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By Lisa Rehburg

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There is almost $20 trillion dollars of life insurance in force in the United States. In 2019, roughly eight million life insurance policies were lapsed, meaning clients stopped making the premium payments and let them go (American Council of Life Insurers, 2020). More significantly, $100 billion of face value is lapsed by people over the age of sixty-five *each year* (Life Insurance Settlement Association, 2022). Some of these may be your clients, and they may have no idea that they're abandoning money.

Your client's life insurance policy is an asset that they own, just like their car or house. As an asset, it can be sold for cash. The process of selling a life insurance policy is very much like selling a house, which is a familiar process for clients. Drawing the comparison between selling a policy and selling a house may help clients to understand not only *why* selling a life insurance policy may make sense, but also the process of doing so.

In this article, you'll learn how life insurance settlements function much like real estate, why people might choose to go through this process, and how you and your clients can transform these assets for mutual benefit.

Similarities to Real Estate

Does a house always fit your needs during your entire lifetime? For some people, yes, but for most, no. Perhaps over your lifetime, your house may become too small or too big, too far away from family, too far away from the office, etc. When your house no longer suits your needs, you sell it, right? In a similar fashion, the same can be true of a life insurance policy.

A 2010 survey prepared for the Insurance Studies

Institute estimates that 90% of seniors, had they known about a life insurance settlement, would have considered it. In addition, 49% of advisors cited lack of knowledge as the reason for not recommending life insurance settlement options to clients (Life Insurance Settlement Association, n.d.-a).

Real estate transactions and life insurance settlements sound so different, don't they? But they are really quite similar, and knowing this may help clients, and their advisors, feel more comfortable considering a life insurance settlement. Here's how life insurance policies and real estate both:

1. **Are assets**. Everyone understands their house is an asset, but a life insurance policy? Yes. In 1911, a Supreme Court decision, *Grigsby v. Russell*, defined a life insurance policy as an asset. Justice Oliver Wendell Holmes said in his statement of decision, "it is desirable to give to life policies the ordinary characteristics of property…to deny the right to sell except to persons having such an interest is to diminish appreciable the value of the contract in the owner's hands" (1911). The result? A life insurance policy (any kind, including term policies) can be sold and transferred to anyone the owner wishes, just like a client can transfer their home to whomever they wish. The process of transferring ownership involves simply signing an insurance company's Change of Ownership form, which each carrier has. This is like signing over the deed to your property. The new owner takes over the policy, as the new owner of the house takes over the property.
2. **Can be sold.** Because a life insurance policy is deemed an asset that can be transferred to whomever a client wishes, it can be sold, just like a house. The process of selling a life insurance policy is called a life insurance settlement, or a life settlement, for short. A life settlement is simply the sale of a client's life insurance policy to a third party, usually an investor group. The client receives a lump sum of cash today. In exchange, the buyer becomes the new owner of the policy—the new payor of the premium—and collects the death benefit when the client passes away. Like a buyer of a house purchases the house that fits their needs, so investors purchase policies that fit their needs, to increase the performance of their portfolios and to diversify their holdings from market fluctuations.
3. **Have a fair market value**. When you want to sell your house, do you call your mortgage company and ask them what they will give you for it? Of course not. In a similar way, when a client calls their insurance company to surrender a policy, that is essentially what they are doing. But your home has a fair market value in the marketplace, and so does a life insurance policy. Studies show that selling a life insurance policy through a life settlement can generate more than four times the cash surrender value of the policy (London Business School, 2013). Even term policies have value and can be sold.
4. **Can be marketed direct or through a broker.** When you sell your house, you have the option to market your home to buyers directly or to use a real estate agent. When you market your own home, you save commission, but you have to do all of the work. More importantly, how do you know if the offer received is the best one in the market? The vast majority of people enlist an experienced real estate agent who knows the marketplace, how to present a home in the best fashion, and how to market the home to obtain the best value. In exchange for these services, a real estate agent usually realizes a commission when the home is sold. The same is true of life settlements. Clients always have the option of going directly to investor groups, to avoid commission. But how do clients know if they received a fair offer for their policy? There are no "comps" for life insurance policies, the way there are for houses. Investors, understandably, are trying to obtain a policy for the least amount of capital expended. A life settlements broker is very similar to a real estate agent in that they represent the client, know the market, know all the different investor groups, the types of policies investors are looking for, and can market the policy to many investor groups to leverage offers to obtain the best value for the client's policy. A commission is paid only when the policy is sold.
5. **Have similar sales time frames.** From engaging a real estate agent to the close of the sale when the client receives their funds, selling a house is usually a multiple-month process. Similarly, from the time a life settlement application is received by a broker or direct buyer, to the time the client receives their funds, the time frame is usually three to five months in order to properly obtain information and market the policy. Medical records must be obtained in order for the buyers to evaluate a client's life expectancy, as well as illustrations from the carrier to show premium projections into the future. From the time an application is received, it can be 60 to 90 days

before investors make an offer. If doctors return records faster, or if a client has their records up front, this can significantly reduce this time frame. If an offer is made and accepted, it is usually four to six weeks for the process to complete.

