

**UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK**

JEFFREY LEONARD, IN HIS CAPACITY AS  
TRUSTEE OF THE POPLAWSKI 2008  
INSURANCE TRUST; PHYLLIS POPLAWSKI;  
PBR PARTNERS, BRIGHTON TRUSTEES,  
LLC, on behalf of and as trustee for COOK  
STREET MASTER TRUST III; BANK OF  
UTAH, solely as security intermediary for COOK  
STREET MASTER TRUST III; PEAK TRUST  
COMPANY, AK, on behalf of and as trustee for  
SUSAN L. CICIORA TRUST and STEWART  
WEST INDIES TRUST; and ADVANCE  
TRUST & LIFE ESCROW SERVICES, LTA, as  
securities intermediary for LIFE PARTNERS  
POSITION HOLDER TRUST, on behalf of  
themselves and all others similarly situated,

Plaintiffs,

vs.

JOHN HANCOCK LIFE INSURANCE  
COMPANY OF NEW YORK and JOHN  
HANCOCK LIFE INSURANCE COMPANY  
(U.S.A.),

Defendants.

Civil Action No. 18-cv-04994-AKH

**DECLARATION OF KEITH MCNALLY IN SUPPORT OF CLASS COUNSEL'S  
MOTION FOR ATTORNEYS' FEES, REIMBURSEMENT OF LITIGATION  
EXPENSES, AND INCENTIVE AWARDS**

I, Keith McNally, declare as follows:

1. I submit this declaration in support of Class Counsel's Motion for Attorneys' Fees, Reimbursement of Litigation Expenses, and Incentive Awards, in connection with the proposed class action settlement between Plaintiffs, on behalf of themselves and the proposed class, and Defendants John Hancock Life Insurance Company of New York and John Hancock Life Insurance Company (U.S.A.) (together, "John Hancock"). I have personal, first-hand knowledge of the matters set forth herein and, if called to testify as a witness, could and would testify competently thereto.

**A. Experience and Qualifications**

2. I am a company director and the Chief Operating Officer at Demeter Capital Limited ("Demeter Capital"). Demeter Capital is authorized and regulated by the United Kingdom's Financial Conduct Authority (FRN 745647) and is a financial consulting company that offers independent, discrete and high quality analysis to clients active in alternative investments with a core focus in the insurance market. Demeter Capital has 3 other company directors, James Rouse, Marcos Flores, and Alejandra Limones who have worked together in a broad range of senior positions in institutional investor capacities in the longevity markets, which includes working at a large bank, large asset manager and as advisors to insurance companies. Demeter Capital works with large, regulated institutional investors with a mandate to assess and acquire life related exposure in the US and Europe to include life settlements and longevity/mortality derivatives. The team at Demeter Capital has traded in over \$20bn longevity risk swaps, notes and securitizations since 2003. Additionally, the team at Demeter Capital executed the first ever swap in the UK Pension fund market.

3. At Demeter Capital, I am responsible for advising on the creation of new life settlement investment funds and consulting for large financial institutions on their investment in

life settlements. Prior to Demeter Capital, I was a Managing Director and Global Head of Macro Investor Products at Credit Suisse. I was also a member of the Credit Suisse's European Fixed Income Operating Committee. From 2006 to 2011, along with Demeter Capital company directors James Rouse and Marcos Flores, I was a leading member of the Credit Suisse Longevity Markets Group which structured and executed a number of pioneering synthetic longevity/mortality deals in the financial markets. I was also internal legal counsel at Credit Suisse in New York supporting various fixed income structuring businesses including the Latin American team. I was a New York State qualified attorney (retired) and hold an MSc in International Securities, Investment and Banking as well as a Law (LLB (Hons)) degree.

4. My colleague James Rouse is also a company director of Demeter Capital as well as its Chief Investment Officer, responsible for the risk models and underwriting of life settlement assets. Prior to Demeter Capital, Mr. Rouse was a Managing Director at Fortress Investment Group where he was primarily responsible for the analysis and pricing of life settlement portfolios. Prior to Fortress, Mr. Rouse had spent 11 years at Credit Suisse most recently as a Director within the Longevity Markets Group where he was responsible for the development of structured products and longevity derivatives linked to life settlements and pension schemes. Prior to the Longevity Markets Group, Mr. Rouse was in the Risk Management Division of Credit Suisse. Prior to Credit Suisse, Mr. Rouse worked as a manager within the Risk Control division at Sumitomo Bank and as a manager in the Financial Institutions Group at Deloitte and Touche.

