Chapter 1

DON'T NEED, DON'T WANT?

Your Life Insurance Policy Could Pay Off Now

Fun is like life insurance; the older you get, the more it costs.
—Kin Hubbard

Don't you hate it when you've spent a ton of money on something you don't need? That can feel even worse if you're still paying for it.

Does this remind you of your life insurance policy?

I know. You're tempted to just walk away since it no longer serves you. But what if you could sell it?

Shockingly, up to 90 percent of life insurance policies[1] never pay a death benefit. Instead, they expire, lapse, or are surrendered. In short, most people who have purchased life insurance get little to nothing for the money they've spent. How much sense does that make? None. You wouldn't want to walk away from a Lamborghini just because you didn't drive it anymore. No, you'd sell it. Hello!

So, if you need (or want) money—and who doesn't—you may be able to do precisely the same thing with a life insurance policy that has outlived its purpose.

People like us pay our life insurance premiums each year to protect our loved ones or business partners. We are true proponents of life insurance. But let's be real, this is a policy you hope doesn't get used anytime soon. If you're lucky, you will outlive the need for your life insurance policy. But what happens when:

- This policy that you have been paying for is no longer needed or you just can't afford the often-rising premiums?
- Your children are no longer dependents, and you've built up enough wealth to make sure your family is taken care of for the rest of their lives?
- You and your business partner have sold your company, and the insurance policies you had in place to protect each other and your families are no longer wanted?
- Then there are all the families who purchased policies to cover the expected estate taxes upon the second spouse's passing, and now federal exemptions have increased so much that only 0.1 percent of Americans will have to pay a federal estate tax.[2]

"I was paying premium on a policy originally intended for estate taxes, but I no longer have the tax liability."

These are just some of a slew of potential situations where life insurance played a pivotal role in significantly leveraging money to provide security and peace of mind, but now the need for such coverage has diminished or evaporated altogether.

Most people believe they have only three options for their now unwanted and unneeded life insurance policies. They include:

1. Keep the policy and continue paying the increased premiums.
2. Decrease the death benefit of the policy to maintain an affordable premium.
3. Let the policy lapse and receive any potential cash value that has accumulated if it's a permanent policy.

What if there was a fourth option that might benefit you or your client much more? Would you like to learn how you could potentially profit from the sale of your life insurance policy? We're going to introduce you to a strategy that insurance companies do not want you to know about.

We feel you should be in the know about a relatively unknown yet powerful option: life settlements. Your home, automobile, boat, investment portfolio, investment real estate, and business interests are all considered capital assets. However, most people aren't aware that your life insurance policies are also considered a capital asset—an asset that may have significant value.

How can this be? I hear you asking yourself.

The answer starts with getting acquainted with what a life settlement is and what it's not.

So, what is a life settlement?

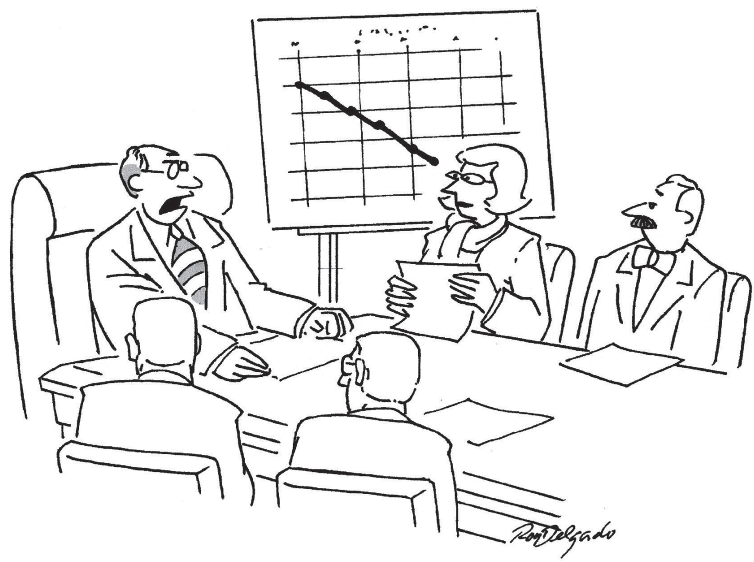
A life settlement is the sale of an existing life insurance policy, often to a third-party institutional investor. These investors on what we call the secondary market often include pension funds, hedge funds, or banks. The policy is put up for sale for more than its cash surrender value and less than its death benefit.

