

# Life Settlement – A Valuable Asset Hiding in Plain Sight

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## **Life Settlement Disclosures:**

- In a life settlement agreement, the current life insurance policy owner transfers the ownership and beneficiary designations to a third party, who receives the death proceeds at the passing of the insured. As a result, this buyer has a financial interest in the seller's death.
- A policy owner should consider the continued need for coverage. If the policy owner plans to replace the existing policy with another policy, the policy owner should consider the availability, adequacy and cost of comparable coverage.
- Policy owners considering the need for cash should consider other, less costly alternatives.

When an individual decides to sell their policy, s/he must provide complete access to his/her medical history, and other personal information, that may affect his/her life expectancy. This information is requested during the initial application for life settlement.

- After the completion of the sale, there may be an ongoing obligation to disclose similar and additional information at a later date.
- Individuals should discuss the taxation of the proceeds received with their tax advisor.

## Life Settlement Disclosures (cont):

- ValMark Securities, Inc. considers a life settlement a security transaction.
- A life settlement may affect the insured's ability to obtain insurance in the future and the seller's eligibility for certain public assistance programs, such as Medicaid, and there may be tax consequences.
- ValMark Securities, Inc. and its registered representatives act as brokers on the transaction and may receive a fee from the purchaser.
- A life settlement transaction may require an extended period of time to complete. Due to the complexity of the transaction, fees and costs incurred with the life settlement transaction may be substantially higher than other securities.
- Once the policy is transferred, the policy owner has no control over subsequent transfers.
- If you are a buyer of a life settlement or an investor, then you should be aware that:
  - Investment in a life settlement is highly speculative
  - Although a substantial profit may be realized, a substantial loss is also possible.
  - The death benefit may never be paid.

A hand holding a brass compass in front of a mountain landscape. The compass is open, showing the dial with cardinal and intercardinal directions. The background features snow-capped mountains under a clear blue sky, with green valleys in the foreground.

# NAVIGATING LIFE SETTLEMENTS

WHAT IS A LIFE SETTLEMENT?

# Topics

1. What are your options for an unwanted life insurance policy?
2. How does Ohio law protect a policy seller?
3. When does selling a policy make sense?
4. What are some real-life examples?
5. What is the best life settlement process?



“YOU MISS 100%  
OF THE SHOTS  
YOU DON’T TAKE.”

WAYNE GRETZKY

# One of the Most Overlooked Options by Advisors



**49%**

of financial advisors admit they lack knowledge about life settlements<sup>1</sup>



**MORE THAN  
\$112  
BILLION**

of policy face value lapses by seniors over age 65 each year<sup>2</sup>



**8 OUT OF 10**

policyowners didn't know they could sell their policy<sup>3</sup>

<sup>1</sup> The Hidden Value in your Life Insurance, 2016, <http://www.lifehealthpro.com/2013/09/16/>

<sup>2</sup> Life Insurance Settlement Association, 2015, <https://www.lisa.org/life-policy-owners/consumer-blob/blog/2015/02/25/lapsed-life-insurance-policies-an-astounding-number>

<sup>3</sup> The Life Settlements Report, 1/31/2019, <https://pipeline.thedeal.com/article/14851134/Index.dl>

# You Have to Tell Your Clients About Life Settlements



**177,528**

Licensed Life  
Insurance Agents  
In Ohio

**73**

Licensed to  
Facilitate Life  
Settlements

Ohio Department of Insurance 5.1.2021

# Life Insurance is Capital



A life insurance policy is a capital asset, just like your home, stocks, bonds, and your business.

# What is a Life Settlement?



A life settlement is the sale of an existing life insurance policy on the secondary market to a third party for fair market value.

- The owner sells policy in exchange for a lump sum settlement that can be higher than cash surrender value and less than the death benefit
- The, buyer, a third-party institutional investor, becomes the owner of the policy, makes premium payments, and collects the death benefit at the insured's death.
- With institutional investors, policies are owned in large blind trusts with other policies.
- Insured has Life Expectancy (LE) greater than 24 months.

