8 Myths of Life Insurance Settlements Debunked!

By LISA REHBURG

Ever since Benjamin Franklin helped start the first life insurance company in the U.S. in 1759, life insurance has been a key part of our lives and financial planning. Today, the U.S. is the leading life insurance premium writing country in the world with over 290 million life insurance policies in force amounting to approximately $20.3 trillion in face value. Just policyholders 65 and older have 38 million policies in force with a face value of more than $3 trillion.

But, according to research from the Insurance Studies Institute, 500,000 seniors each year lapse their life insurance policies. That's a big number! To put even more numbers behind that claim, the Life Insurance Settlements Association's (LISA) own research shows that Americans 65 or older leave over $100 billion in benefits on the table each year by lapsing or surrendering their life insurance policies.

Many clients think they only have three options: pay the premium, lapse the policy or surrender the policy. There are more options available, and a life insurance settlement is one of them.

Simply put, a life insurance settlement is the sale of a life insurance policy to a third party (usually an investor group) who gives the client cash for the policy, and in turn, becomes the owner of the policy, pays the premiums, and receives the death benefit when the policy matures. The client benefits from receiving substantially more than the surrender value for the policy. According to a 2014 London Business School Study, "Americans who sold their unwanted life insurance policies, collectively received more than four times the amount they would have received had they surrendered them to their life insurance companies."

Yet, the vast majority of people do not know about life insurance settlements. Even if someone has heard about them, preconceived ideas and misinformation abound. This article outlines some of the common myths, and the corresponding realities:

Myth #1—Only permanent policies can be sold. Untrue! Yes, even term policies can be sold. In fact, term policies represent the second most sold type of life policy sold, behind universal life. How? The key is that the policy must be convertible and the policy cannot be past the conversion deadline. Many term policies, if convertible, have conversion deadlines based upon the age of the client, or on the length of time the client has been insured. Some have conversion deadlines corresponding to the end of the policy term. An important suggestion is, if a client wishes to sell a term policy, plan to start six months ahead of the deadline to allow plenty of time to complete the settlement.

Myth #2—Only the very ill can sell their policies. Untrue! The industry essentially started in the 1980s as viaticals, with terminally ill clients selling their policies to pay medical bills or improve their quality of life. Some people think that is where we still are today, but the market has changed dramatically since then. Even though viaticals still exist, they have a very small impact. Life insurance settlements are completely different, focusing on clients who no longer want or need their policy.

An investor does consider a client's health and life expectancy when determining how much to offer on a policy. It is true that the shorter the life expectancy, the higher the value paid for the policy. But, that does not mean that clients who are relatively healthy cannot sell their policy. An investor also considers the premiums that need to be paid and the face value of the policy in making a determination about how much to offer a client. There are many instances where investors are willing to purchase the policy of a relatively healthy individual. Every client's situation is unique, but their relative health does not preclude them from selling their policy.

(continued on page 21)

Life Settlements Debunked

(continued from page 17)

Myth #3—Only large policies can be sold. Untrue! Each investor has their own parameters surrounding the types of policies they wish to purchase. So often the focus of media articles and blogs are clients who received hundreds of thousands of dollars for their policy. Yes, it is true clients can receive that amount, but their policy also usually has a multi-million dollar face value. Many clients have policies well below $1 million and are mistaken that only larger policies can be sold. The reality is policies as low as $100,000 in face value can be sold, and in some rarer instances, even below $100,000.

Myth #4—Most people sell their policy because they need the money, or need to pay medical bills. Untrue! The life insurance industry has done a good job of adding accelerated death benefits and critical illness provisions to their policies, giving clients additional options, so they don't have to sell their policies in their time of need. Rather, most people sell their policy because they no longer want or need the coverage. Many times, clients purchased the policy 10, 15 or 20 years ago, but now, the reason they originally purchased the policy is no longer relevant. The policy is simply not needed any longer. Some examples are: the client has retired and no longer needs the income replacement; their home is paid off; the client's sale of a business , so the "key man" policy is no longer needed; a rental property or significant asset has been sold, making the policy purchased to cover payment for that asset unneeded. Additionally, the Tax Cuts and Job Act (TCJA) of 2017 also helped make a large number of life insurance policies unneeded. By more than doubling the estate tax exemption from $5.49 million per individual to $11.2 million, and $10.98 million for married couples to $22.4 million, life insurance policies purchased to cover estate taxes also may no longer be needed. This change is estimated to reduce the number of estates subject to the estate tax by about two-thirds.

Policies also become unwanted: a term policy that is about to expire; some universal life policies are becoming unaffordable as they mature; or due to limited income in retirement, policies become too expensive. There are some adjustments that can be made to these types of policies to make them more affordable, but if nothing is appropriate, a life insurance settlement can be a good option.

Myth #5—Clients have to sell the entire policy. Untrue! A client may choose to sell only a portion of their policy. A good example is a client who has a $1.5 million term policy, but is retiring. The mortgage is paid off so she doesn't need all of the coverage and doesn't want to pay the premiums anymore for all $1.5 million, but she still would like some death benefit. She has chosen to sell $1 million of her policy, and retain $500,000 in death benefit.

Myth #6—Only people in their 80s or older can sell their policy. Untrue! As we discussed in Myth #2, age is relevant in determining what an investor will offer for a policy. Generally, life insurance settlements are best for clients age 65 or older, but that is just a guideline.

Myth #7—Only the wealthy clients benefit. Untrue! A life insurance settlement can be a good option any time a policy is not needed or wanted. With policy face values from $100,000 being sold, a life insurance settlement is very accessible for many people.

Myth #8—Life insurance settlements are not well regulated or illegal. Untrue! Believe it or not, a U.S. Supreme Court decision in 1911 paved the legal foundation for life insurance settlements. Justice Holmes said in his 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." What that means is a life insurance policy is an asset, like a car or house. The owner of a life insurance policy has the right to transfer it to whomever they choose. So, life insurance settlements are not illegal, but what about being regulated? The life insurance settlement industry is highly regulated. Forty-three states and the territory of Puerto Rico regulate life insurance settlements, affording protection and transparency for approximately 90 percent of the U.S. The National Association of Insurance Commissioners (NAIC) and the National Conference of Insurance Legislators (NCOIL) have also been very involved in crafting model language and disclosure notices to protect consumers, which have been adopted by the majority of states. Disclosures include transparency in the offer details, sales commissions, alternatives to selling a policy, risks of selling a policy and more. Further, sellers must be deemed competent to enter into a life insurance settlement agreement, and beneficiaries consent prior to a policy being sold. There are also mandatory waiting periods before someone can sell their life insurance policy. In California, the waiting period is two years, with very limited exceptions such as the owner of the policy is terminally ill, a spouse dies, divorce, retirement from full time employment, physical or mental disability, disposition of ownership interests in a closely held corporation or an order or judgment from a court. As a result of this regulation and transparency, there have been no consumer complaints against a licensed life settlement company since 2012.

The Insurance Studies Institute found 90 percent of seniors surveyed would have considered a life insurance settlement, had they known about them.

Lisa Rehburg is president of Rehburg Life Insurance Settlements, a life insurance settlements broker. Rehburg is energized by helping brokers and their clients benefit from unwanted or unneeded life insurance policies. By having access to many investor groups, Rehburg Life Insurance Settlements can place more policies and realize a better return for clients. Rehburg has been working with brokers in the health and life insurance industries for over 30 years. She can be reached at (714) 349-7981, lrehburg@aol.com or www.rehburglifesettlements.com.