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CASHING IN

An Insurance Man Builds A Lively Business in Death

As Life Settlements Boom, Banks, Regulators Circle; Betting on Larry King

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FORT WASHINGTON, Pa.—Alan Buerger wants to show investors the upside of death.

The former insurance salesman runs Coventry First LLC, which lets investors essentially bet on—and profit from—other people's demise.

His company is in the business of buying rights to life-insurance policies. In an arrangement known as a "life settlement," Coventry pays the holder a lump sum for the policy now, takes over paying the premiums for as long as the insured person lives, then collects the benefits—generally worth far more—when the person dies. Coventry keeps some of the policies in its own portfolio. It sells others to institutional investors. From an investor's standpoint, as a general rule, the sooner these people die, the better.


Alan H. Buerger

This positions Mr. Buerger at the forefront of a controversial but rapidly growing industry. So far, the life-settlement business involves a tiny slice of the $9 trillion in individual death benefits pending in the U.S. But an industry trade group, the Life Insurance Settlement Association, has grown from 16 member companies at the decade's beginning to 165 today, including major firms such as Deutsche Bank AG.

Now banks including Goldman Sachs Group Inc., Credit Suisse Group and Bear Stearns Cos. want to expand the industry further. In April, these banks helped form the Institutional Life Markets Association to lobby against efforts to restrict the business. Some Wall Street firms are also seeking to buy policies more directly, trying to cut out parties such as Coventry. This year, Cantor Fitzgerald LP set up an Internet-based exchange for those who want to sell or buy policy rights.

Life settlements stir objections, and not only because they make some people squeamish. Some state regulators have called life-settlement terms unfavorable in some cases to policyholders. They've also charged that certain arrangements flout the spirit of laws designed to keep speculators from taking out policies on strangers.

Policyholders, too, have lodged complaints. Television talk-show host Larry King filed a lawsuit in October against a Maryland insurance brokerage, claiming he got a raw deal when he sold two policies on his life, with face values totaling $15 million, for $1.4 million. Among his complaints: With one of the policies, Mr. King says he doesn't know who has a financial interest in seeing him dead.

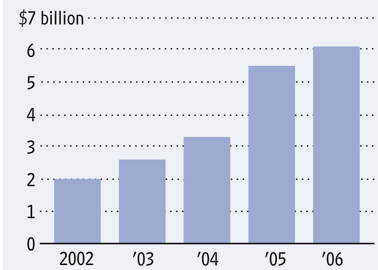
Among the biggest critics are the insurers that issue the policies that make up the life-settlement trade. Some, such as MetLife Inc., say the concept turns what they say should be protection for surviving family members into a vehicle for speculators. Insurers don't generally protest when people sell policies they've held for a long time. But many, such as AXA Equitable Life Insurance Co., a unit of AXA SA, oppose deals in which the policy is purchased with the intent of transferring it quickly to an investor, a phenomenon some call stranger-originated life insurance.

Life settlements also threaten the business model for life insurers. Each year, about 6% of life-insurance policies lapse, according to the Insurance Information Institute, a trade group, as people forget about them or decide they don't need them anymore. Coventry and its rivals raise the prospect that fewer policies will be abandoned, leaving insurers to pay out more in death benefits. Meanwhile, insurers already pay an often-small sum to policyholders who cancel coverage, but they may have to find a way to pay more to compete with life-settlement firms' payouts. "That would drive the premiums through the roof," says MetLife's chief executive, Rob Henrikson.

A battle between the nascent life-settlement industry and insurers is expected to play out over the coming year in individual states, where insurance is regulated and laws covering life settlements are spotty and varied.

Rising Industry

The estimated face value of life-insurance policies that have been purchased in life-settlement deals



Source: Conning Research & Consulting

At the core of the battle is Mr. Buerger. His firm, based in Fort Washington, Pa., has bought the rights to life-insurance policies with face values of $12 billion since 2001, he says. That puts Coventry among the industry's top players: Overall in the U.S., life-insurance policies worth $19.5 billion were traded from 2002 to 2006, estimates Conning Research & Consulting Inc., a Hartford, Conn., firm that tracks the insurance industry. Others believe the figure is higher.

