

# U.S. Structured Finance Newsletter

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## MEDICAL UNDERWRITING IN LIFE SETTLEMENT TRANSACTIONS

Medical underwriters provide an evaluation of the health conditions of the insured based on medical records and history. They also establish a life expectancy estimate, a mortality rating and a confidence level that are applied to base mortality tables in addition to a primary-disease category (necessary to determine and maintain the concentration limits or diversity of the deal structure). Life expectancies are developed from the insured's medical files, which are submitted to the provider by the broker or agent then forwarded to the medical underwriter. Issuers typically require the provider to engage the services of at least two independent medical underwriters to evaluate the life expectancies of the insureds.

Medical underwriting firms utilize a debit/credit system designed to assess medical data and measure the excess mortality associated with a specific impairment. The system assigns a certain number of debits/credits for each impairment and also assigns a varying number of debits/credits based on the severity of the ailment and overall health condition of the individual. The debit/credit system provides a quantifiable decision process of weights of various "good" and "bad" health factors. The impact of the impairments on life expectancy calculations is identified in underwriting manuals developed by the life insurance industry. Medical underwriting companies often develop proprietary underwriting manuals using the results of the firm's experience. However, it should be noted that proprietary manuals include only the experience of that firm rather than a broader spectrum of data and results that can be typically found in industry-developed manuals.

Medical files do not typically have current or updated records but usually contain a medical history of the insured, often spanning a number of years. Additional testing or information requests are generally not permitted. Underwriters review each file and establish a life expectancy based on the medical impairments noted in the insured's medical history. While there is no requirement that the files contain medical information covering a certain length of time, life expectancy calculations from multiple and independent medical underwriters are necessary to abate the risk of an incorrect life expectancy calculation and should generally be no more than 12 months old. However, the complete medical history of the insured should be considered in the underwriting of the file.

Additionally, medical files may be submitted more than once to an underwriting firm. This may happen when the insured does not receive the expected price or for other various reasons. Underwriting firms should take every precaution to ensure that the medical files of multiple or repeat submissions contain the identical medical histories as previous submissions along with more current medical data, if available. DBRS believes it is prudent for life settlement transactions to have at least two independent medical underwriters calculate life expectancy, mortality ratings and confidence levels for each file in addition to providing a summary assessment of the medical impairments of the insured along with each debit, credit and/or flat extra applied to the insured.

It should be noted that medical underwriting firms that perform life settlement underwriting functions can be staffed with varying levels of expertise. Some firms use life insurance underwriters with extensive experience in life settlements while others employ physicians with expertise in various fields. DBRS looks at the staffing adequacy of medical underwriting firms to ascertain the company's ability to handle expected growth and volume, as well as provide training on medical advances and overall health and lifestyle changes. However, DBRS considers favorably those firms that use a balanced approach in reviewing medical files and assigning life expectancies by staffing or contracting experienced life insurance underwriters and doctors with expertise in various disciplines, including geriatrics and internal medicine. While this approach may not mitigate the risk of incorrect life expectancies, it provides some assurances that the impairments noted in the medical file have been accurately assessed.

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