5. My colleague Marcos Flores is also a company director of Demeter Capital as well as its Chief Executive Officer, acting as an expert consulting advisor for institutional clients in the insurance and credit lending markets globally. Prior to Demeter Capital, Mr. Flores started Hibiscus Capital Limited ("Hibiscus") in 2012, a consultant to large Private Equity Funds and

Insurance Companies with strategic investments. Prior to Hibiscus, Mr. Flores spent 12 years working at Credit Suisse as a Managing Director within the Longevity Markets Group. In his role, Mr. Flores was responsible for the origination, structuring and distribution of longevity risk, which included life settlements. During this time, he was a SIAP (Significant Influential Approved Person) for the Financial Services Authority of the UK and worked with CARMAC (Credit and Risk Management Committee) within Credit Suisse to develop the global strategy of the longevity business at the bank. Prior to his activity in the longevity asset class, Mr. Flores led the Fixed Income structuring teams at Credit Suisse for Europe and Latin America. Mr. Flores joined Credit Suisse when the firm merged with Donaldson, Lufkin & Jenrette, where he was a member of the Latin American Structuring team. Mr. Flores had also spent three years in Commodities Sales and three years at an affiliate of the Spanish development bank, Banco Exterior de Espana, based in Mexico.

**B. Valuation Purpose and Materials Considered**

6. Demeter Capital was retained by Class Counsel to independently value the non-monetary benefits for a specific portfolio of life insurance policies (the “Class Policies”) contained in the proposed settlement of the above referenced action. These benefits include: (a) a commitment not to increase the cost of insurance rates (“COI”) for a period of 5 years following final approval of the settlement. John Hancock further promises that, if any opt out or other ongoing litigants negotiate a COI freeze period longer than 5 years, John Hancock will match that duration for the Class Policies (the “COI Rate Freeze”); and (b) a commitment not to contest a death claim on the grounds that the policy lacks an insurable interest or for misrepresentations in the application (the “Validity Confirmation” and together with the COI Rate Freeze, the “Non-Monetary Benefits”).

7. In conjunction with my colleagues, I participated in the preparation of the valuation of the Non-Monetary Benefits. I have relied on the financial market and modeling expertise of my colleagues in the completion of this work. The valuation methodology, valuation opinion and primary significant assumptions for the opinion, are proffered below and, in more detail, in the report, dated March 11, 2022, on the valuation of the Non-Monetary Benefits, which is attached as Exhibit A (the “Report”).

8. In determining the estimated valuations of the Non-Monetary Benefits set forth in this Declaration, I have employed methods and analyses of a type reasonably relied upon by experts in the field of life settlements in forming the opinions and inferences on the subject.

#### **C. Assumptions and Valuation Methodology**

9. The primary significant scenario assumptions are set forth in Section 1 of the Report. The valuation methodology is set forth in Section 2 of the Report.

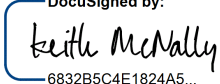
10. Demeter Capital is receiving compensation for time spent on this assignment. The engagement of Demeter Capital for this assignment and the compensation for completing it are not contingent on the development or reporting of a predetermined value or any direction in value, the amount of the valuation opinion, or the attainment of a subsequent event directly related to the intended use of this valuation.

#### **D. Valuation Opinion**

11. As a result of procedures performed, it is my opinion that a reasonable estimate of the Non-Monetary Benefits is **\$67.76m**. This amount represents the estimate of the COI Rate Freeze of **\$55.96m** as detailed in the Report and the estimate of the Validity Confirmation of **\$11.79m** as detailed in the Report.

I declare that the foregoing is true and correct under penalty of perjury under the laws of the United States.

Executed this 11 day of March, 2022 at London, United Kingdom.

DocuSigned by:  
  
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Keith McNally

# **EXHIBIT A**

**Report On the Value of the Non-Monetary Benefits Achieved in the Class Action  
Settlement with John Hancock (the “Report”)**

**Executive Summary**

As a result of the analysis set forth in this Report, Keith McNally of Demeter Capital Limited (“Demeter”) has determined that a reasonable estimate of the value of the two Non-Monetary Benefits secured for the benefit of the Settlement Class, is the following:

<b>Commitment</b>	<b>Value</b>
COI Rate Freeze	\$ 55.96m
Validity Confirmation	\$ 11.79m
<b>Total</b>	<b>\$ 67.76m</b>

For this Report “Settlement Class” is assumed as the 1,277 policies identified in the file of policy data provided to Demeter by Class Counsel. These 1,277 policies exclude policies which are excluded from the Settlement Class definition by dint of filing a separate litigation claim or having previously reached a settlement with John Hancock (“Excluded Policies”) and also assumes that there are no opt-outs to the Class (policies which opt-out are “Opt-Out Policies”) although the deadline to opt-out has not yet expired.

**Scope**

Demeter was retained by counsel for the plaintiffs in connection with a class action against John Hancock Life Insurance Company (U.S.A.) and John Hancock Life Insurance Company of New York (collectively, “John Hancock”) in order to value the non-monetary benefits contained in the settlement agreement in connection with its forthcoming motion for final approval of the settlement and a concurrently filed motion for attorneys’ fees, reimbursement of litigation expenses, and incentive awards.

This Report provides an estimate of the value of two commitments from John Hancock with respect to the Settlement Class.