In such a transaction, the policy owner sells the policy in exchange for a lump sum cash payment. The policy owner is often the insured but can also include entities such as businesses or an irrevocable life insurance trust.

Once the policy is sold to the institutional investor, they become the policy's owner. It is now their responsibility to make all the premium payments moving forward. In return, they will eventually receive the death benefit upon the insured's death. These institutional investors purchase many different life insurance policies to diversify their holdings. It is helpful to know that the purchased policies are owned in large blind pools with many other policies. This helps to assure client confidentiality.

In addition, the investors participate in the performance of the grouping of numerous policies. You can think of it as similar to a mutual fund portfolio where the investors are less concerned about each individual equity holdings they own and more focused on the overall performance of their pool of assets. Even though the institutional investors who purchase unwanted policies do not have access to an insured's personal information, reputable companies service these portfolios and keep confidential records of the names and contact information needed to track an insured's health.

Although it's possible to sell a policy to an individual investor, this is not a standard or recommended practice. An individual investor would need to have a one-on-one relationship with the insured and policy owner, and confidentiality would not be possible. For obvious reasons, we feel strongly that an insured should never sell their life insurance policy to any individual who stands to profit from the insured's death. No one wants to see a Tony Soprano get involved with such a beneficial solution for unwanted life insurance policies.



" We need to ask ourselves . . ' what would Tony Soprano do ? ' . . "

What a life settlement is not

Speaking of Tony, you may be relieved to know that a life settlement is not a viatical settlement. Viatical settlements arose as the AIDS epidemic took hold in the 1980s. In a typical viatical settlement, the insured is terminally ill and has a life expectancy of 24 months or less. An example is a father who owns a $250,000 life insurance policy on his life. If he maintains the policy, his family will receive $250,000 in tax-free proceeds from the insurance company upon the father's inevitable and rapidly approaching death. What if the family does not have the economic means to fulfill the family dream of visiting Europe together and seeing the Eiffel Tower before his passing? Investors may offer the family $150,000, allowing the family to travel together. In this case, the investor would collect the entire death benefit upon his passing.

Although there are positive outcomes in viatical settlements, there is often too much room for others to take advantage of vulnerable policyholders. Unlike viaticals, life settlements involve policyholders who may not be terminally ill but generally have a life expectancy of between two and 15 years instead of just 24 months. Life settlements also tend to involve policies with higher net death benefits than viatical settlements.

What's in it for you or your client?

The bottom line is that unneeded and sometimes financially burdensome life insurance policies can often be sold for a heck of a lot more than you would get by simply letting them go. Of course, like most major financial transactions, this should only be considered after a thorough analysis of the pros and cons of retaining the policy versus selling or surrendering it. But suppose a life insurance policy is no longer necessary. In that case, a life settlement could result in the policy owner receiving a more significant amount than if the policy was allowed to lapse or was surrendered for its cash surrender value.

The most effective way to get you in the know on life settlements is to share actual case studies. Before we share these sometimes surprising stories, it's important to know the following:

- All client names have been changed to protect confidentiality.
- The gross offer we procure for our clients is always reduced by commissions and expenses related to the sale.
- Every client's experience is unique, and there is no guarantee that a life settlement will generate an offer greater than the current cash surrender value. In such cases, the client can always surrender their policy to the carrier if the coverage is no longer needed.
- This material is intended for informational purposes only and should not be construed as legal or tax advice or investment recommendations. Please consult a qualified attorney, tax advisor, investment professional, or insurance agent about the issues discussed herein.
- Although all the life settlement financial details in these stories use exact numbers, the names of the individuals and details about their lives have been changed to protect their privacy.

Okay, so now that we're done with all that, let's meet some people who, with a little (or a lot of) help from our Valmark Financial Group team, have made life settlements work for them.

Tackling the increased cost of insurance

After teaching second grade in Ohio for years, Nancy DeRose and her husband Charles, who spent his career at Proctor &

Gamble but is now deceased, retired to San Rafael, California. Over the next 15 years, Nancy focused on learning about the birds in this new place she now calls home. Birdwatching is a popular hobby for many people; however, Nancy, who refers to herself as a twitcher or birder, takes it to an entirely new level of passion. She's so serious about birds, we believe she could go head-to-head with most ornithologists.