6. **Go into escrow**. Escrow is opened in both life settlements and real estate once an offer is received and accepted. In both instances, escrow protects the client during the process of changing ownership. The buyer deposits the sale money into escrow. During escrow, the change of ownership and change of beneficiary forms are sent to the carrier. Once the carrier processes these forms and confirms the changes have been made, escrow is closed. Within one to three days, the client will receive their money, either by check or wire transfer, whichever the client prefers.
7. **Result in unrestricted funds**. When you sell your house, are the sale proceeds restricted in any way? No. You can do anything with the money that you wish, right? The same is true of selling a life insurance policy. Clients can do anything: save for retirement, pay for long term care needs, travel, donate to their favorite non-profit, etc. Proceeds are unrestricted; however, the funds may be taxed, just like if you have a gain on the sale of your house. The good news is, thanks to the Tax Cuts and Jobs Act of 2017, the taxation on life settlements proceeds is much more favorable (Weinberger & Katz, 2018). The premiums that are paid into the policy are a basis, which can be deducted from the policy sale proceeds. Therefore, if the policy sale proceeds are below the premiums paid into the policy since the inception of the policy, there should be no tax to the client. If the policy sale proceeds are higher than the basis, the amounts received up to the basis are free of income tax. Amounts received in excess of the cash value are treated as capital gains. In some cases, with universal life or whole life policies, there could be a small window of ordinary income tax due between the basis and cash value. Clients should always consult their tax professionals before they sell their policy to receive guidance on their personal tax implications.
8. **Have consumer protections**. Like real estate, there are state-mandated disclosures that clients must sign to make sure they understand all aspects of life settlements. The transaction is very transparent, including the sign-off of all beneficiaries and commission disclosure. The investor groups themselves go through an extensive registration process with each state in which they do business, and many states require that they post bonds. Many states also mandate that investors annually file the details of the policies that have been purchased. Life settlement brokers also need special licensing. To find a reputable life insurance settlements broker, look to see who focuses on educating clients—not selling them. Also, ask them how long they have been in business, do they focus only on life insurance settlements, are they licensed in your state, how many buying groups do they have access to, do they have a fiduciary duty to their clients, and what are the commissions? Research their website and interview them to be sure you are comfortable working with them. The Life Insurance Settlements

Association (www.lisa.org) has additional resources on their website.

Life settlements are highly regulated by Departments of Insurance across the country (Life Insurance Settlement Association, n.d.-b). To inquire about the specific regulations for your state, simply do an internet search for "department of insurance" and your state to find the website for the entity regulating your state's insurance practices.

Why Clients May Want to Consider Selling Their Policy

Over time, our life insurance needs may change, making policies no longer needed, wanted or affordable. Maybe a spouse has passed away, the house is now paid off, a business or key asset has been sold, the premiums no longer fit into a retirement budget, or a term policy may be coming to the end of the term.

Almost all term policies are "convertible," meaning that the policy can be converted from a term policy to a permanent policy like universal or whole life, with no health questions. This can be done easily with a conversion application that every carrier has. Sometimes, a client may wish to convert only a part of their term policy to a permanent type of policy and plan to walk away from the balance of the policy.

Some policies, typically universal life policies, may be "blowing up" or "imploding," meaning the cash values have not grown as much as they were initially illustrated to do, due to a lower interest rate environment. In these cases, clients are faced with dwindling cash values and the prospect of having to put more money into the policy to pay for the ever-increasing cost of insurance. These policies have become unaffordable to maintain.

Or, perhaps, a client is trying to find a way to pay for long-term care needs: assisted living, memory care, home care, aging in place, etc. A client with health impairments may look to "repurpose" this asset to help make their life more comfortable while they are here.

How Much Are Policies Worth?