# Who Are The Buyers?

- Insurance Companies
- Mutual Funds
- Hedge Funds
- Private Equity
- Pension Plans
- University Endowments

# Why Are They Buying?

- Greater Return than Bonds
- No Correlation With Stocks or Bonds

# Ohio Protection for Life Insurance Policy Sellers (ORC 3916)

1. Buyer must be approved by the Ohio Department of Insurance
2. Requires full disclosure of:
  - All offers, counteroffers, acceptances and rejections related to the sale of the policy
  - Any affiliation or agreements between the settlement broker and the buyer
    - Identify and disclose conflicts of interest
  - The amount and method of calculating the brokers compensation

## Ohio Protection for Life Insurance Policy Sellers (ORC 3916) (cont)

3. Seller must be paid within three days of written acknowledgement the insurer has changed the policy owner and beneficiary to the buyer
4. The seller has the right to rescind the contract at any time up to 15 days after receipt of payment
  - If the insured dies prior to the end of the 15 day rescission period, the contract is automatically rescinded, subject to repayment of the sales proceeds.

# Why Sell?

## Common Life Settlement Situations

1. The sale of a business
2. Business owner of key person retiring or exiting from business
3. A decline in estate value and/or a decrease in estate tax liability
4. Term policies or rider that are about to expire, lose their conversion privilege, or come to the end of their current premium guarantee
5. Retirement – income replacement policies no longer needed or too expensive
6. Chronic illness
7. The policy has had a significant premium increase due to policy performance, and it is no longer affordable

# The Wall Street Journal

November 16, 2012

***Draining Away!***, by Leslie Scism & Joe Light

*“In the next few years, millions of savers are in for a surprise that could cost them tens of thousands of dollars now – or hundreds of thousands later.*

*The reason: Universal life insurance policies bought years ago when interest rates were high will face cancellation if policyholders don’t pay more.”*

# The Wall Street Journal

September 19, 2018

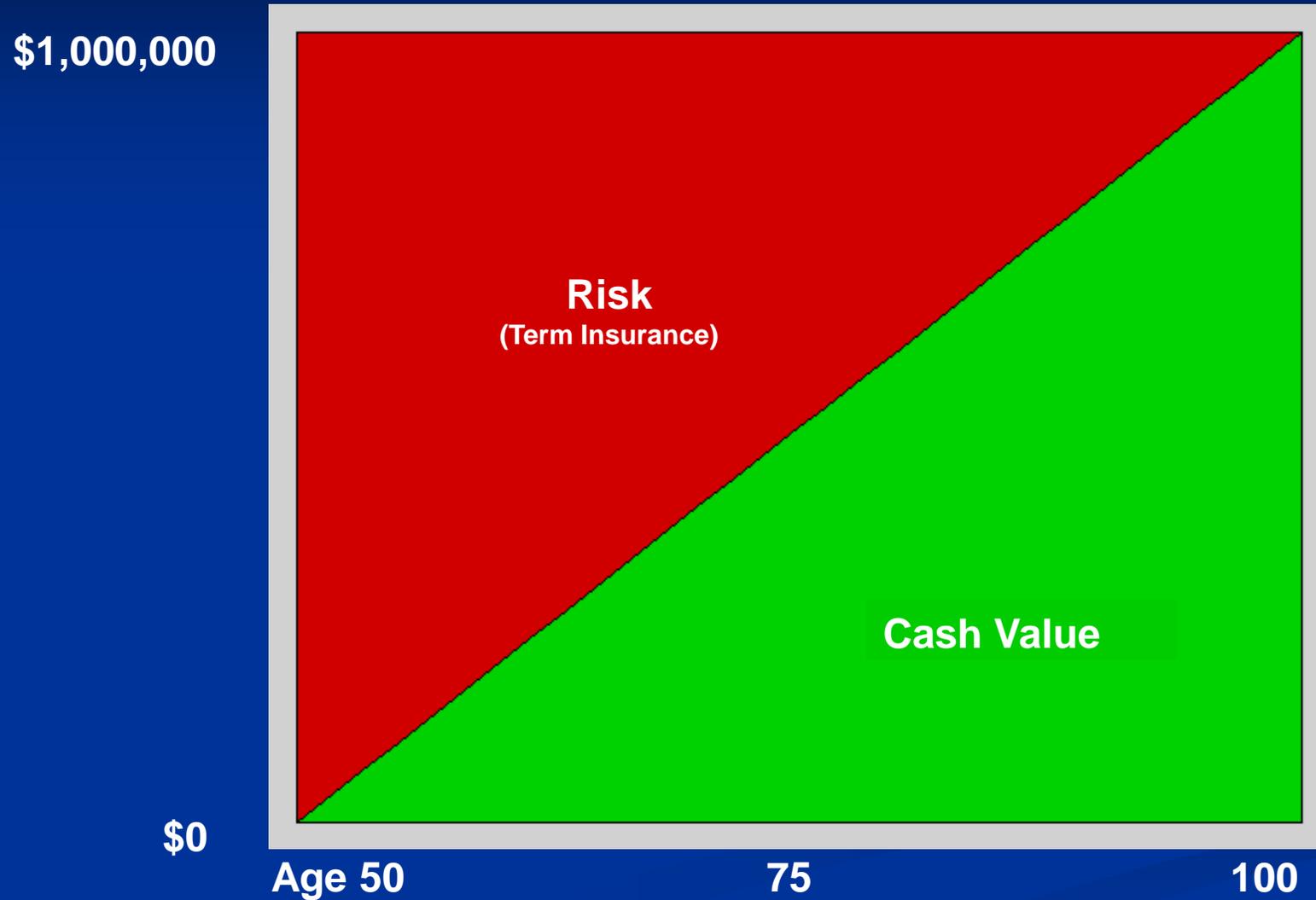
## ***Universal Life Insurance, a 1980s Sensation, Has Backfired,***