The two non-monetary benefits (the “Non-Monetary Benefits”) that are the subject of this Report are the following commitments by John Hancock:

- **COI Rate Freeze.** Agreement not to impose a new COI rate schedule for 5 years following final approval of the settlement, plus a provision that if any other opt-out plaintiff negotiates a longer deal than 5 years, John Hancock will match that duration for the Class Policies. We have been asked to value this (minimum) 5-year period as starting from May 31, 2022 and ending May 31, 2027. We understand the 5 year period will start from the date of final approval by the Court.
- **Validity Confirmation.** An agreement by John Hancock not to challenge or rescind any policies on lack of insurable interest or fraud grounds or based on misrepresentations in the policy application. This promise lasts in perpetuity.



## **General Approach and Data Considered**

A reasonable and fair approach to measure the value of the Non-Monetary Benefits to the Class is a present value of the expected cost of the promises— *i.e.*, the cost of providing the benefit. The discount rate applied to the calculations is representative of life insurance industry projects. A discount rate of 7% has been used. This is discussed in Section 1.8.

The calculations of the benefits' value are made by using future projections of the cashflows of the policies. The projections are performed both with and without the promises, and the value of the benefits is taken as the present value of the difference between the two projections.

The future projections require a modelling of the future mortality of the policies. Demeter has extensive experience with cash flow projections for life insurance policies including universal life insurance policies like policies in the Class. Demeter has regularly performed these types of calculations for our clients including life insurance companies and life settlement funds.

John Hancock has provided its own expectations of mortality for the Class Policies – a table known as JH17A. For the purposes of this Report Demeter has used JH17A as the base scenario table. Demeter has estimated the volatility of expectations of mortality around JH17A. This is described in detail in section 1.

We have been provided with data for 1,500 policies that we understand were in force on December 31, 2017 and were subjected to an increase in COI rates. We have also been provided with a file of policy data as of September 15, 2021, with deaths updated through August 31, 2021<sup>1</sup>. This file also contains, for each policy, the difference between what COI charges would have been under the original scale and what COI charges actually were under the scale imposed as a result of the May 2018 COI Increase. This later file contains 1,277 policies which are the policies within the Settlement Class for which the Court granted preliminary approval, prior to any opt outs.

We were asked to assume that the Non-Monetary Benefits start on May 31, 2022. Therefore, it was necessary to update the Settlement Class from August 31, 2021 to May 31, 2022. For the purposes of this Report, we have assumed a certain rate of lapse as described in section 1.2 and maturities consistent with JH17A from August 31, 2021 to present.

## **Approach for Valuing the COI Rate Freeze**

The Settlement Agreement defines the “COI Rate Freeze” as follows: “For a period of 5 years following the Final Approval Date of the Settlement, John Hancock agrees to not increase the COI rate schedules on the Final Settlement Class Policies above the COI rate schedules in place as of August 31, 2021.”

The Settlement Agreement further provides: “John Hancock agrees that if it reaches an agreement concerning any of the Opt-Out Policies or Excluded Policies to freeze the COI rate schedules on such policies for a duration of longer than 5 years, as measured from the execution date of any settlement, it will extend the duration of the COI Rate Freeze on the Final

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<sup>1</sup> The experience data is through August 31, 2021 but the data was gathered as at September 15, 2021. For example, if someone died on 27th August, but only notified John Hancock on the September 16, that death would not have been included in the file.

Settlement Class Policies so as to make the duration of the Final Settlement Class Policies' COI Rate Freeze as long as that afforded to the subsequently settling Opt-Out Policies or Excluded Policies.”

In providing the COI Rate Freeze, John Hancock is foregoing the ability to raise COI rates even in the event of negative changes to the mortality expectations of the Class Policies. To evaluate the benefit of the COI Rate Freeze, we considered the probabilities of various future changes in mortality scenarios of differing degrees of magnitude, and, using those numbers, the difference in what John Hancock would have been able to charge using a COI increase compared to what they now cannot for the next five years.

### **Methodology for COI Rate Freeze Valuation**

The main driver of a potential COI increase we have considered is the mortality performance of the Class Policies.

The methodology for the COI Rate Freeze valuation is to project death benefits and COI deductions for the policies in five scenarios:

- Scenario 1: John Hancock's mortality expectations improve slightly
- Scenario 2: John Hancock's mortality expectations improve significantly
- Scenario 3: John Hancock's mortality expectations stay roughly consistent
- Scenario 4: John Hancock's mortality expectations worsen slightly
- Scenario 5: John Hancock's mortality expectations worsen significantly

Considering only the mortality factor, the COI Rate Freeze provides meaningful benefits to the Class Policies in the scenarios where John Hancock's expectations of mortality worsen, and John Hancock might have implemented a COI increase but for the freeze – i.e., Scenarios 4 & 5.

Scenario 3 has been built around John Hancock's mortality table JH17A. Nothing in this Report should be taken as an endorsement of the JH17A or the accuracy or suitability of JH17A for any purposes, other than Scenario 3 of this Report and that it records John Hancock's expectations of mortality as of December 31, 2017.

To ensure that JH17A was suitable for Scenario 3 Demeter reviewed the mortality experience of the Settlement Class during the period December 31, 2017 to August 31, 2021. In reviewing the mortality experience of the Settlement Class and comparing it to JH17A, Demeter concluded that using JH17A was suitable for purposes of this calculation.

