# The market is open.


Opportunity.

The secondary market for life insurance is changing the face of financial services. Clearly, the secondary market's central premise — that the value of life insurance is best

determined by independent market forces — has been validated by its spectacular growth. But even more significant are the opportunities that the market presents.


THRIVING
MARKETS OWE
THEIR SUCCESS
TO ONE SIMPLE
IDEA. CHOICE.

# A FREE MARKET FOR LIFE INSURANCE.

Life insurance provides solutions to meet various financial needs. Over time however, circumstances can change, and with them the need for insurance.

In fact, nearly seven out of eight universal life policies never mature in a claim. While the right of consumers to sell unwanted insurance to another party was affirmed by the courts nearly 100 years ago, a lack of willing buyers had effectively eliminated the option. Until now.

It was during a visit to London's Royal Exchange in 1844 that Elizur Wright, the nation's first insurance commissioner, witnessed the practice of selling existing life insurance. Concerned by the absence of any regulation of these sales, Wright introduced legislation requiring U.S. insurers to repurchase the policies they issued. He also introduced a formula that defined how much insurers would pay — an amount that came to be known as cash value.

While Wright's reforms were intended to protect the consumer's equity in their life insurance should they ultimately choose to forfeit the policy, the reforms had another less favorable outcome. They created a monopsony.

As a result, policyowners wishing to exit an underperforming policy have had only one buyer — the issuing life insurer. The only way to break the monopsony was to give consumers access to buyers who were willing to pay more than cash value. The secondary market has done exactly that.

**88%** of Universal Life policies never result in a death claim. They are either surrendered, or worse, allowed to lapse.

# Monopsony vs. a free market.

*A monopsony exists when a seller can only sell to one buyer. For more than 100 years,this has been the case in the life insurance industry. Consumers wishing to sell their insurance had only one potential buyer: the company that issued the policy. Consider a similar scenario in the world of real real estate. After living in a house for several years, the homeowners decide to sell, but are told that instead of putting the house on the open market, they must sell it back to the original builder — at the price determined by the builder. The absence of a free market in life insurance has effectively created an anti-competitive environment where depressed valuations andlimited consumer choice are the norm.*

*The secondary market is changing that.*

# 20%

of policies on insureds over age 65 have a market value that exceeds their surrender value.

