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New Ways to Get in Touch with Old Clients

Revisiting Estate Plans Through Life Settlements

By Larry Simon, president and founder, Life Settlement Solutions, Inc.

Several years ago, you helped your clients choose an estate plan, life insurance policy and planned giving schedule that would fit their needs based on their projected end-of-life desires. Now those middle-aged clients you served are AARP members.

As one might expect, people's lives and needs change drastically between ages 65 and 85 and often financial plans made previously no longer apply. Think of a client you may have served 15 years ago. Imagine, for a moment, that he survived a major heart attack this past year. Your client may have been comfortable living on his pension, but now the bulk of his income goes toward hospital fees, doctor visits, medication and other medical expenses. The money he would have used to pay his life insurance premium is now redirected and his policy will lapse. The lapse occurs with more than 90% of policyholders.

Once a policyholder recognizes that the life insurance policy no longer fits present or future needs, agents can provide a valuable service by facilitating the client's ability to convert a life policy into cash. Through life settlements, agents can give their clients financial options that were previously unavailable. With the cash realized through a life settlement, clients may choose options, such as estate plans or planned giving, which may better suit their financial goals. Clients can take their life settlement and pay medical bills, donate to nonprofit agencies, or redirect estate plans toward family, friends or other end-of-life needs.

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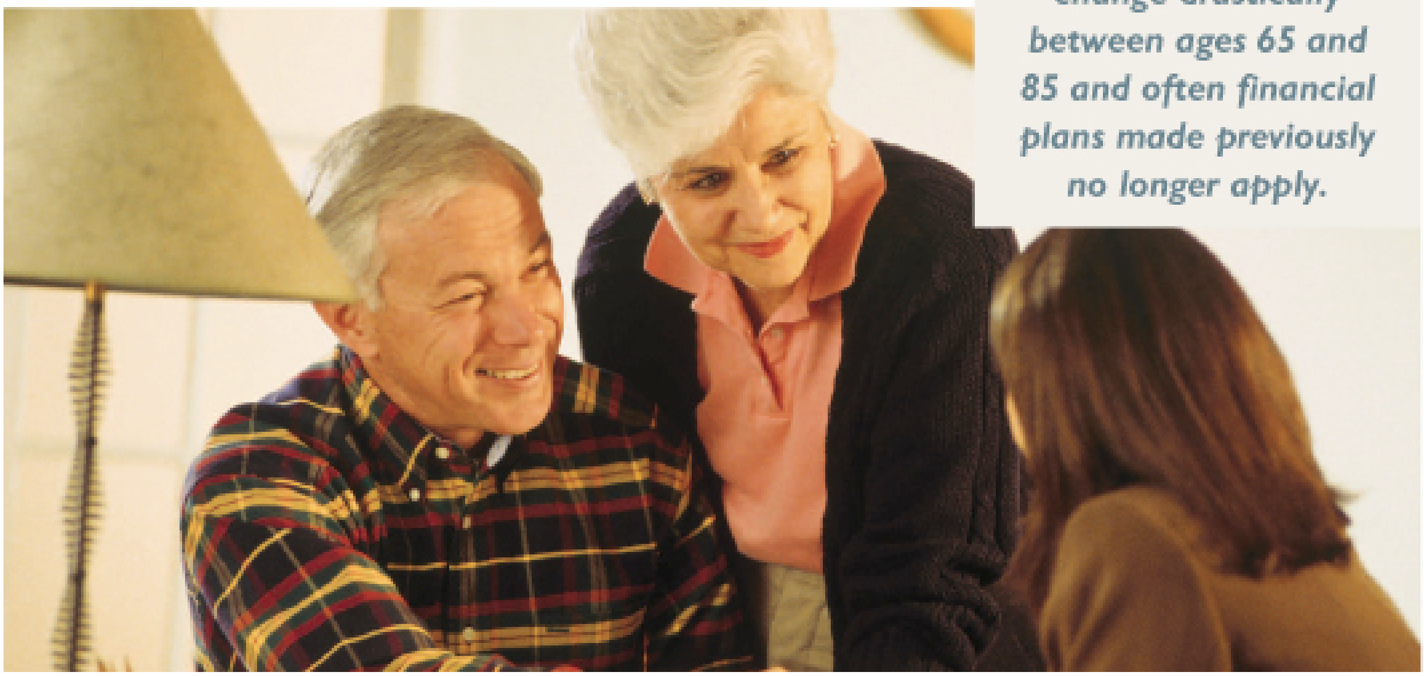

It does not make sense for most policyholders to surrender their policies to the carrier. The secondary market for life insurance policies gives a policyholder the ability to respond to changes in his or her life, according to a 2002 Wharton Financial Institution Center study titled, "The Benefits of a Secondary Market for Life Insurance Policies." According to the study, the sale of a policy by an eligible individual to a life settlement firm is beneficial in a variety of situations, such as the following:

- The policyholder wants to replace an individual policy with a survivorship policy or a long-term care policy.
- The policyholder needs funds for long-term care or medical expenses.
- There is an increase in the liquidity of the policyholder's estate, which eliminates the need for the policy.
- A reduction in the value of the policyholder's estate reduces the tax liability for which the life insurance policy was designed to provide.