by Leslie Scism

*“A long decline in interest rates caused premiums to soar when they were supposed to stay level.”*

# Cash Value Life Insurance

\$1,000,000 Death Benefit



# Life Insurance Company Assets Supporting Policy Dividend Rates

	<u>MassMutual</u>	New York <u>Life</u>	Northwestern <u>Mutual</u>
Cash	2%	2%	1%
Bonds	58%	72%	69%
Mortgages	<u>16%</u>	<u>12%</u>	<u>17%</u>
	<b><u>76%</u></b>	<b><u>86%</u></b>	<b><u>87%</u></b>

# Life Insurance Company Assets Supporting Policy Dividend Rates

Net Yield on Mean  
Invested Assets:

	<u>MassMutual</u>	<u>New York Life</u>	<u>Northwestern Mutual</u>
<b>2019</b>	4.28%	4.38%	4.19%
<b>5 Year Avg</b>	4.62%	4.57%	4.41%

# Life Insurance Company Assets Supporting Policy Dividend Rates

Bond Maturity:

	<u>MassMutual</u>	New York <u>Life</u>	Northwestern <u>Mutual</u>
<b>1 Yr or Less</b>	10.9%	7.3%	6.6%
<b>1 to 5 Yrs</b>	25.3%	27.4%	33.4%
<b>5 to 10 Yrs</b>	<u>26.8%</u>	<u>34.7%</u>	<u>33.5%</u>
	<b><u>63.0%</u></b>	<b><u>69.4%</u></b>	<b><u>73.5%</u></b>

# Life Insurance Company Assets Supporting Policy Dividend Rates

Current Bond Yields  
(5/6/2021)

	Maturity		
	<u>5 Years</u>	<u>10 Years</u>	<u>15 Years</u>
- U.S. Treasury	0.80%	1.57%	1.83%
- AA Corporate	1.05%	2.09%	2.57%
- A Corporate	1.20%	2.31%	2.85%

# Four Options For Policies No Longer Wanted



**1**  
*Surrender/  
Lapse*

**2**  
*Change  
(if possible)*

**3**  
*1035  
Transfer*

**4**  
*Sell  
Policy*

# Life Settlement Process

1. Collect policy information to determine the projected cost of keeping the policy in-force
2. Collect insured's medical history. Medical records only, no medical exam
3. With medical history, get a professional assessment of life expectancy
4. With this information, policy buyers will determine if their investment targets can be achieved by paying more than the cash value for the policy. If so, an offer is made to buy the policy