*— Conning Research and Consulting*

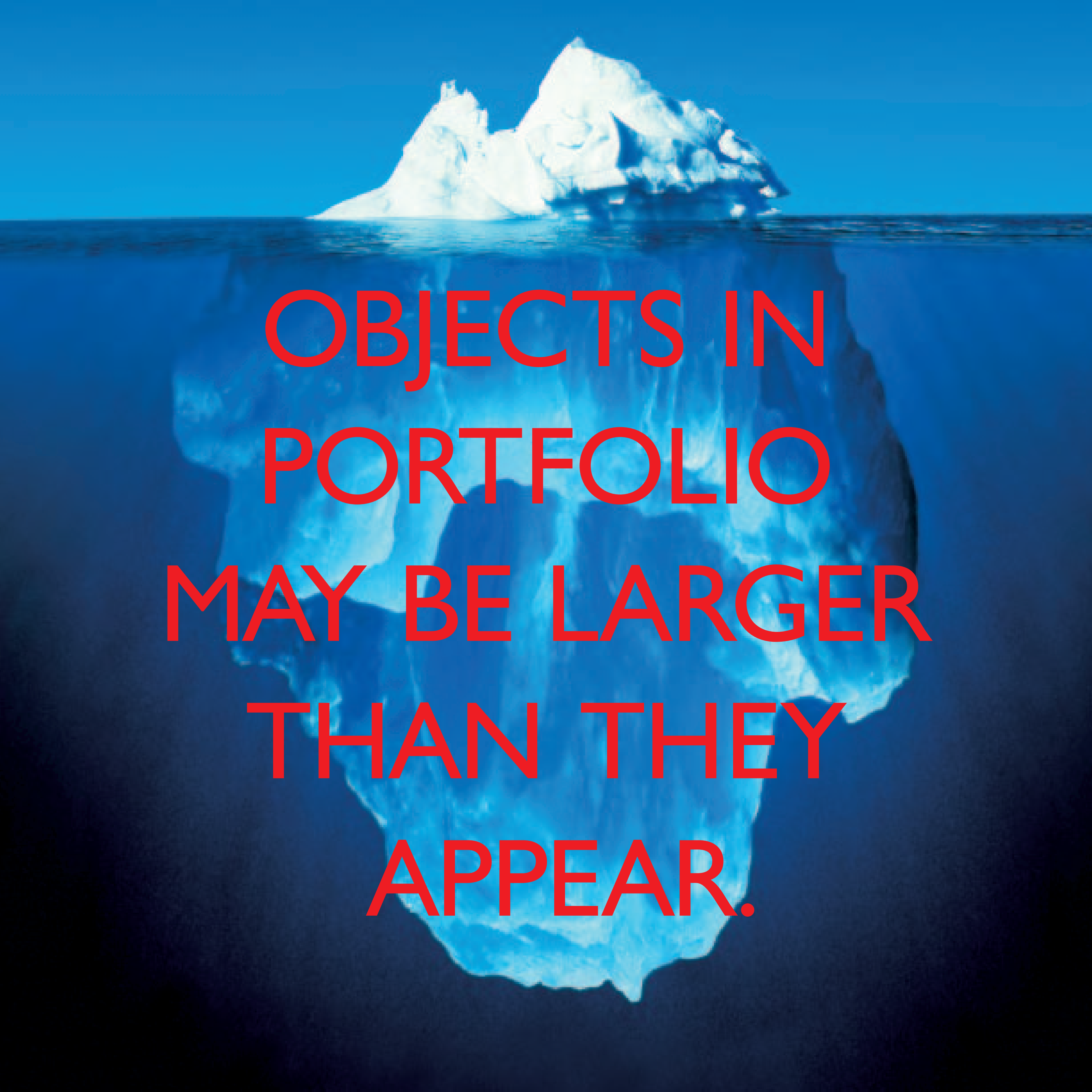
## THE RISE OF MARKET VALUE.

In its simplest terms, a surrender is essentially the sale of a policy back to the insurance company for the cash value. But what if the insured's health has declined since the policy was issued? The same rate class no longer applies and the policy may be worth considerably more than the surrender value. Until recently, if such a policyowner opted out of a policy via a surrender or lapse, the additional value was ceded back to the insurance company. The secondary market gives consumers the option to realize this excess value.

The implications are profound. Like other assets, life insurance now has a fair market value. A policy's worth can now be defined in terms of what buyers would offer in a competitive marketplace. In other words, life insurance has become a fully evolved asseton par with equities, bonds, real estate and other holdings.

## The New Nonforfeiture Values.

*Nonforfeiture values specify the options available to the policyowner in the event of surrender. Their purpose is to provide minimum guarantees based on cash value. However, existing nonforfeiture values as calculated by insurance carriers ignore several key factors, including the health of the insured. As a result, they can dramatically undervalue a life insurance policy. The secondary market, by contrast, provides a free market environment that offers an independent appraisal of the policy. In this way, the secondary market has created a new source of nonforfeiture value that truly reflects the equity of the policy.*


OBJECTS IN PORTFOLIO MAY BE LARGER THAN THEY APPEAR.

## The market has opened unprecedented financial options for consumers.

### Life Settlement

*Enables policyowners age 65 or older to receive fair market value for their life insurance. A solution for clients wishing to reallocate the assets from unneeded or underperforming life insurance.*

### SWAPP℠ (Settlement with a Paid-up Policy)

*Allows policyowners age 65 or older to transfer a policy's market value into a new paid-up policy. Ideal for clients wishing to eliminate premiums while retaining coverage.*

### Variable Annuity Rescue

*Allows consumers age 65 or older to exit a poorly performing variable annuity for an amount in excess of surrender value. An effective exit strategy for clients who don't need the annuity's death benefit.*


# Accessing the market.

As a result, there is an entirely new reality to owning life insurance. Policyowners over the age of 65, working with their advisors, should have their policies appraised, especially when considering a surrender or lapse. Armed with accurate information about what they would likely receive for a policy on the secondary market, consumers can now make educated financial decisions and exercise a new degree of control over their assets.