"In some cases, a new life insurance policy may be obtainable on terms better suited to a client's changed situation, such as new individual life policy or joint-survivorship coverage," according to the report.

Other ways life settlements benefit end-of-life planning is if the policy is not in a trust, but owned by the client. The sale proceeds could be used to pay the gift tax on a gift the client makes to loved ones. Meanwhile, other clients want to give their heirs cash instead of a policy. By doing this, clients avoid the risk that the policy will be included in their estate if they die within three years after making the gift. The gift would be given tax-free, using the annual $10,000 gift-tax exclusion.

These transactions have become an important factor in the estate planning for seniors. By liquidating a policy for an amount higher than the cash-surrender value, policy owners get the following benefits:

- Higher cash payout than the cash surrender value.
- Funds to cover long-term care.
- Generating profit from a nonperforming or worthless asset.
- Relief of monthly premium expenses.
- Alternative funding for LTC policies, annuities or other investments.
- Additional funds to supplement retirement income.
- Funds to seek treatments not covered by health insurance.
- New options in estate planning and planned gifts.

Life Settlements Provide Options for a Variety of Seniors

Life settlements are not viaticals. Unlike viaticals, life settlements (also known as "senior settlements" or "high-net-worth transactions") are based on the proposition that some insured people no longer want, need or can afford their coverage. Instead of selling the policy back to the issuing insurance company at less than market value or allowing the policy to lapse and forfeiting the value, life settlements allow another exit option, which can maximize the cash value for the policy owner. Consequently, life settlements have quickly developed into a viable and attractive alternative product.

The market opportunity exists primarily because life insurance companies usually pay low surrender values when a policy owner decides to redeem or cash in the policy. The surrender values are usually so low that a qualified life settlement provider company can pay a higher value.

Life settlements aren't for everyone. A good candidate typically has $500,000 or more in universal life coverage though virtually any type of life insurance, and those held in irrevocable life insurance trusts may qualify. Life settlements are designed for people who are not suffering from a life-threatening or catastrophic illness and whose life expectancy is greater than two years, but usually not more than 10. The policy must have been issued two or more years ago, generally by an A-rated U.S. insurance company.

The reasons a life settlement solution might work for a client are varied. Perhaps the policy owner has accumulated enough wealth that he or she is essentially self-insured. In other cases, the policy premiums may have become too expensive and unaffordable and the client wants to seek other coverage. Other scenarios might include a policy owner removing a policy from a taxable estate or replacing a single-life policy with a joint and survivor policy.

Will This Option Fit Your Client?

Once a life settlement company locates an eligible life insurance policy and confirms initial eligibility requirements are met, the insured's medical records are sent to one or more medical evaluators for a life expectancy rating. Suppose that an offer to purchase the policy is to be extended to the owner. Let's look at what the basis for determining the bid price that will meet investment criteria as established by the capital funding sources. It involves the results of these evaluations and information derived from a policy illustration that was generated by the insurance company that issued the policy.

Policies that life settlement companies consider for purchase must meet certain eligibility requirements. The following are typical criteria formed with the life settlement companies, investors or lenders:

- It is beyond any carrier or statutory contestability period and is fully renewable, subject only to the payment of premiums.
- The insured's life expectancy is between 25 and 144 months based on one or more medical evaluations from an approved evaluator.
- Term policies must have a minimum term life insurance coverage equal to the greater of two times the life expectancy or 10 years.
- The face value of such policy cannot exceed $20 million.

Policy owners who accept the offer and sell their ownership interest in the policy relinquish ownership and beneficial interest in the policy in exchange for a cash payment. Upon the insured individual's death, the investor, as designated owner and beneficiary, receives the policy's death benefit. The capital invested in life settlements earns a "yield" in exchange for assuming the cost to maintain insurance coverage and the timing risks associated with future realization of benefits.

Identifying the Right Life Settlement Company

An evolving market, the life settlements industry has grown leaps and bounds in the last few years. It is important for life settlement brokers and agents to understand the life settlement market and the players with whom their clients will enter agreements. First, brokers and agents should do their due diligence by gathering information from several competitive companies and targeting those whose senior management has had the most life settlement experience. German company Scope Group ranks and rates life settlement companies; so far it is the first and only company to do so. Scope offers information on its Web site at www.scope-group.com. Agents and brokers should seek companies with an A-rating or higher.

In addition, the following due diligence guidelines can help agents make the right choice for themselves and their clients:

- Look for proven industry experience, preferably at least $500 million in purchased aggregate face value to date.
- Confirm that the company is funded institutionally and will not re-sell the contract to an individual investor.
- Check with the state attorney general's office or state insurance department for any complaints or legal action against the settlement provider.
- Insist on a settlement provider that uses reputable, independent financial institutions to hold the money in escrow until the change of ownership closes.
- Determine and disclose all tax implications to your client.

Larry Simon is director, chief executive officer and president of Life Settlement Solutions, Inc., based in San Diego, California. LSS and its management have an established, proven industry record, having purchased life insurance policies with nearly $1 billion aggregate face value to date. For more information and to determine if a life settlement is the right option for your client, contact Life Settlement Solutions at 858/576-8067 or visit www.lss-corp.com.