The Class Policies were issued to insured individuals with four different classes of policy for non-smokers: standard plus, standard, preferred, and preferred plus and two classes for smokers: standard and preferred. Some of the life insurance policies have extra rating factors.

This classification was due to medical underwriting which leads to a Select and Ultimate rate pattern, and JH17A is a select and ultimate rate table.

The average duration of the policies for the period December 31, 2017 – August 31, 2021 was 11.9 years and average issue age 73.3. The select effects of underwriting at this age/duration will have mostly worn off and the mortality experience described above reflects primarily on the ultimate rate assumptions of the JH17A table. These ultimate rates will be the most important assumptions for the Class Policies for any future redetermination.

For future mortality improvements for the purposes of this Report, for Scenario 3, we have used an internal mortality improvement assumption from John Hancock's mortality experience studies.

Mortality for Scenarios 1, 2, 4 & 5 have been generated as described below in Section 1.1 (Mortality).

We have then calculated the value in these scenarios with a present value calculation of the resulting cash flows, using a discount rate of 7%.

The calculations use cashflows through May 2027, which consider that John Hancock cannot raise rates for that period. Cashflows after May 2027 are not included in the calculation as the COI Rate Freeze promise ends absent an extension triggered by the Settlement's MFN clause.

The Settlement promise includes a provision that if any other Opt-out Policy or Excluded Policy holders negotiate a longer freeze period than 5 years, John Hancock will match that duration for the Class Policies. For the purposes of this Report we have assumed that the COI Rate Freeze will be for 5 years and have not accorded a value to the probability of extending the period to match a negotiation by a third party.

Each of the five scenarios needs to be quantified for

- Extent of the change in mortality expectations; and
- Probability of the scenario.

The quantification of the scenarios and outcomes are detailed in Section 2.

### **Approach for Valuing the Validity Confirmation**

The Validity Confirmation is an agreement by Hancock not to challenge or rescind any policies on lack of insurable interest or fraud grounds or based on misrepresentations in the policy application.

The Settlement Agreement defines the "Validity Confirmation" as follows: "Defendants shall forever be barred from taking and shall not take any legal action (including asserting as an affirmative defense or counterclaim) that seeks to void, rescind, cancel, have declared void, or seek to deny coverage under or deny a death claim for any Final Settlement Class Member based on: (1) an alleged lack of valid insurable interest under any applicable law or equitable principles; or (2) any misrepresentation allegedly made on or related to the application for, or otherwise made in applying for a Class Policy."

The Class Policies have been in force for more than 2 years and are all outside of their contestable periods. This means the risk for a policy holder of a contest to a death claim for reasons such as suicide or inaccuracy in medical statements has now passed. As a result, absent trivial issues such as a failure to present a death certificate, fraud or lack of insurable interest now present the main reasons why John Hancock would not pay a death benefit claim.

The calculation of the value of the Validity Confirmation was performed as the present value of the difference between two projections:

- Base case mortality (JH17A) and lapse rate assumptions, and a risk of a challenge to the death benefit payment.

- Base case mortality (JH17A) and lapse rate assumptions, and no risk of a challenge to the death benefit payment.

In providing the Validity Confirmation, John Hancock is foregoing the ability to challenge and resist death benefit claims in the future for Class Policies. In order to provide a valuation of the Validity Confirmation, we estimated the following:

- timing of the future claims for death benefits for the Class Policies;
- the probability that John Hancock could successfully resist a claim; and
- the amount of payout that John Hancock would have saved in the event of successfully resisting a claim that John Hancock is now foregoing (and that is therefore a benefit going to the Class).

The timing of the future claims was projected using JH17A and the lapse assumptions described in Section 1.2. However, whereas the projections for the COI Rate Freeze ended May 31, 2027, the Validity Confirmation has no end date and therefore projections were extended for 40 years – after the likely last policy maturity in the Settlement Class.

The present value of the death benefit claims was calculated by discounting at 7%.

Values are shown in Section 2.