Not far from her home is one of her favorite places on the planet—Mount Tamalpais State Park, which, as a long-time Marin County local, she refers to as Mt. Tam. Although one can drive nearly to the top, 79-year-old Nancy still prefers to hike in a few miles on this 13-mile loop. Nothing excites her more than getting a photo of a Hutton's vireo, a wrentit, or a pygmy nuthatch. She'll then go home and use the shot to paint a watercolor extravaganza.

Nancy's other passion is her only child—her son, Ron, a successful orthopedist—and her two grandchildren, ages 20 and 17. Next year, she wants to take them all, along with Ron's wife, on the Royal Clipper. This five-masted tall ship is listed in Guinness World Records as the largest full-rigged sailing ship in the world. Her 42 sails require a crew of 20 to get the 439-foot clipper ship doing 17 knots on sail power alone.

On this trip, Nancy can combine the two most important elements of her life, her loved ones and her beloved birds. She plans to visit the bird sanctuaries of the West Indies while her family soaks up the Caribbean sun. But that's going to take money.

Nancy would have had enough to pull off the trip, but she found out that her insurance company was increasing the premiums on the $4 million universal life insurance policy that she and Charles had purchased in 1995 for estate planning purposes. It turns out that, for Nancy to maintain the policy through her life expectancy, her planned premium would increase from $44,000 to $106,000.

That's not just a premium hike, that's more like an ultramarathon without any of the associated pleasure.

While Nancy might have just been able to afford the increased premiums if she scaled back, she certainly would never be able to afford to take her family on this dream vacation. Then she realized that she no longer needed the policy for estate planning purposes. The new tax laws had raised the federal exemption level to more than $12 million. Even if that dropped back down to $5 million in 2026, as it is expected to do, she would be fine. So why pay for an expensive policy she no longer needed?

Instead of simply walking away or surrendering her policy for its cash value, Nancy consulted her accountant, who turned to us for help. We provided the pair with four options: surrender the policy, reduce the death benefit, pay the increased premiums, or the fourth option—sell the policy. Instead of surrendering the policy, Nancy, whose life expectancy at that point was roughly six to ten years, took our recommendation and decided to pursue selling the policy through a life settlement.

Our life settlement team worked with multiple providers through a professional bidding process and negotiated a settlement offer, resulting in a total gross offer of $1,521,000, or two and a half times the cash surrender value. That's a heck of a lot more than the policy's $640,602 cash surrender value. And boy, that extra $880,398 she grossed will sure finance one heck of a family/birding holiday.

An all-too-often-unknown option

In most states, insurance carriers are not required to tell the owners of life insurance policies that they have the option to sell their policy instead of lapsing or surrendering it. Therefore, it's the financial advisor's responsibility to educate clients regarding the life settlement option. Unfortunately, most insurance agents, financial planners, CPAs, and estate planning attorneys we've come across have been unaware of such solutions for unwanted life insurance policies.

According to a 2015 survey by Wealth Management, 40 percent of financial advisors,[3] by their own admission, know little to nothing about life settlements, which helps explain why only 11 percent have ever recommended a life settlement to their clients.[4]

Not surprisingly, studies show that more than 50 percent of seniors had no idea they could sell their policies.[5] Of those, nearly 90 percent who lapsed or surrendered their policies back to insurance carriers would have considered selling the policy had they known that life settlements existed.[6] Luckily, Nancy was introduced to us before she surrendered her policy.

How do life settlements work?

Okay, let's review some basics and introduce a few others.

The buyers of life settlements—often referred to as life settlement companies or providers—can hold the policies to maturity and collect the net death benefits. Others will bundle many purchased policies together and resell the assortment of policies to hedge funds or other investors.

The people who sell their policies do so in exchange for a lump-sum payment. The amount they will receive in the secondary market depends on a number of factors, including their age, their health, and their policy's terms and conditions.

In addition to paying you a lump sum for your policy, the buyer agrees to pay any additional premiums that might be required to support the cost of the policy for as long as you live. In exchange, the buyer will receive the death benefit when you die. And if they let the policy lapse, that's on them, not on you, since you will have already received payment in exchange for your policy.

