

INSURANCE MARKETING

THE PREMIER RESOURCE FOR MARKETERS OF LIFE, HEALTH, AND FINANCIAL PRODUCTS

# RIDING THE LIFE SETTLEMENT WAVE



# How BGAs can get involved in this growing market

BY GREGORY SCHMITT AND LARRY SIMON

**S**elling a life insurance policy through a life settlement may be a major step for a policyholder, even if the policyholder is a high-net-worth client, but marketing life settlements to this group can present a unique set of challenges. As with other life insurance-related products, the most important consideration for BGAs is demonstrating to customers the value of those offerings.

Many agents have helped scores of clients choose an appropriate life insurance policy based on clients' projected end-of-life needs and desires. Smart agents know that as the years go by, their clients' lives and financial needs can drastically change. In fact, as many clients approach their 70s and beyond, life insurance products may make up a disproportionate amount of their net worth. Until recently, most individuals in this situation had no choice but to continue paying premiums, let their coverage lapse, or surrender policies for a minimal cash value.

Let's take, for example, an agent who facilitated life insurance coverage for a client 15 years ago. This client survived a major heart attack this past year. He 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.

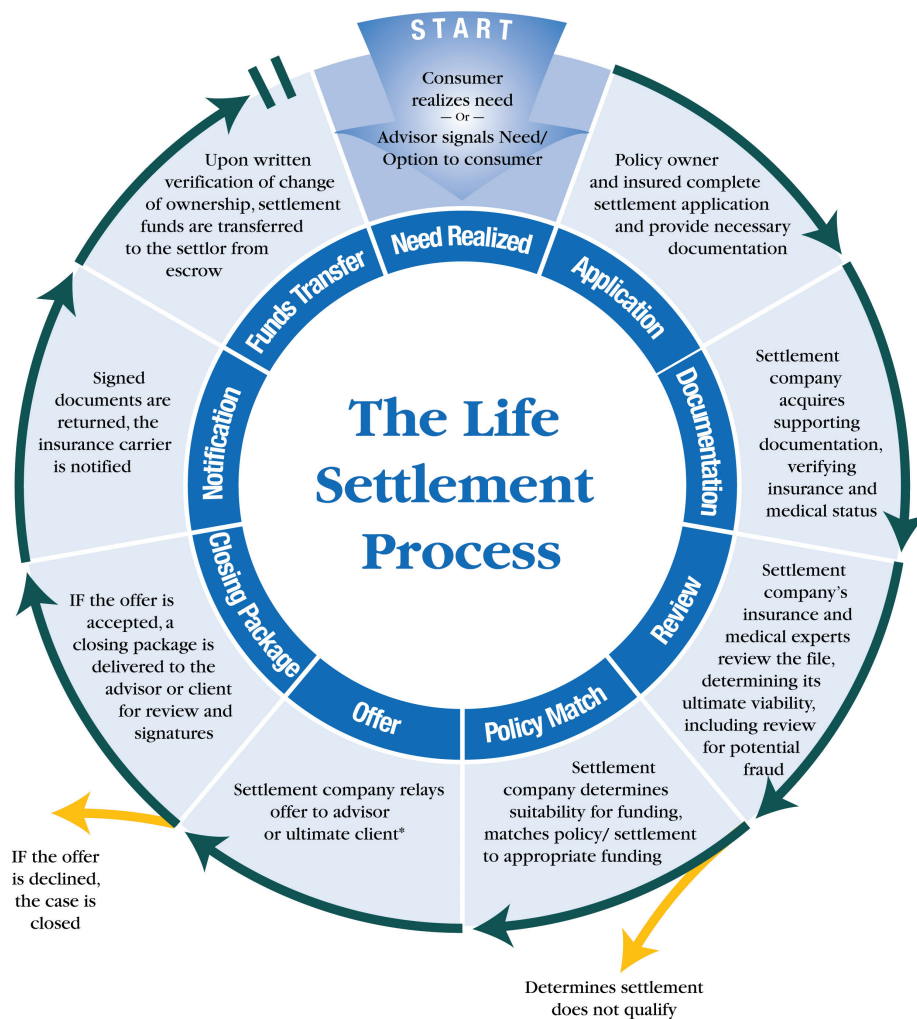
Life settlements, also known as senior settlements, enable seniors to sell unneeded life insurance policies in a secondary market for an

amount greater than the cash value offered by their insurance company but less than the death benefit. Life settlements give seniors access to funds they might have otherwise lost had they let their policies lapse or surrender — something that occurs with nearly 80 percent of universal life policies, according to a June 2005 report by Bernstein Research.

## How life settlements work

With a life settlement, a life insurance policyholder sells the benefits of the policy to an investor, typically a large bank or other institutional investor. Most investors do not directly negotiate with policyholders; rather, they provide financing for life settlement companies that negotiate pricing and compensation with a broker or agent. The producer, in turn, acts as the fiduciary representative of the policy owner for the purposes of establishing a purchase price. The life settlement company is the contracting party that enters into an agreement with the policy owner for the sale of the policy and is often the company that manages post-settlement servicing of policies on behalf of the institutional investor that becomes the new beneficiary of the policy.

A good candidate for a life settlement typically has \$500,000 or more in universal life coverage, although any type of life insurance or irrevocable life insurance trusts may qualify. The policy must have been issued within the past two years or more, in most cases by an "A" rated U.S. insurance company.



\* Settlement companies can work with the advisor or directly with the ultimate client (the policy holder or the insured), depending on the wishes of the advisor.

