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Which Policies Work as Life Settlements?

By Steve Shorrock, ChFC, CLTC, FLMI

I receive phone calls on a daily basis from agents about the viability of selling a life insurance policy in the secondary market. Since life insurance is property, insureds have the right to sell a policy which has become unwanted or unneeded. A Supreme Court decision nearly 100 years ago, the landmark 1911 Grigsby vs. Russell ruling, confirmed this principle.

As with any other marketplace, some products are more in demand than others. Essentially, the secondary market is not significantly different from the primary market. Life insurance carriers will sell coverage within certain parameters based on their underwriting, and funders of life settlements will buy polices based upon their own investment criteria.

2009 was a difficult year on many fronts, including the secondary market for life insurance. Although the number of policy owners interested in exploring the life settlement option actually increased due to the economic hard times, the financial crisis had a huge impact on the capital markets. As a result, the number of potential buyers and the capital available for the purchase of policies declined dramatically. By some estimates, the number of completed settlement transactions during 2009 declined by as much as 80% from the prior year.

New sources of buying power have recently entered the market. For the moment, the sweet spots are:

- Universal Life or Survivor Universal Life with one insured deceased.
- Term insurance which is convertible to universal life.
- Face amounts of $100,000 to $5 million.
- Insureds in their late 70s and 80s.
- A life expectancy (LE) under 12 years.

Less preferable are Whole Life policies as these are much more rigidly structured without the same flexibility of a Universal Life policy. The funder could not take money out of a Whole Life policy except through a loan, whereas a UL policy allows for more ready access. Also, Whole Life typically has higher premiums and a higher cash value, both detrimental to a sale in the secondary market.

Variable Life policies can be as challenging to settle as Whole Life. There is only a small group of funders looking for variable policies due to the complexity of the product. And since FINRA, the Financial Industry Regulatory Authority, has determined that Variable Life insurance policies are considered securities, the parties who can sell, buy, transfer or be compensated for transactions are governed by laws and regulations in addition to applicable life settlement regulations.

The market for financed policies (even full recourse) continues to be very limited. A recent survey found that 50% of seniors are not aware of the benefits life settlements can provide and are deprived of that opportunity. Recent life settlement regulation in some states requires life insurance companies to notify the policy owner that a life settlement is an option to surrendering or lapsing the policy. Indeed, you as the agent have the fiduciary responsibility to discuss this option within your older clients' financial plans, especially if the policy fits the parameters listed above. FA

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