# Male Age 64

## Policy Summary

### Policy Information

Policy Date	2002
Health Class	250% of Standard
Death Benefit	\$1,500,000
Annual Premium	\$16,147
Cash Value	\$548

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### **Annual Premium Required to Keep Policy In-force**

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9 years, age 73	\$52,000
13 years, age 77	\$60,000

Statistics listed are for illustrative purposes only. Actual results may vary.

# Male Age 64 Life Settlement Life Expectancy

Life Expectancy

Company

Months

Years

A

94

7.83

B

72

6.00

C

28

2.33

# What Does Life Expectancy Mean?

At life expectancy approximately one-half (50%) of the original group is expected to still be living.

We have listed the year-by-year actuarial probability of survival based on the three independent life expectancy reports summarized above.<sup>1</sup>

# What Does Life Expectancy Mean? (cont)

Less than 15%  
probability of survival

<u>Year</u>	<u>End of Year Age</u>	<i>Probability of Survival <sup>1</sup></i>		
		<u>A</u>	<u>B</u>	<u>C</u>
		<u>28 Months</u>	<u>72 Months</u>	<u>94 Months</u>
1	65	77.71%	94.70%	96.80%
2	66	51.93%	87.22%	92.19%
3	67	31.07%	78.88%	86.88%
4	68	15.61%	69.54%	80.67%
5	69	5.56%	58.88%	73.21%
6	70	1.30%	48.15%	65.16%
7	71	0.14%	37.95%	56.84%
8	72	0.00%	28.44%	48.24%
9	73	0.00%	19.85%	39.46%
10	74	0.00%	12.68%	30.86%
11	75	0.00%	7.38%	23.07%
12	76	0.00%	3.84%	16.41%
13	77	0.00%	1.72%	10.93%
14	78	0.00%	0.61%	6.67%
15	79	0.00%	0.14%	3.60%
16	80		0.01%	1.63%
17	81		0.00%	0.57%
18	82			0.13%
19	83			0.01%

1. 2015 VBT mortality table adjusted to the reported life expectancy in the three independent life expectancy reports summarized on slide 31.

# Net Offer Summary

Provider	Initial Offer	Auction / Round													
		<u>1</u>	<u>2</u>	<u>3</u>	<u>4</u>	<u>5</u>	<u>6</u>	<u>7</u>	<u>8</u>	<u>9</u>	<u>10</u>	<u>11</u>	<u>12</u>	<u>13</u>	<u>14</u>
Company 1	\$175,000	High	\$240,000	High	\$270,000	\$285,000	High	\$335,000	High	\$385,000	High	\$445,000	High	\$485,000	High
Company 2	\$119,000	\$224,000	High	\$260,000	High	\$280,000	\$305,000	\$305,000	\$345,000	High	\$395,000	High	\$475,000	High	\$510,000
Company 3	\$140,000	\$182,000	\$240,000	High	\$270,000	\$280,000	\$295,000	\$315,000	\$345,000	High					
Company 4	\$91,000	\$182,000	\$240,000	High	\$270,000	\$280,000	\$295,000	\$315,000	\$345,000	High					
Company 5	\$70,000	\$182,000													
8 Other Companies	No Offer														

Provider	Auction / Round													
	<u>15</u>	<u>16</u>	<u>17</u>	<u>18</u>	<u>19</u>	<u>20</u>	<u>21</u>	<u>22</u>	<u>23</u>	<u>24</u>	<u>25</u>	<u>26</u>	<u>27</u>	<u>28</u>
Company 1	\$520,000	High	\$585,000	High	\$605,000	High	\$655,000	High	\$675,000	High	\$695,000	High	\$725,000	\$725,000
Company 2	High	\$550,000	High	\$595,000	High	\$615,000	High	\$665,000	High	\$685,000	High	\$705,000	High	

Net payment after offer reduced by commissions and expenses related to sale.  
 Statistics listed are for illustrative purposes only. Actual results may vary.

