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In the latter part of 2008 we have seen financial turmoil and market spasms that are unprecedented in history. While, it turns out, that some folks foresaw the looming danger in sub-prime mortgages, it's doubtful that anyone could have estimated the devastation it wrought throughout the world. Venerable financial institutions have either evaporated or been brought to their knees and governments are scurrying about to shore up the financial system and calm fears.

It's nearly impossible to know how many more dominoes will tumble before some stability reappears. In the midst of this chaos, it is only natural to question the soundness of every type of financial institution and the products they offer. Structured settlements and the life insurance companies who offer them should be no exception to this examination.

The good news is that, as of this writing (November 2008), all of the life insurance companies that offer structured settlements have indicated that they have minimal exposure to the sub-prime mortgage market and have avoided significant damage to their portfolios. In fact, the only company in the structured settlement market with any involvement to this point is American General Life Insurance. It's rating was down graded by AM Best from A+ to A.

American General is a wholly owned (but separate) subsidiary of the multi-national holding company American International Group (AIG). AIG captured headlines (and US Treasury money) recently due to its liquidity crisis from providing insurance to the credit default swap (CDS) market. When the CDS market began to rapidly decline, AIG needed to come up with billions of dollars of cash to meet the terms of its insurance agreements.

On its balance sheet AIG had more than enough assets to meet the cash requirements, but the assets were either not readily convertible to cash (e.g. their profitable subsidiaries), or they were in the form of surplus assets in their life insurance subsidiaries which, by regulation, they could not access. And, therein, lies one of the inherent strengths of life insurance investments.

You see, unlike most other financial industries, the insurance industry is regulated only at the state level. That means that fifty state insurance departments are paying attention to the financial status and business practices of the companies licensed to do business in their states. While most other financial services companies do, indeed, have accountability to state regulators, their primary regulation (if any) comes at a Federal (SEC, FDIC, Federal Reserve etc.) or national (NASD, CFTC etc.) level.

A quote from a recent document put out by the American Council of Life Insurers sums up the current state of life insurance pretty well,

"With over $5 trillion in assets and a conservative investment and underwriting profile, the life insurance industry is one of America's strongest business sectors. The life insurance industry has an unparalleled record of honoring its obligations to policyholders and is well positioned to continue this proud tradition.

At the end of 2007, life insurers held a surplus of over $281 billion. <u>This surplus represents assets above and beyond what is required to pay expected claims.</u>

The financial strength of the life insurance industry is further supported by independent ratings agencies. According to a September 2008 Fitch Ratings report, the life insurance industry's balance sheet remains strong. Fitch believes the industry is well capitalized, with aggregate risk-based capital (RBC) levels in excess of the 'AAA' threshold, and has the capacity to absorb potential losses as the credit crunch plays out.

In addition to the industry's solid asset base, insurance consumers enjoy the protection of state insurance guaranty associations, which provide protection to insurance policyholders for their guaranteed contract benefits. These associations ensure policyholders receive their benefits in the event of a major financial loss of an insurer."[1]

We are not suggesting that it is impossible for life insurance companies to fail. Given times like these it's anyone's guess where the next "land mine" could be and who or what it might impact. In fact, according to the Weiss Rating Service website, from 1988 to 2005 a total of 226 life insurance companies failed. Of that total, financial data was provided for 89 of the companies. Out of those 89 companies, 93% had total assets under $1 billion and 68% had total assets under $25 million. Only one company had total assets over $10 billion (it had $14.08 billion).

For perspective, according to the National Association of Insurance Commissioners website, as of December 31, 2007 the companies in the structured settlement business had a mean average of about $113.5 billion in total assets. The largest was Metropolitan Life with over $297 billion and the smallest was Aviva Life with $6.8 billion. Aviva Life's parent company, Aviva PLC, is the fifth largest insurer in the world with $795 billion in assets and they back the Aviva Life structured settlements through their Capital Maintenance Agreement (CMA). Incidentally, American General has over $36.5 billion in total assets with a surplus of nearly $6 billion.

In reality, no one can absolutely guarantee that any financial instrument is risk free. However, life insurance investments have, historically, been safer than stocks, bonds and even bank deposits. The life industry has a huge vested interest in maintaining the public trust. Consequently, when a life company has gone into receivership, solvent life companies have acquired the failed company's policies and maintain the guarantees in one form or another. This not only protects policyholders, but it also protects the viability of the industry.

So, the answer to the question, "How safe are structured settlements?" is that they are tremendously safe, probably safer than nearly any other type of investment with the exception of U.S. Treasury securities.