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Life Settlements: An Effective Tool for Longevity Planning

By SCOTT THOMAS AND JEFF HALLMAN

Seniors in the early years of retirement are faced with a new reality: They may actually live longer than they had expected thanks to advances in health care and medical treatment. While living longer is good news for most seniors, many worry whether they can make their retirement savings last for more years than they spent working.

Insurance and financial advisors are taking note of their clients' angst regarding longevity planning. In some instances, advisors are recommending life settlements as part of the solution to help their clients leverage their financial resources for maximum impact.

Financial goals change as clients age

The pace at which clients are advancing into their retirement years is forcing some advisors to modify their thinking. With one American turning 73 every seven seconds, coaching clients in this age bracket requires deep insight into their changing financial priorities and current state of mind.

Today, a client in their 70's may be primarily concerned with planning for their long-term care to avoid becoming a burden on loved ones. But 20 years earlier, that same client's financial priority might have been to carry large amounts of life insurance coverage to maintain financial stability for family members in the event of his death.

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Life settlement transactions provide insight

For agents and advisors who are looking to evolve their coaching strategies to meet the financial longevity challenges of aging clients, it helps to have unique insight into the financial objectives that motivate seniors to sell obsolete policies.

Based on a recent review of the life settlement cases brokered by Asset Life Settlements, many retired seniors were motivated to sell their life insurance policies in order to achieve the following priorities:

- Fund long-term care and medical expenses
- Enhance retirement lifestyle
- Pay off debt
- Purchase an annuity
- Provide a cash legacy for loved ones or charitable causes
- Maximize current assets/investments; grow existing wealth
- Reduce or eliminate unnecessary expenses

As noted above, the top reasons seniors sell policies are to pay for long-term care and medical expenses. Also cited as top priorities are enhancing lifestyle, paying off debt, purchasing annuities, and providing cash legacies.

Case in point: Life settlement for early stage Alzheimer's

Advisors recognize that longevity also means the potential for a client to develop a degenerative illness such as dementia which typically incurs higher costs in the form of residential care.

We recently brokered a life settlement for a 65 year old woman who had been diagnosed with early stage Alzheimer's. Her financial advisor contacted us and explained that the family's financial objective was to identify an immediate source of funds for her possible future treatment in a quality memory care unit because her condition was advancing rapidly.

In the process of reviewing her financial resources, the advisor noted that she owned a $400,000 term life insurance policy that was no longer needed. Although she and her husband had been planning to let the policy expire at the end of its term, the advisor recommended converting it to a Universal Life policy and then selling the policy in the secondary market. The proceeds could then be used to supplement her existing cash assets to pay for her future residential care.

We submitted the case to 11 secondary market buyers and received only three offers. The case presented a challenge to buyers due to the insured's young age and life expectancy. But in the end, the family agreed to accept an offer for $80,000. Considering that the alternative was to let the policy expire at the end of its term and receive zero cash, the family was grateful to have an additional source of funds to help pay for her future care. While the financial advisor who handled the case received a commission on the term life conversion, he refused to accept any commission on the life settlement so he could maximize the cash proceeds that went to his client.

Maximizing current assets is critical to longevity planning

Aside from selling policies to pay for medical expenses, long-term care and the other reasons listed above, some seniors have cited more unique factors – such as using the proceeds from a life settlement to maximize current portfolio assets, purchase new investments, and reduce monthly expenses.

Financial advisors recognize that a senior client's greatest fear is outliving his/her retirement savings. Their clients are looking to them to maximize and grow their existing assets.

Rather than allow costly premiums to drain the liquidity in the senior's estate or letting the policy lapse, it makes sense to optimize and monetize the asset value of the policy by selling it in the secondary market for the highest possible amount.

A recent study by a major financial services firm revealed that 44% of advisors expect that longer client life spans will significantly impact their businesses over the next decade.

Helping senior clients achieve their fiscal fitness goals sometimes requires thinking outside the box. Maximizing the value of the policy often requires selling the dormant asset in the secondary market and repurposing the cash proceeds in a manner that can generate more wealth and provide greater financial leverage.

For seniors burdened by premium payments for policies they no longer need, their unwanted life insurance policy has ceased to be an asset and has instead become a liability. Rather than allow costly premiums to drain the liquidity in the senior's estate or letting the policy lapse, it makes sense to optimize and monetize the asset value of the policy by selling it in the secondary market for the highest possible amount.