# Male Age 64 Life Settlement Maximum to Seller Calculator

Policy Face Amount	\$1,500,000
Cash Surrender Value	\$548
Gross Offer	\$815,000

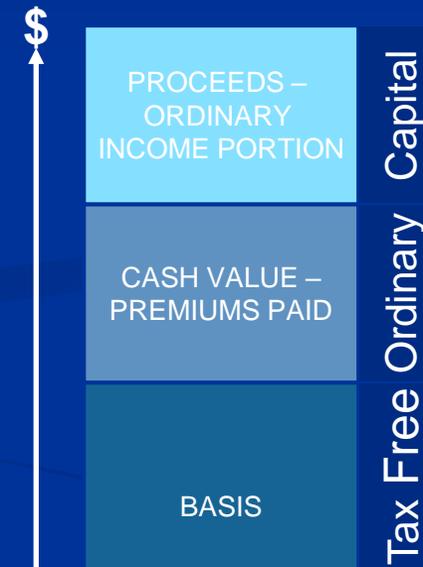
<u>Seller Gets the Great of Gross Offer Less Sales Fee of:</u>	<u>Net to Seller</u>	<u>Total Sales Fee</u>	<u>W&amp;C Share</u>
1.) 6% of Face Amount	\$725,000	\$90,000	\$54,000
2.) 30% of Gross Offer	\$570,500	\$244,500	\$146,700
3.) 1/3 of Offer Amount > CSV	\$543,516	\$271,484	\$162,890



## LIFE SETTLEMENT TAXATION

### 2017 TAX CUTS AND JOBS ACT

1. The portion exceeding the ordinary income portion will be taxed as a capital gain.
2. The portion exceeding cumulative premiums paid up to the cash surrender value will be taxed as ordinary income.
3. The portion of the proceeds received up to the policy owner's adjusted basis in the contract will be received tax free. (Basis = Premiums paid)



**Male Age 64**  
**\$1,500,000 Universal Life Policy**  
**Income Tax on Policy Sold**  
**Through Life Settlement**

Life Settlement Payment	\$725,000
Basis	<u>(\$207,403)</u>
Taxable Amount	<u>\$517,597</u>
<b>Capital Gain Tax (25%)</b>	<b>\$129,399</b>
<b>Net After-Tax Cash Proceeds</b>	<b>\$595,601</b>

# Male Age 64

## Keep Vs. Sell Analysis

### Assumptions:

Insurance Amount	\$1,500,000
Cash Value	\$548
Life Settlement Payment	\$725,000
Estimated Income Tax (25%)	<u>(\$129,399)</u>
Net Life Settlement Payment	\$595,601
Annual Premium	<u>\$60,000</u>
Total First Year Investment	<u>\$655,601</u>

# Male Age 64

## Keep Vs. Sell Analysis

<u>Yr</u>	<u>End of Yr Age</u>	<u>Life Settlement Pmt/ Annl Prem</u>	<u>Total Investment</u>	<u>Tax-Free Insur Amt</u>	<u>Required Annl Compounded After-Tax Return to Match Policy</u>
1	65	<b>\$655,601</b>	\$655,601	\$1.5M	128.80%
2	66	\$60,000	\$715,601	\$1.5M	46.75%
6	70	\$60,000	\$955,601	\$1.5M	9.13%
8	72	\$60,000	\$1,075,601	\$1.5M	5.19%
11	75	\$60,000	\$1,255,601	\$1.5M	2.12%

Statistics listed are for illustrative purposes only. Actual results may vary.

## Male Age 58 Cancer Survivor

- \$2,000,000 10 Year Term Policy at the end of the 10<sup>th</sup> Year
- Sold \$1,500,000 for \$260,000 (net to seller)
- Kept and converted \$500,000 with an annual premium of \$5,240

Net payment after offer reduced by commissions and expenses related to sale.  
Statistics listed are for illustrative purposes only. Actual results may vary.