## **Section 1 - Scenario Assumptions**

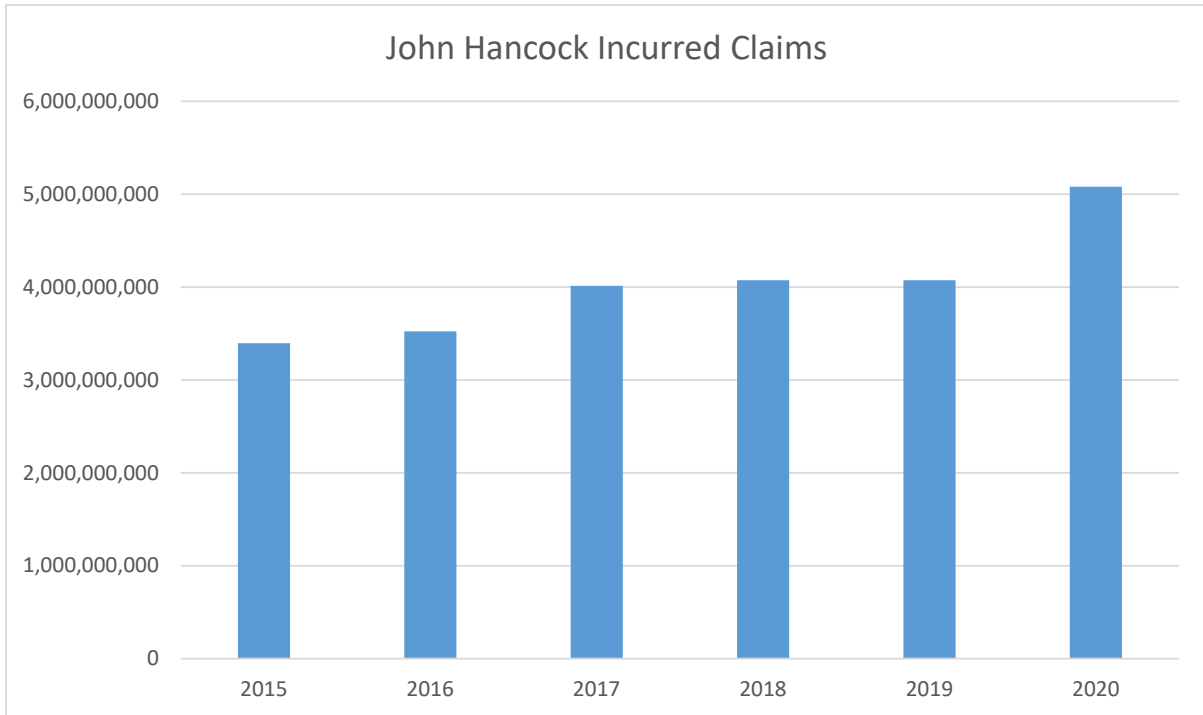
For purposes of this Report, Demeter has considered only the potential for COI increases driven by the projected performance of the Class Policies. We take no position and offer no opinion in this Report as to when a COI increase by John Hancock would be permissible under the terms of the policies, or what factors may appropriately be considered by John Hancock under those terms, or what grouping of policies into classes is permitted by John Hancock under the terms of the policies.

Our projections make use of the following assumptions.

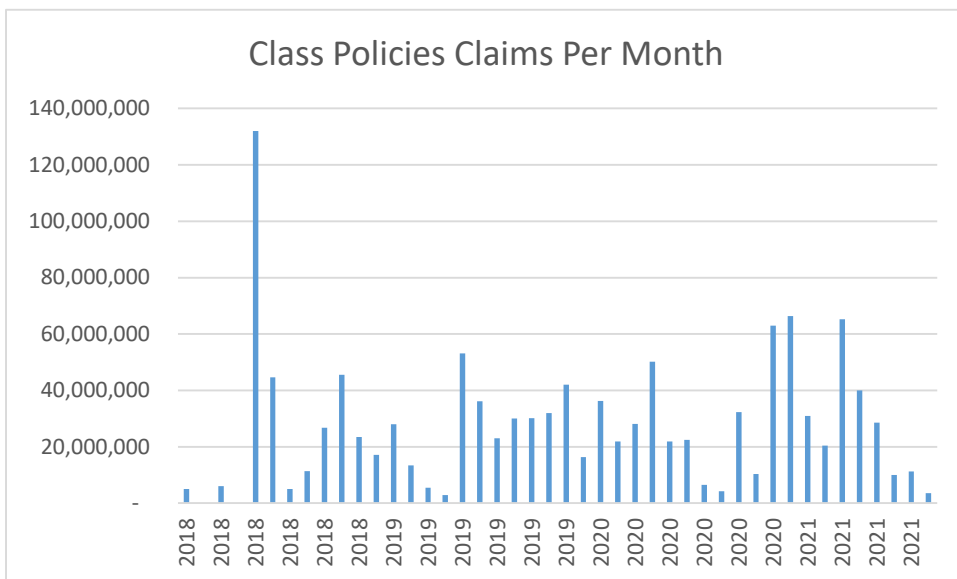
### **1.1 Mortality**

John Hancock used an internal table (JH17A) with various scalars and future mortality improvements applied to project mortality at the time of the last COI redetermination. This Report considers the potential for variation in John Hancock's mortality rates for the Class Policies over the next 5 years. John Hancock has the risk that its mortality expectations for the Class Policies increase and is unable to increase COI rates as a result of this settlement.

Mortality varies over time, John Hancock's NAIC returns state that total claims (across all life products) increased in 2020 during the time of the Covid-19 pandemic.



On a month-by-month basis the Class Policies demonstrate greater volatility than would be seen in aggregate for a year across the whole of John Hancock’s platforms. The graph below shows the claims history for the Class Policies from Jan 2018 – August 2021.



