Life Insurance Settlements: Defined and Explained

Types of Life Settlements

Traditional Life Settlement
This is the most common form of life settlement. In a traditional life settlement, the licensed life settlement provider (the buyer) will pay the policy owner a cash settlement amount above the surrender value but below the death benefit. The buyer will assume all rights of the policy and receive the death benefit upon the death of the insured(s).

Retained Death Benefit
In a retained death benefit scenario, the buyer will take over paying premiums on the policy. The policy beneficiaries are assigned a retained death benefit amount directly from the insurance carrier which will be paid upon the death of the insured(s). This amount is usually more than what the seller receives in a traditional life settlement. The original owner is no longer required to pay premiums and will receive no cash now. This option is beneficial for those who find premiums to be too expensive but still want their beneficiaries to receive a portion of the death benefit.

Hybrid Life Settlement
With this option, the seller of the policy can receive a combination of traditional life settlement and a retained death benefit. This can provide cash now and retain some death benefit for the family/trust/beneficiaries.

Top 3 Reasons to Sell Your Life Insurance Policy

#1: Your lifestyle/needs have changed and the policy is no longer needed.
Change is inevitable. As you move through the stages of life, you may find that you no longer have a need for your life insurance policy. Examples of lifestyle changes that could alter your need for life insurance include: divorce, retirement, reduced estate tax burden, lack of need by the beneficiaries, poor policy performance, excess insurance, or the closure of a business with key man insurance.

#2: The premiums are no longer affordable.
Depending on the terms of the policy you own, changes in the insurance market could drive up the price of the future premiums you pay. These changes force people to surrender their policy or let them lapse.

#3: Funds are needed to pay for medical care or other expenses.
A cash settlement could be used to pay for assisted living, pay premiums on another existing life insurance policy, pay off tax liability, or purchase an income-generating annuity.

The Life Settlement Process - 5 Key Phases

1. **Deciding to Sell**. Determining if a life settlement is the right choice for you is an entirely personal matter and should be carefully discussed with family and financial advisors.
2. **Determining Eligibility.** There are specifics that determine if an individual will qualify for a life settlement, such as: ongoing premiums, life expectancy of the insured(s), and the death benefit of the policy. Your life expectancy is calculated by a medical underwriter based on your medical history and/or obtained by your medical records.
3. **Offer and Acceptance.** If eligible, the buyer will extend an offer to the policy owner.
4. **Contracting and Verification.** State-approved life settlement documents are utilized to record the life settlement transaction and agreement between the policy owner and buyer. The policy owner, insured(s) and buyer must sign and notarize the life settlement contract. The verification process includes ensuring all documents are accurately complete, the policy is in good standing with the insurance company and the funds for the purchase have been put in an escrow account for the policy owner/seller.
5. **Ownership Change and Release of Funds.** The buyer will send a request to the life insurance company to change the ownership/beneficiary and subsequently assume full rights of the life insurance policy. Once the changes are confirmed, the escrow agent is instructed to release the funds to the seller.

Case Study

- Husband and Wife ages 84/85 with several life insurance policies totaling $19 million.
- Existing policy with $6 million death benefit and $0 cash surrender value required significant premium to keep the policy in force through life expectancy.

Result

- Policy was sold in a life settlement for $1 million, gross of tax.
- Result: Policy worth $0 if surrendered but client obtained $1 million for it in the settlement plus relief from all future premiums.

Summary

In 1911, the U.S. government ruled that life insurance policies are personal property. This outcome allowed your life insurance policy to be bought, sold, and traded, just like any other high-value asset. It has the power to be liquidated and turned into cash. There are many different scenarios where a life settlement can help someone turn their insurance policy into a living benefit. Contact us today to explore your life insurance policy options!

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