Unlocking the Value in Business Insurance

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Businesses have long recognized the value of life insurance protection, and have employed life insurance contracts to meet a wide variety of needs. In this difficult economic environment, many business organizations may find that they have a "hidden" asset on the balance sheet: life insurance policies previously purchased for specific purposes can sometimes be converted to cash via the secondary market for life insurance—life settlements.

A life settlement involves the purchase of a life insurance policy by an unrelated third party for an amount in excess of the cash surrender value. Life settlements are typically available for insureds over the age of 70, or those whose health may have become significantly impaired over time.

Business Life Insurance

There are a number of circumstances where business-owned life insurance policies are employed. Businesses often procure coverage on highly valued employees (key man insurance) to mitigate against the loss of income and/or the cost of finding a replacement for an employee or owner who performs a vital role in the day to day operation of the enterprise.

Another common use of life insurance contracts is to fund the transfer of ownership in the event of the death of a partner or major stockholder (buy/sell insurance). In these programs, the insurance is usually owned by either the business itself (or the key owners) and the premiums are paid with business funds. In addition, many business organizations have beneficial ownership and control of policies which reside within trusts designed to provide employee benefits of various kinds (Section 419 plans, qualified pension plans, non-qualified deferred compensation plans, etc.).

Finally, some businesses have set up corporate owned life insurance (COLI) plans to fund future liabilities (such as post-retirement health care) that must be recognized currently on the balance sheet.

Once these programs are in place, they are often "forgotten." Premiums are typically paid via automated payment programs and little attention is paid to them until and unless an insured employee actually dies and a claim needs to be filed. It is in fact not uncommon for businesses to continue paying premiums long after the insured employee has retired or otherwise left the organization.

Unlocking the Value

For businesses which do own policies of one sort or another, the first step is obviously to determine whether the coverages are still serving a valid business purpose. If it is determined that they do not (or that any cash generated through a settlement could be put to a better use), the next step is to determine which policies might be good candidates for settlement.

Life settlements are generally available when the insured is 70 years of age or older, so any insurance policies that are still in force on employees who have retired or otherwise left the business are a good place to start. In some situations, owners or key employees may still be active in the business despite being well past "normal" retirement age, and those policies may also be viable candidates for settlement.

Policies on younger individuals may also qualify for settlement where the insured has undergone a significant change in his/her health status—insureds as young as age 60 may be candidates. Situations where the insured is terminally or catastrophically ill (as evidenced by a life expectancy of two years or less) may qualify for a "viatical settlement" or accelerated benefits under the policy itself.

When policies are identified as potential settlements, the first step is to engage a qualified life settlement broker to evaluate the situation. Typically this involves filling out an application and obtaining a current illustration to maturity (minimum level premiums to 100). Based upon this information the broker can perform a preliminary valuation and determine whether or not there is likely to be a market for the policy.

Many business organizations may have "hidden assets" on their balance sheets in the form of unneeded life insurance policies. Advisors can perform a valuable service by helping these organizations identify and convert their assets into working capital. FA

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