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MEL MARTINEZ, FLORIDA, RANKING MEMBER

United States Senate
SPECIAL COMMITTEE ON AGING
WASHINGTON, DC 20510-6400
(202) 224-5364

April 6, 2009

The Honorable Mary L. Schapiro
Chairman
Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549

Dear Chairman Schapiro:

As Chairman of the Special Committee on Aging and a member of the Banking, Housing and Urban Affairs Committee, I take seriously my responsibility to protect and advocate on behalf of seniors, particularly with regard to ensuring that seniors are treated fairly in the marketplace and have access to accurate and unbiased information related to their finances. Recently, I have become concerned with some aspects of the rapidly growing secondary market in life insurance. At present, there is little transparency with respect to this market, as well as a significant amount of confusion and variation among state and federal authorities as to the appropriate regulatory approach to the transactions involved. Therefore, the regulatory authority of insurance departments and state securities administrators is inconsistent among states and, in some cases, non-existent.

Until recently, an individual with a life insurance policy who no longer needed it or could no longer afford it had two choices: surrender the policy for its cash value or stop paying premiums and allow the policy to lapse. The emergence of the life settlement industry provides consumers with the alternative of selling their policies to investors for less than the net death benefit, but for more than the cash surrender value. Originally developed as a response to the AIDS epidemic in the 1980s, the life settlement market has experienced exponential growth in recent years. It is estimated that the face value of policies sold to investors had grown from about $2 billion in 2002 to $12 billion in 2007.[1] This is largely due to the tertiary market in life settlements in which investors purchase fractional interests in securitized bundles of policies in a manner similar to the trading of mortgage-backed securities. Industry analysts predict that the potential market will exceed $160 billion over the next few decades.[2]

Legitimate life settlements can provide a valuable option for seniors who no longer want or need their existing life insurance policies, and need cash to pay costly medical bills not covered by Medicare or long-term care expenses. However, recent news reports,[3] complaints by

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[1] Conning Research & Consulting, Inc., *Life Settlements: New Challenges to Growth 2008* (Hartford, Connecticut: 2008).
[2] Ibid.
[3] Matthew Goldstein, "Death Bonds: Inside Wall Street's most macabre investment scheme yet," Business Week (July 30, 2007).

state law enforcement,[4] and notices from investor advocates[5] identify potential risks for both seniors who sell their policies in the secondary market, as well as for seniors and others who invest in these transactions. For example, on the seller side of the transaction, there is potential for seniors to have unexpected tax liability (the Internal Revenue Service has yet to rule on whether any settlement money received in excess of the policy's cash value is a capital gain), loss of insurability, undisclosed commissions or even bid-rigging by brokers, and possible legal liability to their insurance companies in certain circumstances.

Likewise, for most senior investors, purchasing securities backed by life settlements poses substantial risks, which is why life settlement investments are not generally considered suitable for non-institutional investors.[6] The cash flow from a life settlement portfolio can vary greatly depending upon the longevity of the policy seller, the validity of the mortality risk ratings provided to the investor, the credit risk of the insurance companies that issued the policies, and the lack of a strong or consistent regulatory environment.

As you begin to evaluate the SEC's organizational structure and enforcement efforts, I urge you to evaluate the extent to which life settlement providers and brokers should register and disclose their activities to the Commission. As part of this evaluation, SEC should clarify what elements of a life settlement transaction it considers covered by under federal securities laws. The Commission should then take steps to proactively and systematically review the identified elements, and where appropriate, take actions to regulate these products in an effort to increase transparency. Given the significant expansion of the market for these types of investments, the lack of a strong regulatory framework, and the resulting potential for fraud and abuse on seniors selling and investing in these products, it is vital that we take every step to ensure the future integrity of the market.

Thank you for your consideration. I would appreciate a response prior to a Committee hearing we have scheduled regarding life settlements on April 29, 2009. Please contact Cara Goldstein of the Committee's staff on (202) 224-5364 if you have questions concerning this matter.

Sincerely,

Herb Kohl

Herb Kohl
Chairman

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[4] People of the State of New York v. Coventry First LLC et al,, New York Supreme Court, New York County, No. 404620-2006, (10/26/2006). http://www.oag.state.ny.us/media_center/2006/oct/complaint.pdf.

[5] FINRA, Notice to Members 06-38, August 2006.

[6] Leimberg, S., Callahan, C., Casey, B., Magner, J., Reed, B., Rybka, L & Siegert, P. (2008). *Tools and Techniques of Life Settlement Planning*. Cincinnati, OH: The National Underwriter Company.