Depending on the size of the death benefit and the insured's life expectancy, the proceeds from a life settlement can result in a substantial cash windfall for the senior and provide additional liquidity to create financial leverage.

Recent market data indicates the average face value of policies sold in the secondary market is approximately $1 million, and that the average settlement value (lump sum payment to the seller) is approximately $250,000. Other market data describes the average paid to sellers based on the amount beyond the policy's cash surrender value. According to the Life Insurance Settlement Association (LISA) and a survey conducted by the U.S. Government Accountability Office (GAO), policy owners in the U.S. received 4-8 times more than the policy cash surrender values from life settlements during the period from 2006-2009.

Irrespective of the methods used to calculate the average amount paid out to policy sellers in a life settlement, the message is clear and powerful. Selling an unwanted life insurance policy and investing the proceeds can be a smart financial move when the circumstances fit.

Some wealthier seniors who already have sufficient financial resources to meet their financial goals are using the proceeds from life settlements in more creative and speculative ways. For example, one of our senior clients used the cash windfall from his life settlement to purchase investments in digital currencies.

Reducing expenses is an important longevity goal for many seniors

For many seniors, maintaining a policy that has outlived its relevance makes little sense. Once the children are grown or the business is sold and the income protection is no longer needed, many policy owners discover that they are better off selling an unwanted policy and using the proceeds in ways that are more relevant to their current needs.

The added consequence of selling an unwanted policy is the fact that it helps the senior "reduce expenses" by eliminating costly premiums that have become a drain on the insured's budget. This is especially true for those owning Universal Life policies where recently their annual premiums spiked dramatically due to increases in the cost of insurance (COI).

But selling the policy does not always mean foregoing death benefit coverage altogether. Some seniors achieve their goal to reduce their premium expenses by selling only a portion of the policy. This type of life settlement transaction is known as a "life settlement with retained death benefit" (RDB).

We've negotiated many RDB life settlement transactions where the policy sellers have maintained a more appropriate (reduced) level of death benefit coverage while also eliminating annual premium payments altogether. In some cases, the seniors were able to (1) free themselves

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of costly premiums, (2) retain a more appropriate level of coverage without any future premiums, and (3) also walk away with a cash windfall.

Selling with confidence: Using a broker is essential

The GAO report mentioned above cited a number of challenges that need to be addressed as the industry moves forward. One of those challenges involves knowing how to receive the highest possible value when selling a policy. According to the following excerpt from the GAO report: "Life settlements can provide policy owners with a valuable option …but policy owners can face challenges in assessing whether they are being offered a fair price for their policy."

It's important for seniors and their advisors to know that selling a policy for the highest possible amount in the secondary market requires a broker. While providers (buyers of policies) may offer to purchase a policy from the senior in a direct transaction, the downside is that the policy seller (senior) will never know whether the amount offered by that one provider is the highest possible value the market (other buyers) will offer. That's why it's important to use a licensed experienced life settlement broker, such as Asset Life Settlements, who negotiates with the industry's top funding sources to receive multiple offers from buyers competing for the purchase of a policy.

One final note about why using a broker is essential. Many policy sellers may not know that a life settlement broker has a fiduciary duty by law to represent the policy seller in negotiating with providers (policy buyers) for the highest possible offer for the seller's policy. On the other hand, providers are not required to demonstrate a fiduciary duty to the seller. Their primary mission is to purchase policies for as little as possible.

Advisors create value for their senior clients

Broadening awareness is key to helping our aging population uncover a hidden solution to achieving financial wellness as they live longer. Unfortunately, many seniors are still not aware of the existence of the secondary market for unwanted policies and each year life insurance lapses by seniors over the age of 65 total more than $100 billion face value.

The good news is that a growing number of financial professionals, estate attorneys and CPAs are creating value for their senior clients by recommending life settlements when it appears to be in the client's best interests. In addition, some states have begun enacting consumer disclosure laws requiring carriers to inform policy owners who may be planning to surrender or lapse a policy about their options, including selling an unwanted policy in the secondary market.

We are happy to be a resource to advisors and/or their clients for any questions you might have about life settlements.

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