In providing the COI Rate Freeze, John Hancock is foregoing the ability to raise COI rates in the event of negative changes to John Hancock’s best estimate mortality expectations of the Class Policies. To evaluate the benefit of the COI Rate Freeze, we considered the probabilities of various future changes in John Hancock’s best estimate mortality by using scenarios of differing degrees of magnitude, and, using those numbers, the difference in what John Hancock would have been able to recover using a COI increase compared to that John Hancock now cannot increase COI rates for the next five years.

To calculate the probabilities of changes in mortality we required estimates of the volatility of mortality rates.

In August 2015 Demeter published a report using base Qx shock variance of 12% and mortality improvement variance of 0.75%. Demeter reviewed industry data around expectations of shock changes in mortality rates to see what changes or updates should be made to this.

Sources for this review included insurance industry regulators who require life insurance companies to hold surplus capital above what might be expected, for unexpected shocks to risk factors.

Demeter reviewed publications from the following authorities:

The European Insurance and Occupational Pensions Authority's<sup>2</sup> Solvency II capital adequacy program.

The International Association Of Insurance Supervisors<sup>3</sup>

The Financial Stability Board<sup>4</sup>

Office of the Superintendent of Financial Institutions (OSFI)<sup>5</sup>

Australian Prudential Regulation Authority (APRA)<sup>6</sup>

The American Academy of Actuaries provided a presentation to the NAIC<sup>7</sup> in a report dated November 9, 2019, by the Mortality Work Group of which considered a number of risk factors to mortality, including,

- Volatility risk: The risk of natural statistical deviations in mortality experience.
- Level risk: The risk of incorrect experience mortality assumptions.
- Trend Risk: The risk that future mortality improvement is different than assumed
- Catastrophe Risk: The risk of a short-term spike in mortality or a longer-term increase in mortality from a currently unknown health event, including Pandemic or Terrorism

Many regulators work towards high degrees of confidence. For example, the American Academy of Actuaries work uses the 95% percentile of risk.

For the purposes of this Report, we need to estimate the expected value of the Non-Monetary Benefits, and not the 95% percentile. To do this we have assumed a log normal distribution for mortality changes.

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<sup>2</sup> <https://eiopa.europa.eu>

<sup>3</sup> <https://www.iaisweb.org>

<sup>4</sup> <https://www.fsb.org/>

<sup>5</sup> <https://www.osfi-bsif.gc.ca/Eng/Pages/default.aspx>

<sup>6</sup> <https://www.apra.gov.au/>

<sup>7</sup> [https://content.naic.org/sites/default/files/call\\_materials/Agenda%20%26%20Materials%20LRBC%2011-9-21.pdf](https://content.naic.org/sites/default/files/call_materials/Agenda%20%26%20Materials%20LRBC%2011-9-21.pdf) at attachment C

Review of the literature sources listed above revealed nothing that would conflict with Demeter’s report of 2015; if anything the events of the past few years have confirmed the reasonableness of the settings used in that report and this Report uses the same settings.

These give rise to the following scenarios:

Scenario	QX Shock	FMI <sup>8</sup> Shock	Scenario Weight <sup>9</sup>
Scenario 4 – Worsen Slightly	109%	-0.6%	23.9%
Scenario 5 – Worsen Significantly	122%	-1.3%	11.8%
Scenarios 1, 2 & 3 - No COI rate adjustment	100%	0%	64.2%

For comparison, the life insurance industry incurred an increase in claims of 15% in 2020 (*Source*: NAIC data) during which the Covid-19 pandemic occurred. The CDC have reported excess population mortality for 2020 of 10.9% and 12.5% for 2021.

We have assumed that on average the scenarios occur two years into the COI Rate Freeze. This timing incorporates the fact that John Hancock updates its mortality tables roughly every three years, and the carrier might contend that there is an implementation delay between updating a mortality table and implementing a COI increase.

## 1.2 Lapse

The relationship between COI charges and mortality for the products is such that lapses favour John Hancock. John Hancock faces the risk that lapse rates are lower than expected and is unable to increase COI rates as a result of this settlement.

Demeter reviewed the assumptions for lapse that John Hancock used in the last COI redetermination and compared them to the Settlement Class experience for the period December 31, 2017 to August 31, 2021.

Demeter found John Hancock’s lapse rate assumptions did not accurately predict the lapse rate of the Settlement Class policies.

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<sup>8</sup> FMI means future mortality improvement.

<sup>9</sup> Weights use the Gaussian Quadrature rule.

We are familiar with the life settlement market, and the Class Policies are common products in life settlement investor portfolios. The lapses on the book are therefore likely to be lower than general life insurance books, which often have lapse rates of 4-6%.<sup>10</sup>

Investors tend to buy large face policies, as the administrative costs of running small face policies make them uneconomic investments. Face size is often an important indicator of lapse rates for these policies as the larger face policies are more likely to be purchased in the life settlement market.

The table below shows the history of lapses for the Settlement Class during the period December 31, 2017 to August 31, 2021.