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In addition, policies considered for purchase by life settlement companies must meet certain eligibility requirements:

- The policy must be beyond any carrier or statutory contestability period, fully renewable, and subject only to the payment of premiums.
- The insured's life expectancy must be between 25 and 168 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 should not exceed \$20 million, although a handful of companies can purchase policies greater than this amount.

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.

If an offer to purchase the policy is to be extended to the owner, the results of these medical evaluations, along with the information derived from a policy illustration generated by the insurance company that issued the policy, serve as the basis for determining the bid price that will meet investment criteria as established by capital funding sources.

If a policyholder accepts the life settlement company's offer, he or she relinquishes ownership and beneficial interest in the policy in exchange for a cash payment. As the new policyholder, the investor must maintain all premium payments in order to keep the policy in force. The concept is much like the buying and selling of mortgage contracts — in this instance, an insurance contract is bought and sold with the investor acquiring both the

beneficial interest in the contract and the obligation to provide for servicing and administration of the contract.

The market exists primarily as an alternative to surrender values payable by life insurance companies when a policy owner decides to redeem or cash in the policy. These surrender values are often lower than what a qualified life settlement provider company can pay.

### Getting involved in the life settlement market

Before an insurance marketing group gets involved in this market, it should assess the demand for life settlements from its agent distribution force and whether its agents' brokers-dealers approve of these transactions. If the demand exists and approval is given, insurance marketing groups should:

- Fully research and understand the appropriate and inappropriate situations for life settlements.
- Conduct legal and compliance due diligence to understand state licensing requirements, proper errors and omissions insurance coverage, contract development for agreements between the marketing group and agents, HIPAA requirements, record-keeping, and requirements for brokering settlement contracts.
- Evaluate whether to work through a broker or directly with providers.
- Conduct interviews with brokers and funders to understand the advantages and disadvantages of working with each.
- Develop marketing programs for use with a distribution force to train them on the benefits of life settlements.
- Generate a case flow.
- Build infrastructure and staff to process, package, and obtain market value assessments of each contract.
- Track information on all life settlement cases, including the status of each case, and communication with agents and insureds. Technology is a key component of tracking a large volume of cases at various stages.

### A market positioned for growth

Encouragingly, the findings of the March 2006 study by the Agent's Sales Journal, the sister publication of Insurance Marketing magazine, revealed agent demand for life settlements is on the verge of exploding onto the mainstream insurance scene (See page 14 for study results). The nationwide survey of



licensed insurance agents indicated that although fewer than two in 10 agents (18 percent) have ever performed a life settlement transaction, the market intrigues them. More than one-quarter (27 percent) say they are likely to perform a life settlement transaction in the next year.

Further, 73 percent of agents said they do not anticipate offering life settlements in the foreseeable future. The reason? A lack of information. Six in 10 agents said they do not feel they know enough about life settlements. Even those who have never performed a life settlement transaction believe that it would benefit clients as a financial planning tool (71 percent).

What's clear is that while agents want to learn more about life settlements, they need a resource they can turn to for more information. Insurance marketing groups (BGAs, MGAs, IMOs, FMOs, etc.) can provide a solution by doing research, working with life settlement providers, and supporting agents who want to serve their high-net-worth clients via life settlements.

### *What to look for when partnering with a life settlement company*

Insurance marketers should perform due diligence by gathering information from several competitive companies, targeting those with the most experience, best resources, and best reputation. Additionally, a life settlement company should have an excellent senior management team providing life settlement, life insurance, legal, and investment banking experience.

Further, the insurance marketing organization should determine whether it is possible to conduct the broker services of packaging cases, running policy illustrations,

obtaining life expectancy reports and obtaining market price offers from various funders. If not, the organization should work through an established, experienced broker who has relationships with top funders in the industry that will adhere to independent marketing organization/agent non-circumvention agreements.

When evaluating life settlement providers, here's what to look for:

- Providers that are experienced and ethical. Regulation of life settlements is not the same in all states, and some states do not regulate the industry at all.
- A life settlement company that is licensed or otherwise qualified to do business in the state in which the insurance marketing organization resides.
- Proven industry experience, with preferably at least \$1 billion in purchased aggregate face value to date.
- An institutionally funded company that will not re-sell the contract to an individual investor.
- Any complaints or legal action against the settlement provider. This information can be obtained by checking with the state attorney general's office or state insurance department.
- Companies with the ability to provide marketing support functions and expertise.
- Established communication processes to provide an up-to-date status of each settlement transaction.
- Documentation of pricing offers received from multiple funders to ensure a competitive process.
- Compensation disclosure.

Of course, there are times when it is not a good idea for a BGA to get involved in this market. For example, there may be times

when their broker-dealer prohibits involvement in life-settlement transactions due because of discomfort bred from an unfamiliarity with the industry, securities supervision issues, or a lack of sufficient supervision or infrastructure to effectively process the expected volume of settlement transactions. Further, the BGA must assess the expected revenue from this line of business to ensure that they can meet their goals based on added infrastructure and a reasonable return without having to depend on unreasonable compensation. Firms must also ensure that they are properly licensed to transact settlements based on the laws of the states in which they are located and represent clients.

Many BGAs can significantly enhance their practices by establishing an efficient, ethical life settlements operation. By providing this alternative to customers with unneeded life insurance, they can turn a policy lapse event into a value-added service to the customer by providing funds to purchase more appropriate life insurance, fund investment programs, prevent future policy lapses, retain customers, and generate additional sources of revenue.

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