

Robin & Peter on LIFE SETTLEMENTS



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Life Settlement Opportunities for Business Life Insurance

Life settlements are frequently viewed, primarily, as an option for personal life insurance and estate planning policies that are no longer wanted, needed or affordable. However, business-owned policies or personally-owned business purpose policies can also make excellent life settlement candidates, yet these policies are often overlooked.

When a business owner leaves, whether due to retirement, disability or the sale or liquidation of the business, advisors should be alert to the possibility of a life settlement. Quite often, the business will own or be paying for any number of policies on the life of the departing owner.

Life insurance policies are purchased by businesses for a variety of reasons: to fund a buy-out of the owner's interest under a stock redemption arrangement, for key person purposes to offset the financial loss that would have been sustained by the business had this person died prematurely, or for creditor protection purposes to secure loans that may have been made by the business. In some instances, policies are not owned by the business itself but rather by co-owners of the business to fund a cross purchase arrangement.

Although sometimes the exiting business owner will have a use for some of the coverage, a significant portion of the insurance may no longer be needed, wanted or affordable. A very large percentage of policies bought for buy-sell arrangements and key person needs are term insurance. So in addition to having a decreased need for coverage, the rising cost of the term insurance may be quite unappealing, if not altogether unaffordable, especially for an aging retired business owner.

Term insurance, that is convertible to universal life, can be an excellent prospect for a life settlement. Yet producers often overlook these policies under the mistaken belief that term insurance cannot be sold in a life settlement.

Sometimes it is desirable to keep a portion of the coverage in force. Permanent life insurance, generally, cannot be split for a life settlement. But term insurance has the additional advantage that a portion can be sold in a life settlement and the balance of the policy retained.

For example, a retiring business owner sold his business which was paying for a \$3 million term insurance policy on his life. He did not want, nor could he afford, to continue paying for the policy out of his own pocket. However, he did want to keep \$1 million in force, but he wasn't sure he could afford even that. \$2 million of the policy was converted and sold in a life settlement transaction and he was able to convert the balance, personally, by using the proceeds of the life settlement.

Life insurance funded executive benefit arrangements, such as deferred compensation and split-dollar plans, are also significantly impacted by the departure of a key executive or business owner. While policies bought for deferred compensation plans are often, but not always, retained to pay benefits or to reimburse the company for those payments upon death, in some situations a life settlement may be a more attractive option. Split-dollar plans, that were intended to be rolled-out with minimal tax consequences, are no longer being given such favorable tax treatment. A life settlement can provide an attractive exit strategy from a split-dollar arrangement.

Qualified pension and profit-sharing plans also may own policies on retiring business executives. Although these policies must first be transferred to the insured to comply with ERISA, they are also candidates for a life settlement.

When a business changes hands, is liquidated or is reorganized and owners or executives leave or retire, there are often life insurance policies left behind that were purchased for purposes or needs that no longer exist, or the policies simply become unaffordable. A life settlement can bring unexpected value from these policies which can make a meaningful difference in the lives of business owners and executives. As a trusted advisor, you owe it to your clients to bring this valuable option to their attention.

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