Face Size	Start DB	DB Lapse/Surrendered	#Policies	# Lapse Surrendered	% By DB	% By Count
Greater than or equal to \$2m	3,619,523,595	51,803,591	602	10	1.4%	1.7%
Less than \$2m	398,673,114	19,165,635	675	41	4.8%	6.1%

From this data we developed the following lapse rate assumptions:

- Face Size greater than or equal to \$2m: 0.5% per year
- Face Size less than \$2m: 1.5% per year

As a result of our familiarity with the life settlement market, we believe it is unlikely that lapse rates will significantly vary from the rates above in a manner to cause a COI increase by John Hancock in the next 5 years. Accordingly, these lapse rates have been used in all of the projection scenarios to evaluate the Non-Monetary Benefits.

### **1.3 Investment Returns**

At the time of the last COI redetermination John Hancock wrote that the difference in investment return assumptions between current expectations and pricing was not passed to policy holders in the COI increase as:

- A crediting rate mechanism adjusts for changes in yields over time; and
- A hedging program is in place.

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<sup>10</sup><https://www.soa.org/resources/research-reports/2019/2009-13-us-ind-life-persistency-update/>



Additionally, it should be noted that the cash value of the policies was low (\$129.6m on \$5.4bn of death benefit or 2.4% of death benefit<sup>11</sup>) and can be expected to remain low given the ownership profile of the Settlement Class.

These factors mean there is little further downside to John Hancock from investment returns in the next 5 years and variations in this factor have not been considered for this Report. Investment returns have not been included in the projection scenarios.

#### **1.4 Expenses and Premium Taxes**

The average face size of the Class Policies is \$3.0m, this is larger than the industry average policy size of \$183,780<sup>12</sup> and means that COI and Premium load deductions are much larger than expense deductions. Changes in Premium Taxes rates are infrequent and tend to be for small amounts. For these reasons potential variations in expenses and premium taxes were considered immaterial for the purposes of this Report. As a result, expenses and premium taxes have not been included in the projection scenarios.

#### **1.5 Premium Funding Pattern**

At the time of the last COI redetermination, John Hancock wrote that changes in premium funding patterns were not material and they had not passed these changes on to policy holders. This included a projection of payment of planned premiums until the cash account was exhausted and thereafter payment of the minimum premium to keep the policy in force each month.

For the purposes of this Report, we have projected payment of the minimum premium to keep the policy in force each month. This is consistent with the high rates of life settlements in the Settlement Class and low cash account values (2.4% of death benefit).

The premium payment pattern has been assumed for all projection scenarios, there is little further downside to John Hancock from a change in funding patterns in the next 5 years, and variations in this factor have not been considered for this Report.

#### **1.6 Taxes**

John Hancock performed its last COI redetermination gross of taxes. John Hancock claimed this was in the policy holder's favour as the taxes on the Settlement Class are largely recoveries and corporate tax rates fell from 35% to 21%. Without purporting to endorse this assumption, for the purposes of this Report, we have calculated the value of the Non-Monetary Benefit of freezing COI increases gross of taxes, as this is consistent with John Hancock's methodology for this COI increase.

#### **1.7 Contest Success Probability and Pay-out Rates of Resisted Claims**

Data from market aggregate figures provides information about how often carriers resist a death claim:

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<sup>11</sup> Total for all 1,500 policies including opt-outs.

<sup>12</sup> Source ACLI data for 2020.

Year	Disputes Settled (\$millions)	Amount Paid (\$millions)	Amount Denied (\$millions)	Incurred Claims (\$billions)	Denied / Incurred Ratio
2015	829.1	206.5	622.5	73.5	0.85%
2016	805.9	153.8	652.0	74.8	0.87%
2017	812.2	247.9	564.3	77.0	0.73%
2018	855.8	110.4	745.4	78.4	0.95%
2019	868.8	303.0	565.8	79.8	0.71%
2020	669.1	320.5	348.6	92.0	0.38%
Total	4840.9	1342.2	3498.7	475.5	0.74%

Source: ACLI tabulations of NAIC data.

The last few years have seen a resurgence of STOLI litigation.<sup>13</sup> By making this settlement, John Hancock is foregoing the option to take part of this wave of new STOLI litigation and instead provides payment certainty on the policies and thus value to the Class Policies. Also new in this trend has been an increase in success rates where some carriers have been able to convince courts to permit the retention of some or all the premiums received.

John Hancock has contended that many of the Class Policies are unlawful STOLI, *see, e.g.*, Dkt. 174 (Amended Answer) at Eighth Affirmative Defense (alleging unclean hands and rescission). For these reasons, it is reasonable for settlement purposes to use the aggregate market rate data to provide the settings for the model scenario that includes risk of a challenge to payment of death benefit:

- Probability of resisting claim =  $\$4,840.9\text{m} / \$475.5\text{bn} = 1.02\%$
- Payout amount for resisted claim =  $\$1,342.2\text{m} / \$4,840.9\text{m} = 27.7\%$

### **1.8 Discount Rates**

To define the value today of the Non-Monetary Benefits provided by the Settlement, we have to present value the future cash flows with a certain discount rate.

The owners of the portfolio are likely to fall into two disparate groups.

- Individuals who are currently receiving low rates of interest on their bank deposits, often less than 1% and who rarely use discounting to assess the value of a project.
- Life settlement funds who target high returns on capital and who are typically earning 8-9% returns on capital.