## Male Age 89

Death Benefit                      \$1,500,000

Cash Value                              \$28,020

Annual Premium to Keep In-Force:

4 Years                                      \$88,764

7 Years                                      \$101,647

**Seller Paid:                              \$910,000**

# Life Settlement of Policies After Sale of a Business

## Male Age 63

Death Benefit	\$9,000,000
Cash Value	\$0
<b>Seller Paid:</b>	<b>\$112,000</b>

Net payment after offer reduced by commissions and expenses related to sale.  
Statistics listed are for illustrative purposes only. Actual results may vary.

# Life Settlement of Policies After Sale of a Business

## Female Age 82

Death Benefit	\$8,000,000
Cash Value	\$22,214
Annual Premium to Keep In-Force:	
5 Years	\$294,160
10 Years	\$461,773
15 Years	\$536,131
<b>Seller Paid:</b>	<b>\$3,150,000</b>

Net payment after offer reduced by commissions and expenses related to sale.  
Statistics listed are for illustrative purposes only. Actual results may vary.

# What Policies Are Life Settlement Buyers Looking For?

## Policy Type



# **What Policies Are Life Settlement Buyers Looking For?**

## **Policy Size: \$500,000 to \$5,000,000**

Fewer Buyers < \$500,000 or > \$5,000,000.

## **Insured's Age 70 and Older**

- Sweet spot: ages 75-85
- Older, if the policy is second-to-die
- Life expectancy 15 years or less

## PREQUALIFICATION QUESTIONNAIRE

Please answer the following questions to enable us to be as accurate as possible when evaluating your health for Life Settlement options.

Name: \_\_\_\_\_ Date: \_\_\_\_\_

Date of Birth: \_\_\_\_\_ Height: \_\_\_\_\_ Weight: \_\_\_\_\_ State of Residence: \_\_\_\_\_ Yes | No

Do you have a personal history of any of the following conditions?

Cancer or Tumors?  Yes  No

If yes, what type and/or location? \_\_\_\_\_

What was the stage or grade? \_\_\_\_\_

Diagnosed (month/year) \_\_\_\_\_ Treatment completed (month/year) \_\_\_\_\_

Asthma, emphysema, obstructive sleep apnea or COPD?  Yes  No

Depression, Anxiety, or other mental/nervous condition?  Yes  No

Cardiovascular disorder, including heart attack, coronary artery disease, arrhythmia, valvular disease, heart murmur, cerebrovascular disease, stroke, or TIA?  Yes  No

Diabetes, elevated blood sugar, or glucose intolerance?  Yes  No

Any disorder of the bones, muscles, or joints?  Yes  No

Any falls or fractures in the past 5 years? \_\_\_\_\_

Do you have a history or cognitive impairment, Alzheimer's, or other form of dementia?  Yes  No

Any other health impairment or medically treated condition? \_\_\_\_\_  Yes  No

Have you had any medical tests, such as a treadmill stress test, X-Ray, MRI, heart scan, sleep study, or echocardiogram?  Yes  No

Have you ever used nicotine in any form?  Yes  No

If yes: Type: \_\_\_\_\_ Frequency: \_\_\_\_\_ Last used: \_\_\_\_\_

Are you currently taking any medications? If yes, please provide name and dosage: \_\_\_\_\_  Yes  No

\_\_\_\_\_

\_\_\_\_\_

Have you had a COVID-19 vaccination shot?  Yes  No

If yes, which one?  Pfizer,  Moderna, or  Johnson & Johnson

If YES was selected for any of the above questions, please provide details below: \_\_\_\_\_  Yes  No

# Recommended Life Settlement Process



- Fiduciary representation for your client
- Full transparency of all offers, life expectancy results, compensation and fees
- Marketplace exposure to 18 of the top providers, including all direct providers
- Competitive Auction Process designed to obtain highest market value.
- Keep v. Sell Analysis

# Top Situations to Watch For



- Premiums become unaffordable
- Client planning to surrender or lapse their policy
- Business owners who no longer need their policy
- Trust policies no longer needed for estate planning
- Client has a term policy they don't plan to convert

**QUESTIONS?**