After selling your life insurance policy, all you have to worry about is enjoying that money and keeping the policy's buyer waiting as long as possible to collect the death benefit proceeds.

Are you a potential life settlement candidate?

Often when policyholders first learn about settlements and see how lucrative they can be, their eyes light up, and thoughts of newfound funds for a Class A motorhome or vacation home come to mind. So, let's look at who potentially qualifies for such a strategy.

Here are the prerequisites:

- The insured's age is typically 65 and older, unless facing a life-shorting condition.
- Their life expectancy is 15 years or less.
- There has been a decline in health from the original policy issue.
- The life insurance policy has a net death benefit of $250,000 or more (there's no maximum).
- The policy owner can be an individual, trust, or corporation.
- Life insurance policies can be universal life, guaranteed universal life, survivorship universal life, variable universal life, and convertible term. Flexible premium policies like universal life are more favored by buyers because they can readily adjust the premiums going forward.

- The annual premium should be 5 percent of the death benefit (or less), and the cash surrender value should be 15 percent of the death benefit (or less).

A settlement is only possible when the policy's market value exceeds the cash surrender value. Key factors in determining the market value of a policy are the death benefit, the cost of future premiums, and the insured's life expectancy.

As you might imagine, even though it's tough to think about, life expectancy is the key component in determining the market value of a life settlement transaction. The lower the premiums and the shorter the life expectancy, the higher the selling price. Conversely, the greater the amount of premiums that need to be paid and the longer the investor must wait for the death benefit, the lower the policy value.

Let's flip that notion around and look on the positive side. If you don't need the life insurance policy, it can really feather your nest during this chapter of your life.

Missed life settlement opportunities

If you're the owner of a life insurance policy that's no longer required or wanted but aren't sure what to do about that, you're not alone. Unfortunately, as we previously shared, more than half of all seniors have no idea they might be able to sell their life insurance policies. That potentially explains why each year, more than $112 billion in life insurance (face value) is allowed to lapse or is surrendered by individuals over age 65. That's $112 billion with a B![7] That only partially explains why so many people are walking away from the profit they could potentially collect from a life settlement.

Enter life insurance companies, who make far less money when they have to pay out a death benefit than when a policy is allowed to lapse or when it's surrendered. But, of course, that's in all likelihood not going to happen if that policy is sold to an investor. As a result, insurance companies don't exactly make it easy to obtain a life settlement.[8] Not only do they refrain from explaining the life settlement option to policy owners (even threatening to fire those sales agents who do mention it), they lobby for state laws that could restrict or even shut down the life settlement market.

But that's far from the only impediment. The more significant issue gets back to plain old lack of knowledge. As we've seen, not only do policy owners not realize that they can potentially sell those unwanted life insurance policies, but their financial advisors don't realize this either.

Luckily, that wasn't the case for Donald Jenkins.

Higher and higher

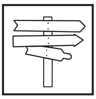
Like Nancy DeRose, Donald Jenkins's premiums on his $1.3 million universal life policy, which was owned by a limited partnership, had soared, a story that's all too common these days.

Donald had spent his career working for Delta Airlines in Atlanta before retiring on a very handsome pension. But the latest premium hike to $95,000—over seven times the original planned premium—just weren't part of his retirement plans, especially since he felt he no longer needed the insurance. When he ran the dilemma by his close friends, they agreed that the policy was no longer necessary. "If you continue to pay for it, you're not going to be able to do all the things you want in life," one of them said. "Walk away."

Being a prudent guy who always likes to consider his options, he decided to consult his CPA before letting his policy lapse. "Before you do anything," the professional said, "you really need to sit down and speak with a financial professional who specializes in life settlements. I'm not sure whether you'll get anything, but if you let it lapse, we know you're not going to get a dime."

When Donald and his CPA met with us, we knew right away that Donald was a candidate for a life settlement. In the four to seven years he probably had left, he certainly didn't need to be paying all that money for a policy he didn't need. But he also didn't need to leave money on the table. A bidding process finally resulted in a total gross offer of $315,000, close to twice the cash surrender value.

The recent premium hikes have proven too steep for a lot of people.



The premium increased unexpectedly and I was no longer able to afford it. I was going to have to let the policy lapse.

