

# Robin & Peter on LIFE SETTLEMENTS



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## The 3 Rights of Life Settlement Prospecting

Three crucial elements must be present for a successful life settlement case: 1) the right insured, 2) the right policy, and 3) the right situation. When any of these key components are missing, it means the case is undoubtedly not a prospect.

### The Right Insured

Generally prospects should be age 70 and above with some decline in health since the policy was issued. Typically, the insured is now highly rated or uninsurable. The younger the insured, the more significant the health issues must be. Occasionally policies sell at younger ages, but the insured would have to have very, very serious and predictable health problems (i.e., ALS, metastasized cancer).

### The Right Policy

Universal life and term that is convertible to universal life are the most attractive contracts to investors. Term policies are frequently overlooked by producers, even though they often make excellent life settlement prospects. Whole life policies, on the other hand, which build significant cash values, would need to attract offers that exceed the surrender value and that rarely happens.

Survivorship policies with only one insured still living also make excellent settlement prospects. If both insureds are still alive, survivorship policies are not commonly purchased, but it is possible if both are in very poor health.

Generally face amounts of \$500,000 and up are preferred, but there are exceptions that go down to as low as \$100,000. The smaller the face amount, the shorter the life expectancy has to be for settlement buyers to be interested. Additionally, life settlement buyers want policies from well-rated insurance companies.

## The Right Situation

Simply put, ***the right situation is when a policy is about to be lapsed or surrendered.*** A life settlement is an alternative to terminating a policy, not to keeping one. So look out for those situations where a policy is likely to be terminated. There are many reasons a policy may be lapsed or surrendered, but certain scenarios seem to be the most common for a life settlement.

- **Term policies or riders that are about to expire or come to the end of their current premium guarantee or lose their conversion privilege.** Term policies are the life settlement prospects which are most often neglected. Many advisors and clients don't realize that a term policy (including group term), if convertible, can be sold in a life settlement. Since term policies almost never have cash surrender value, a life settlement can truly provide "found" money.
- **Retirement.** People commonly review their financial resources and expenses upon entering retirement. At that time, it is not unusual to find policies that are no longer needed that were bought to replace income upon the death of a wage earner. Additionally, the cost of such policies, especially if term insurance, may become unaffordable. These policies can be great candidates for a life settlement and the proceeds can really make a difference in retirement. With the aging and retirement of baby boomers, they represent a massive market for potential life settlements.
- **The policy is no longer affordable due to policy performance.** Interest rates have been at historic lows for an extended period of time. Many policy owners are now being blindsided by premium requirements that dramatically exceed what they expected to pay when the policy was issued. In addition, premium increases may also disturb their estate plans by exceeding their annual gift tax exclusion.
- **Chronic illness.** While chronic illness would ordinarily be a time when the death benefit of a life insurance policy would seem most imminent and most valuable, certain illnesses are long-term in nature and require very costly medical or custodial care. When all else fails, a life settlement can provide critically needed funds to help pay for those expenses.
- **A decrease in estate tax liability.** The Tax Cuts and Jobs Act of 2017 (TCJA) not only reduces the number of estates subject to federal estate tax to an estimated 1,800 annually, but also substantially reduces the estate tax liability for those estates that remain subject to the estate tax. As a result, some policies purchased to offset estate taxes are no longer needed for that purpose. While holding on to the policy might still be a good deal for their heirs, people are usually reluctant to keep more life insurance than is absolutely necessary.

- **Business owners exiting their business through retirement or sale.** When a business is sold, a policy bought for a buy sell agreement or estate liquidity may become unnecessary. In the course of operating their companies, business owners frequently acquire a number of life insurance policies for reasons other than buy sell that also become unneeded or unwanted when they exit the business. These include key person, fringe benefit, creditor protection and even pension policies. Typically, the business was paying for these policies in some manner; either directly, if the policy had been business owned, or indirectly, through the use of a bonus or split-dollar arrangement. With the business no longer in the picture, both the need for the policy and the ability to pay for it may have evaporated.

Using the concept of “the three rights” can be a simple and effective way to describe to accountants and attorneys the type of scenarios that can be life settlement prospects. Sharing this information with those advisors will help uncover life settlement opportunities and establishes you as a life settlement resource.

The sale of an insurance policy can offer significantly greater salvage value than accepting the insurance company’s surrender value, if any, for a policy that is about to be lapsed or surrendered. This additional cash can make a meaningful difference in the lives of your clients. But to have a real prospect you need recognize the right insured, the right policy and the right situation.

As situations come up, please don’t hesitate to give us a call. It can’t hurt to try – it can only hurt not to!

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