But the advantages of market value do not end there. The new financial options presented by the secondary market are elevating the value associated with life insurance.

Such is the conclusion of a study by economists at the Wharton School of the University of Pennsylvania. The authors analyzed the effect of a secondary market on three other financial services industries: home mortgages, catastrophic risk insurance and NASDAQ-listed securities. The study noted that secondary markets in these areas created significant benefits for consumers. The authors conclude that the secondary market for life insurance will do the same for life insurance: increase liquidity, spark new product innovations, enhance perceived value and generate a significant expansion of the primary life insurance market.

"If an issuing company does not provide fair value, policyholders will proceed to a secondary market to get a better deal."

— Chief Actuary of a major U.S. insurer, *Best's Review*, June 2000.

**Pinpointing Value.**

*Before the advent of a secondary market, life insurance policies could not readily be sold and it would have made little sense to speak of a policy's fair market value. Fair market value, as defined by the IRS, is the price at which a willing buyer would pay a willing seller, assuming neither is under any compulsion to act. Until now, the concept of a "willing seller" and "willing buyer" of life insurance was theoretical. By its very existence this growing secondary market for life insurance bestows on every policy a fair market value like the owner's other financial assets.*

SECONDARY MARKET CASE EXAMPLE

# Life Settlement

Policy: Term

Insured: Male, age 75

Face Amount: $11 million

Cash Value: **$0**

**Coventry First purchased the policy for $2.75 million.**

DETAILS ▸

**SECONDARY MARKET CASE EXAMPLE**

## Life Settlement

**Details:** As part of his retirement package, a retiring CEO received an $11 million term policy from his company. His financial planner advised him he could assume the premiums, lapse the policy or consider a life settlement. As the client had no desire to maintain the ongoing premiums he chose a Coventry First life settlement for $2.75 million. This enabled him to reach his goal of establishing a trust for his grandchildren.

SECONDARY MARKET CASE EXAMPLE

# SWAPP℠

Policy: Universal Life

Insured: Male, age 83

Face Amount: $4 million

Cash Value: **$520,000**

**Coventry First provided a $2.3 million guaranteed paid-up policy.**

DETAILS ▸

## SECONDARY MARKET CASE EXAMPLE

## SWAPP℠

**Details:** The client wanted to lower his premium payments but maintain the same level of insurance. A traditional 1035 exchange was unable to accomplish his goal.

His advisor recommended SWAPP from Coventry First. SWAPP provided the client with a $2.3 million guaranteed paid-up policy in exchange for the original policy. The client was able to obtain an additional $1.7 million policy for a much lower premium outlay, giving him the total amount of insurance he needed.

SECONDARY MARKET CASE EXAMPLE

# Life Settlement

Policy: Universal Life

Insured: Female, age 87

Face Amount: $6.5 million

Cash Value: **$705,000**

**Coventry First purchased the policy for $2.5 million.**

DETAILS ▸

SECONDARY MARKET CASE EXAMPLE

## Life Settlement

**Details:** The client was still paying premiums in the tenth year of her seven-year vanishing premium policy. She was extremely dissatisfied with the policy performance, but still needed life insurance for estate planning purposes.

Her attorney recommended the policy be appraised by Coventry First to determine its market value. The policy was valued at more than three times the cash value. The agent, who had originally sold her the policy, was able to use the proceeds to provide a better performing policy and re-establish his overall relationship with the client.