Fortunately, if they no longer need their life insurance policy, they can trade in that expense and often wind up with enough cash to tick off an item or two on their bucket list.

Getting your money's worth

Even though we've been studying this whole situation for a while, as well as working up and reviewing financial plans for all our clients, we can't help being amazed at how many people continue to pay for costly insurance policies they don't need. And it's downright disconcerting when you consider the potential upside of selling those policies. In 2021, Americans who sold the life insurance policies they no longer needed instead of surrendering them averaged a solid 7.8 times more than the cash surrender value. That meant that American seniors pocked $660 million more than they would have had they just accepted what the life insurance carriers were offering.[9]

Alan Baxter is one of those who, rather than surrender the policy and wind up with less than he might have—or nothing at all—was able to profit significantly.

Alan, who has always had a passion for skiing—racing at Mount Hood in high school, working as a volunteer race coach after graduating college, and attending the winter Olympics whenever possible to see the downhill events—purchased a $2 million term policy 14 years ago to cover survivor needs for his children who were minors at that time. In the intervening years, his two sons, now in their mid-30s, had become successful professionals—one a fashion designer at Columbia Sportswear and the other a nurse at Providence Healthcare—and the end of the policy's 15-year term period was nearing.

Although Alan's first marriage ended in divorce, he is happily remarried to Kate, who has stuck by him despite challenges that could have destroyed flimsier relationships. In 2008, Alan's love for speed caught up with him—not on skis but behind the wheel of his beloved 1997 Porsche 930.

He had trailered his race car up to Portland International Raceway (PIR), just as he did several times each summer. As usual, he and his friend Roger had entered their cars into a race sanctioned by the Sports Car Club of America (SCCA), a nonprofit automobile club formed in 1944 that runs programs for amateur racing enthusiasts. This would be their first race since the track's recent and extensive renovation, which included repaving as well as widening turns four through seven and sharpening others to slow down racers before they entered the back straight.

Excited to try out the upgraded track, Alan pushed his mean machine hard. Although the course is almost perfectly flat, the track configuration includes a hard chicane at the end of the front straightaway. Coming into it with too much speed and not enough downshifting or braking action, he hit the new guardrail at over 150 mph. When he awoke at OHSU Spinal Center, he had no memory of the accident. Moments later, the doctor shared the news that Alan was now paralyzed from the waist down.

Although only 66, Alan, who is expected to live for just another four to seven more years, had to reevaluate many things, including his financial situation. When he expressed reservations about continuing to pay for or renewing his term policy since his kids, who were the only beneficiaries, were doing fine on their own, the accountant suggested that life settlement specialists review his policy. During the meeting, Alan was surprised to learn that rather than lapsing his term policy, which had no cash value, or paying more than $45,000 in annual premiums to convert the policy to a permanent policy, he could instead sell the term policy on the secondary market and recoup the $63,000 in cumulative premiums he had paid on the policy as well as additional funds to further enjoy his remaining years.

In the end, a bidding process and negotiated settlement offer brought in a total gross offer of $980,000, $917,000 more than he had paid in term premiums. Talk about creating value on an asset that so many people would assume was worthless!

An attractive environment to sell a policy

Now more than ever, the stars are aligned when it comes to selling a life insurance policy that is no longer needed or wanted. Let's look at the different factors causing this trend.

First and foremost, the low-interest-rate environment we have experienced over the past decade has led to a lot of money flowing into this market from institutional investors to buy policies as they seek higher returns than they can get from traditional fixed-income investments. Let's face it, not even institutions are happy with earning less than .5 percent in a savings account. One life settlement provider announced just a few years ago that it had secured $250 million from investors for policy purchases.[10]

Second, there is currently a great demand for policies and, therefore, more competition among buyers, resulting in what could be called a seller's market.

Third, buyers can borrow money at low interest rates to purchase policies and make future premium payments.

Fourth, life insurance policy values are an excellent non-correlating asset. This means they don't fluctuate with the ups and downs of the stock and real estate markets. The principal risk for investors is not stock market volatility or the safety of their investment. It's that the insured will live too long beyond life expectancy and make the policy purchase not economical.

Of course, an attractive selling environment doesn't necessarily mean that this is a good idea for you or your client. So how do you know whether you should consider a life settlement? That's next.