<sup>13</sup> *See, e.g., Pacific Life Ins. Co. v. Wells Fargo Bank, N.A.*, C.A. No. 8:21-cv-737 (PJM) (D. Md.); *Columbus Life Ins. Co. v. Wilmington Trust, N.A.*, C.A. No. 20-735-MN-JLH (D. Del); *Sun Life Assurance Co. of Canada v. Bank of Utah*, Case No. 21-CV-3973-LMM (N.D. Ga.).

We have used a 7 percent discount rate for this Report which represents a blended average of the low rates of return expected by individuals and the higher rates being earned by life settlement funds.

## 1.9 Reinsurance

Reinsurance is excluded from all the calculations in this Report. Although the availability of reinsurance may have an impact on John Hancock's costs, reinsurance is not relevant to the value that policyholders would obtain from the Non-Monetary Benefits.

## Section 2 - Results

### 2.1 COI Rate Freeze Valuation

As with the Validity Confirmation valuation, we assumed a starting balance of death benefits given the in-force data as of August 31, 2021 and rolled this to May 2022 using JH17A and the lapse rate assumption.

The assumed in-force balance was then projected forward for 60 months using the scenarios described earlier, including lapse, premium payment, and mortality assumptions. The projections were for account balance and death benefits of the policies. The present value of the difference between net death benefit payments<sup>14</sup> and COI charges was calculated:

Scenario \$million	PV COI Charges	PV Net Death Benefit	Difference	Benefit	Scenario Weight
Scenario 4 - Worsen Slightly	\$467.2m	\$1,035.3m	-\$568.1m	\$108.5m	23.9%
Scenario 5 – Worsen Significantly	\$439.3m	\$1,152.3m	-\$713.0m	\$253.3m	11.8%
Scenario 1,2 & 3 - No COI rate adjustment	\$487.5m	\$947.2m	-\$459.7m	Nil	64.2%

The COI Rate Freeze Value was calculated as

(Worsen Slightly Scenario Benefit x Scenario Weight) + (Worsen Significantly Scenario Benefit x Scenario Weight)

The benefit is the difference between the scenario and the COI Rate freeze that John Hancock will be stuck with due to the settlement.

<sup>14</sup> Net means difference between death benefit and account value.

Worsen Slightly Scenario Benefit =  $-\$459.7\text{m} - -\$568.1\text{m} = \$108.5\text{m}$

Worsen Significantly Scenario Benefit =  $-\$459.7\text{m} - -\$713.0\text{m} = \$253.3\text{m}$

Total weighted benefit =  $\$108.5\text{m} \times 23.9\% + \$253.3\text{m} \times 11.8\% = \$55.96\text{m}$

## **2.2 Validity Confirmation Valuation**

In providing the Validity Confirmation, John Hancock is foregoing the ability to challenge and resist death benefit claims in the future for Class Policies. To determine the value of the Validity Confirmation, we performed a probability weighted net present value calculation using the assumptions set forth above. We utilized the data provided to project for the Settlement Class policies death benefits, and account balances for the period from May 2022 to maturity. The projection includes the future probability of lapsing a policy, starting at May 2022 using the lapse rate assumption. We assumed a starting balance of death benefits given the in-force data as of August 31, 2021 and rolled this to May 2022 using JH17A and the lapse rate assumption.

We then applied the JH17A table and future mortality improvements to generate forward Qx, i.e., mortality rates, for each Class Policy and built a set of future survival probabilities starting at May 2022. The future death benefits of the policies were projected using the probability of lapse and death for each month.

For the without Validity Confirmation scenario, the death benefits were reduced for a probability of being contested of 1.02% and a payout ratio of 27.7%.

Estimates of legal expenses incurred in resisting policies were not considered

The results of each life insurance policy in the Settlement Class were then aggregated and discounted to reach our estimated value of the Validity Confirmation.

PV of future death benefits without Validity Confirmation = \$1,599.1m

PV of future death benefits with Validity Confirmation = \$1,587.3m

Value of Validity Confirmation = \$11.79m

### **Section 3 – Impact of Opt Outs**

We understand that the opt out period is still ongoing, and that some of the Class Policies may opt out of the settlement by the opt out deadline of March 28, 2022. As policies opt out of the class, the value of the Non-Monetary Benefits may decrease. Because the number of opt outs is unknown at this point, the analysis in this Report assumes zero opt outs. We will update this analysis when the final number of opt outs becomes known.

### **Conclusion**

Using the methodology and assumptions set forth above as well as our own expertise in the subject matter, we calculated the values of the COI Rate Freeze and the Validity Confirmation. A summary of our findings are set forth in the table below.

Commitment	Value \$
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COI Rate Freeze	\$ 55.96m
Validity Confirmation	\$ 11.79m
Total	<b>\$ 67.76m</b>

We have performed a qualitative review of these results and believe that they are a reasonable calculation of the value of the Non-Monetary Benefits.

Demeter Capital

March 11, 2022