Mr. Buerger won't disclose his privately held company's revenues, though he says they increased fivefold from 2002 to 2006. This year, for the fourth year in a row, he treated Coventry employees and their family members—270 people in all—to an all-expenses-paid trip to Paradise Island in the Bahamas. Coventry gave each traveler a $500 credit to spend on things like fishing trips and restaurants, he says.

Mr. Buerger grew up in the Philadelphia area, the son of a ham-radio equipment salesman who was nicknamed "Ham" Buerger. The younger Buerger first tried selling life insurance in his early 20s, eventually joining the former Shearson firm, where he catered to wealthy clients. He left in 1984 to start running his own life-insurance agency, called Coventry Group.

Now 60 years old, Mr. Buerger has the optimistic demeanor of a polished sales-

(over please)

man. In an interview at Coventry's headquarters in this leafy Philadelphia suburb, he invokes the movie "Field of Dreams," known for the line, "If you build it, they will come." He says: "That's how we see this business."

In the early 1990s, Mr. Buerger sold a controversial product called corporate-owned life insurance (sometimes called janitor's insurance) in which firms took out policies on their employees and collected when they died. In 1996, Congress pared some tax breaks associated with those policies.

He sought new opportunities. He attended a seminar on "viaticals," a strategy popular in the early 1990s that was tailored to terminally ill AIDS patients wanting to sell their life-insurance policies. The development of life-extending AIDS drugs largely put an end to the business.

Mr. Buerger never sold viaticals, but he concluded that the idea of buying life-insurance payouts could be applied to a much larger pool. He reasoned that relatively healthy, wealthy seniors often no longer need policies they may have purchased years earlier, for instance, to benefit now-grown children.

"I felt like I was struck by lightning," he says.

He formed Coventry First in 2000, taking out an $850,000 home-equity loan to make early purchases. It remains a family business: Mr. Buerger is chief executive officer, while his wife, son and daughter-in-law hold senior positions.

Life settlements resonated with older Americans, whose retirement years were stretching longer than many had anticipated. The deals also appealed to policyholders who wanted ready cash for a valuable asset—much like reverse mortgages, which let older homeowners turn their home equity into income that doesn't have to be repaid until they sell their homes or die.

Stephen Ellis needed cash, quickly, when he went over budget on a new house he was building. So the 48-year-old mortgage banker from Annapolis, Md., started shopping two policies, with a combined death benefit of $2 million, that he had taken out on his 75-year-old mother.

Mr. Ellis had been paying $35,000 a year for the policies, he says, but the insurer would have paid him virtually nothing to cash them out. He fielded bids through a life-settlement broker, Chesapeake Financial Settlements LLC, in Rockville, Md. A small firm offered $205,000. He accepted.

"I didn't really look at it as morbid," says Mr. Ellis, who supports his mother financially. "I thought, 'Wow what an incredible way to put a value on this.'" His mother has been in poor health but approved of the sale to benefit him now rather than later, he says. She was unavailable for comment.

Betting on Lives

❖ **The Situation:** The growing life-settlement industry gives policyholders cash for their life-insurance policies, takes over premium payments, then collects benefits when the holders die.

❖ **The Players:** Coventry First is an industry pioneer. Big investment banks are angling for more of the business.

❖ **The Conflict:** Some regulators want to rein in investors who lend seniors money to buy policies that are quickly transferred back to investors.

Some critics say families would generally benefit more by hanging on to the policies. In the Larry King lawsuit, filed in U.S. District Court in Los Angeles, the 74-year-old talk-show host alleges that the Meltzer Group Inc., an insurance brokerage in Bethesda, Md., breached its fiduciary duties.

The complaint alleges that, in 2004, the brokerage advised Mr. King to set up a trust that would buy and then immediately resell a $10 million policy for $550,000. Given Mr. King's age, health and finances, the suit says, he would have been better off keeping the policy to benefit his estate. In part, that's because the sale of the policy generated income taxes. His heirs likely would have taken no income-tax hit, because life-insurance payouts are typically exempt.

The suit also alleges the broker didn't fully disclose commissions and other fees on this transaction and a second one involving a $5 million policy. The suit alleges these charges totaled at least $700,000. That's equivalent to the after-tax proceeds from the $1.4 million Mr. King received for the two policies, says his lawyer, Marshall Grossman.