SECONDARY MARKET CASE EXAMPLE

# SWAPP℠

Policy: Term

Insured: Female, age 74

Face Amount: $10 million

Cash Value: **$0**

**Coventry First provided a $3.5 million guaranteed paid-up policy.**

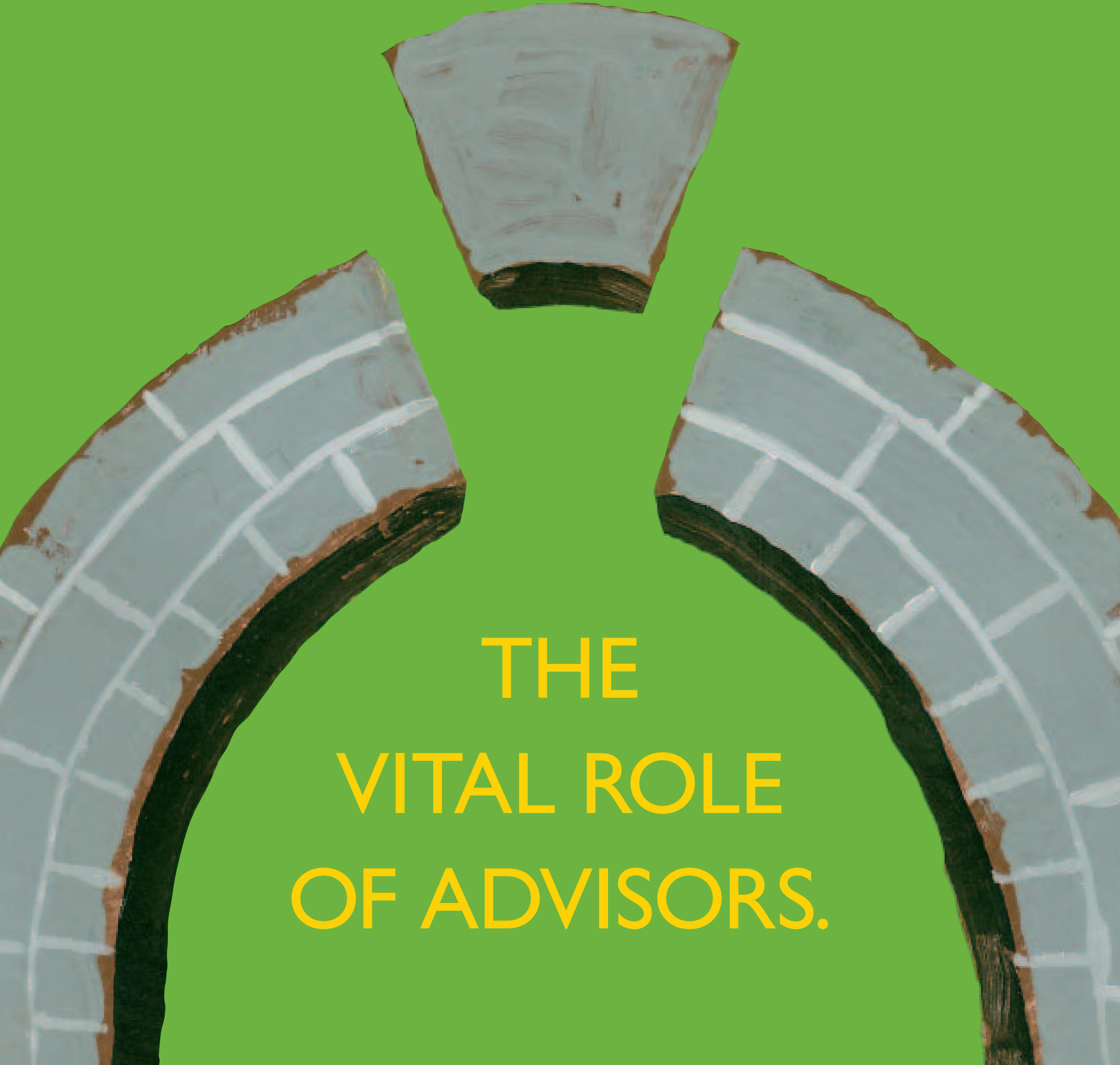
DETAILS ▸

## SECONDARY MARKET CASE EXAMPLE

# SWAPP℠

**Details:** With annual premiums exceeding $300,000, the client was planning to let her $10 million term policy lapse, but she still needed $5 million of insurance to meet her estate planning goals.