This is the big question, right? The short answer is, policies can be worth nothing, tens of thousands or hundreds of thousands of dollars—even, sometimes, millions. The buyers will look at the premiums that need to be paid into the policy, a client's life expectancy, and the face value (i.e., death benefit) of the policy, among other factors, to determine if a policy is worth an offer and how much an offer should be. The smaller the premiums are relative to the face value of the policy, the more valuable the policy because the buyers do not have to pay as much into it to keep it going. The shorter a client's life expectancy, the more valuable the policy, because the buyer will receive their return faster. Investor groups are typically looking for clients with 10 to 15 years (sometimes 20 years) of life expectancy or less. There are no age restrictions, but the older a client is, the healthier they can be to qualify for a life settlement. The younger a client is, the more health impairments to qualify, in order to fit into that 10- to 15-year life expectancy window. Lastly, logically, the higher the face value of the policy, the more potential value because the pay-off is higher for the buyer.

The values of policies are specific to each client. Their policy, premiums, and life expectancy are all unique to them. Here are three real client examples, all of which concern $250,000 term policies.

- **Client #1**: Age seventy-eight with cancer. The policy has five more years on the term. He purchased the policy to take care of his wife, but his wife passed away. His new beneficiaries did not need the money, so he decided to sell the policy to make his life more comfortable. The opening offer on the policy was $15,000 and sold for $128,500.
- **Client #2**: Age sixty-eight with liver issues. The policy was coming to the end of the term and the client was not going to convert it to a permanent policy nor continue it in any way. He was going to walk away with nothing. The opening offer was $50,000, and the policy sold for $75,000.
- **Client #3**: Age seventy-two with minor health issues. As with client #2, the policy was coming to the end of the term, the house was paid off, and she and her husband had ample retirement savings. The policy sold for $8,000.

You can see that policies can be worth varying amounts of money, depending upon the unique circumstances of the client.

Benefitting Your Client...and You!

By sharing this information with clients, you can help them…and yourself, too. By now, hopefully you can see how life settlements can benefit clients. They can also benefit you, no matter your area of expertise. First and foremost, by broaching the issue of life settlements, you fulfill your fiduciary duty to your client to explore and present all appropriate options, so with your help, clients can make the best, most informed decision to benefit them and their families. But your business benefits as well, by helping current clients and also by attracting potential new clients who have never heard of life settlements. And, with money gained from the settlement, people may choose to purchase services that you offer that are more valuable to them than their old insurance policy.

Here are some areas of expertise where life settlements can directly benefit your business.

- **Healthcare advisors**. Funds generated can be used to pay for long term care needs, which can allow clients to move into the community of their choice, pay for care management services or patient advocacy, afford home care, or pay for home modifications for aging in place needs.
- **Financial advisors**. Clients will need your expertise to advise them on how to invest the proceeds, generating assets under management. Perhaps, there are additional products that a client may need, such as annuities.
- **Insurance professionals**. There can be commissions generated from the sale of the policy, but also clients may need additional products, such as long-term care insurance, and now have the resources to pay for it.
- **Legal professionals**. Clients may need advice about how to qualify for government programs, such as Medicaid. Perhaps a client will need an Irrevocable Life Insurance Trust (ILIT) or other trust services to assist with keeping these government programs.
- **CPAs/Money managers**. After a sale, clients may now have the resources to be able to pay for the service they need. You are in a unique position to assist clients because of your close knowledge about their finances. You, more than many, will know when a life settlement may be appropriate.
- **Reverse mortgage professionals**. This may seem odd, right? But, if you have a client that is "short to close" for a reverse mortgage, meaning that the client does not have enough equity in their house to qualify, selling a life insurance policy can generate the funds needed for clients to pay down their mortgage enough to qualify for a reverse mortgage.

Seniors walk away from millions of life insurance policies every year, with little or nothing. According to "The Life Settlements Report" released by *The Deal*, 3,241 people sold their life insurance policies in 2020, receiving a combined $848 million (Life Insurance Settlements Association, 2021). There is a very large gap between the number of policies that clients lapse or surrender, and the number actually sold. Clients are leaving huge amounts of money on the table by lapsing or surrendering their policies before they look at a life settlement, simply because they or their advisors don't know, or have misperceptions, about life settlements.

Life settlements are not perfect for everyone. But hopefully, this article makes it easier to explain the process to your clients when a life insurance settlement may be the right option for them. Not all life insurance policies can be sold, but if you and your client have looked at all alternatives, and the decision has been made to lapse or surrender a policy, a life insurance settlement can be of greater value for both of you. Life settlements create "found money" for the client from an asset they didn't know they had, and a revenue opportunity for you, their Certified Senior Advisor. •CSA

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