelphia firm that's the nation's biggest life settlements buyer. This year alone, Coventry is expected to purchase life insurance policies with \$2 billion in face value. The HBK hedge fund, meanwhile, is providing financing to Ohio-based **Life Equity**, the nation's No. 2 life settlements buyer.

A third big life settlements firm, Minnesota-based Living Benefits Financial Services, got a \$400 million cash infusion two years ago from a subsidiary of Warren Buffett's **Berkshire Hathaway** ([BRKA:NYSE](#) - [news](#) - [research](#)) insurance conglomerate. HBK is an investor in Living Benefits, too.

The hedge funds and Wall Street firms don't like to discuss their involvement in this life-and-death investment strategy. Officials with AIG, Merrill Lynch, HBK and several other firms all either declined comment, or didn't return telephone calls.

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Officials at Coventry aren't as bashful. They say their business is good for consumers because it offers them an opportunity to sell unwanted insurance policies.

"I feel quite passionately about the benefits of secondary market," says Alan Buerger, Coventry's chief executive, who wouldn't discuss his financial backers. "We believe we are creating a market that will benefit consumers because it makes insurance policies more valuable."

The life settlements market is not yet 10 years old and still experiences growing pains.

Some hedge funds have been scared off by the difficulty in valuing life settlements in a portfolio, especially since it can take many years to collect on a policy. It's also been difficult for newer competitors to break into the market, given that Coventry has moved so quickly in dominating the field.

Other investors lament the absence of settlement securitizations, a favorite technique on Wall Street in which the cash flow from lots of individual policies would be pooled for a more predictable return.

To date, there have been only a smattering of securitizations backed by the income from life settlements, and most of those have been under \$100 million. Supporters say that's bound to change as the industry matures and the market gets bigger.

Others say the biggest problem is that investor interest in life settlements is outpacing the available policies to buy.

"There is so much more capital in the market than product right now," says Dan Miller of **Clearwater Settlements**, an upstart life settlements firm. "I think there are opportunities, but it is overheated with dumb money."

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