The suit also alleges that the defendants refused to name the buyer of one of the policies. "The insured never knows if the guy barreling down the highway in a large truck coming in the opposite direction holds the insurance policy on his life," says Mr. Grossman. "We don't know whether the owner is a Wall Street hedge fund or a Mafia don."

In court papers filed this month, the Meltzer Group and its chief executive, Alan Meltzer, said the King complaint "is fraught with misstatements of fact and law" and that Mr. King had full knowledge of any risks. In the filing, the group identified the trust that purchased the policy, but said it is "unaware of the identities of the trust beneficiaries."

A spokeswoman for the group, which is a member firm of National Financial Partners Corp., declined to comment further.

Coventry is identified in the lawsuit as the end buyer of the $5 million policy, but isn't a defendant. "Life insurance is a valuable asset and policyowners should keep their policies," Coventry said in a statement. Life settlements, it says, are for people who for some reason want to drop policies.

Mr. Buerger says the company protects the privacy of its policyholders and sells an interest in policies only to institutional investors. Such parties are generally considered diversified and less desperate to avoid losses on any individual policy should the holder live an unexpectedly long life.

The life-insurance market was once even more freewheeling. In 18th-century England, people took out policies on prominent figures in ill health. The practice was eventually deemed gambling. It led to laws like those in U.S. states today, which generally require that the person who takes out a policy have an established relationship at the time with the insured.

Once purchased, however, the policy is considered property of the policyholder, who is free within certain limits to use it at will. That includes selling to someone else the rights to collect the benefits.

Coventry and other firms controlled by the Buerger family make money by buying up policies and collecting the death benefits, collecting fees on policies they manage for others, and arranging loans to people who want to finance their premiums.

The firm says it pays policyholders on average about three times what insurers pay people who want out of their policies while still alive, the so-called cash-surrender value. Coventry has paid holders more than $2 billion for policies, or nearly 17% of these policies' face value. The cash-surrender values of the policies amounted to $650 million, Coventry says.

Hedge funds and investors, including insurance giant American International Group Inc., have invested in policies Coventry has purchased. Rates of return vary largely depending on when people die, but Mr. Buerger says the compounded rate for the end investor on a portfolio of policies is typically 9% or 10%.

Life settlements appeal to investors' appetite for "uncorrelated" investments—ones that generate steady returns largely independent of the forces swaying stocks and bonds. People die with relative consistency, whether markets are rising or falling. In conferences in recent years, investment banks and ratings agencies have discussed bundling life-insurance policies into securities they can sell to pensions or hedge funds, much as mortgages have been packaged for years.

Life insurers, meanwhile, are on the defensive. Many are lashing out at cases in which investors encourage seniors to take out policies with the chief intent of transferring them to investors as soon as possible. A number of life-settlement firms drum up business by arranging to lend holders money to pay premiums.

Some insurers are increasingly scrutinizing applications before policies are sold, or canceling them before they can be resold. Typically, insurers can rescind a policy unilaterally within the first two years. Insurers are also giving their own policyholders new ways to get upfront cash. New York Life Insurance Co., for one, is offering to lend policyholders money against their future payout, an arrangement akin to a reverse mortgage.

Only about half of U.S. states have life-settlement laws, among them Maryland, Florida and Texas. Most that have the laws require individuals to wait two years before selling a policy to a third party. State officials are sharply divided about whether to keep the two-year rule, or switch to a five-year ban if the insured person is using an outside party's assets to buy the policy. A longer waiting period could make the bet riskier for investors: Though investors may be paying the premiums, if a policyholder dies during that period, the family, not the investors, would get the bulk of the payout.

Authorities have challenged some deals as well. A civil suit by the New York attorney general's office last year alleged that Coventry made secret payments to brokers to lure business away from other life-settlement companies. Florida's Office of Insurance Regulation made similar allegations in an investigation against Coventry announced in May.

A judge threw out much of the New York case this fall, in part because much of the suit didn't involve New York transactions. Coventry says it believes the few remaining claims "have no merit." Coventry settled the Florida investigation, paying no fines but agreeing to cover the investigation's $1.5 million in administrative costs.

Mr. Buerger portrays life settlements as too attractive to policyholders to be significantly curtailed. And he says his firm will thrive amid competition from banks because Coventry has life-insurance expertise that Wall Street lacks.

"They've got the money," he says. "We've got the policies."

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