Her advisor recommended having the policy appraised by Coventry First to determine its market value. Using the market value, the client was able to SWAPP her term policy, with zero cash value, for a $3.5 million guaranteed paid-up policy. She was then able to obtain a complementary $1.5 million policy maintaining the $5 million of insurance with a sustainable annual outlay.



# THE VITAL ROLE OF ADVISORS.

## EXPANDED OPPORTUNITIES.
## HEIGHTENED RESPONSIBILITIES.

A robust secondary market changes what financial advisors must know and do to help their clients make the most of their life insurance. The possibility that a client's insurance will have a market value well above surrender value has at least three major consequences:

- *When estate planners inventory the market value of a client's assets, they'll need to know the fair market value not only of stocks, bonds and real estate, but of life insurance policies as well.*
- *In advising clients how to exit from any unwanted insurance policy, advisors need to consider whether a secondary market transaction at fair market value is the most suitable choice.*
- *In estimating death taxes, advisors need to consider how the IRS will value any life insurance policies on the lives of others. Will it be at their fair market value?*

65+

All clients 65 and over should have their life insurance appraised. Especially whenever a surrender or lapse is being considered.

In short, the professional or fiduciary obligations of financial advisors now include the need to manage life insurance policies with the same level of attention provided to the client's other financial assets. In cases where a bank or trust company is serving as a trustee, they too must factor the secondary market into their management practice.

**The Fruits of Competition.**

*A recent paper entitled, The Benefits of a Secondary Market for Life Insurance Policies, published by the American Bar Association (Real Property, Probate & Trust Journal, Fall 2003), concludes that the secondary market for life insurance is both pro-competitive and pro-consumer. By allowing companies to compete for a client's underperforming or unneeded policies, the secondary market is generating greater consumer choice and favorable valuations for policyowners, and more opportunities for advisors to serve their clients.*

## Writing Opportunity into Law.

*An article published by the* Journal of Insurance Regulation, *Spring 2003 calls for lawmakers to "encourage participation and investment" in the secondary market through proactive legislation. The National Association of Insurance Commissioners (NAIC) agrees, adopting a decisively pro-consumer stance by designing regulations that guarantee consumer access to secondary market transactions. Increasingly, states are recognizing the consumer's right to know about and access the secondary market.*

"What is the liability of the trustee who allows a thinly funded policy to lapse if the policy had a value in the aftermarket?"

— Estate Attorney, *Journal of Financial Planning*, January 2001.

## ENSURING ACCESS. PROTECTING PRIVACY.

With an eye to the opportunities provided by the secondary market, additional steps are being taken to ensure that the market has a solid foundation from which to grow. An important factor in sustaining this growth is the issue of regulation. A number of states are in the process of passing legislation designed to further protect the consumer's rights in the secondary market. Specifically, these include the right to be informed about the opportunities presented by the market, the right to access the market and the right to privacy throughout the transaction. Such legislation is sending a clear message to financial advisors that secondary market offerings are more than a permanent feature of sound financial planning, they are now part of their fiduciary responsibility.

The market's growth is also drawing the attention of capital markets. High-quality institutional funding from leading investment firms is pouring into the secondary market. The importance of this cannot be overstated. As the market expands, institutional backing provides the foundation of a secure funding source. In addition, it carries stringent requirements for security and confidentiality that offer unmatched protections for consumers.


A LASTING MARKET
BUILT ON UNSWERVING
PRINCIPLES.


THIS CHANGES

# EVERYTHING.

The impact of the secondary market is nothing short of profound. Life insurance is far more valuable than ever before, offering consumers new power to plan for the future and new levels of financial freedom. Quite simply, everything is different. Life insurance is being redefined. And it will never be the same.

COVENTRY FIRST

Coventry First bridges insurance and capital markets to open new opportunities for consumers. The company created the secondary market for life insurance and pioneered the resulting life settlement industry. Fueled by bold ideas, a deep understanding of life insurance, and impeccable standards, Coventry First continues to lead the market by providing powerful new tools for consumers and the financial professionals who serve them.

7111 Valley Green Road    Fort Washington, PA 19034-2209    877-836-8300    **coventry**first**.com**