

Longevity Risk in Fair Valuing Level-Three Assets in Securitized Portfolios

Abstract

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Level-three longevity valued assets pose unique valuation risks as securitized pools of these alternative asset classes come to market as investment vehicles for pension plans and individual retirement accounts. No uniform framework is applied to assure consistent fair market valuation and transparency for investor decision-making. Applying existing international auditing standards, IAS §540, and analytical procedures, IAS §520, offers a platform upon which fund managers, their auditors and actuaries can agree upon uniform valuation and presentation guidelines. Application of these quasi-governmental standards will bring future liquidity to otherwise illiquid capital market instruments.

This paper presents a valuation methodology consistent with fair value accounting and auditing standards. The methodology incorporates the longevity predictive modeling of Stallard, *NAAJ* 2007, and is compatible with Bayes Factor weighted average valuation techniques from Kass and Raftery, 1995. Securitizers continue to hide behind the theory of large numbers, despite the work of Milevisky, 2006. The size of securitized portfolios coming to market do not have statistical significance, Longley-Cook, 1962. This is observed in life settlement portfolios where the combination of too few large death benefit policies and large variances in life expectancy estimates challenge accurate valuation and periodic re-valuation.