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Life Insurance Valuation: A New Tool For Advisors

Life settlements present a planning option

BY MICHAEL L. COBEN

YOUR CLIENT IS RETIRING AND considering a change in life insurance. His policy carries a sizeable cash value. Time to surrender, right? Not so fast. Somebody else may be willing to pay more for the policy—much more.

One of the pillars of sound financial planning is the regular appraisal of a client's real estate, businesses, equities and other holdings. Historically, life in-

The rise of the secondary market for life insurance has given policy owners access to what consumers in virtually every other sector have long enjoyed—fair market value.

TO MARKET, TO MARKET

As a result, financial advisors are rethinking their approach to managing a client's life insurance assets. Instead of surrendering or lapsing a policy that is underperforming or no longer needed, advisors are taking clients' policies to market to determine what they are worth.

The result is often a win for all parties involved. Take the example of a client who purchased a \$3 million term policy several years earlier to cover a business loan for his company. Due to a change in his health, the business was sold and the loan repaid. But what to do with the term coverage? Normally, the policy would be allowed to lapse. Instead, the client's advisor suggested a valuation which yielded an offer of \$930,000 on the secondary market.

Over the past few years, life settlements—as these transactions are known—have moved into the mainstream of financial planning. They offer qualifying policy owners the opportunity to sell policies that are no longer meeting expecta-

tions or simply no longer needed and receive significantly more than cash value in return. According to Conning and Company, 20% of all insureds over the age of 65 own policies with a market value exceeding surrender value.

But policy valuation does more than identify the best price for unneeded or underperforming life insurance. It gives consumers new power to make financial planning decisions. Consider the case of a 74-year-old female with a \$10 million term policy. The annual premiums in excess of \$300,000 no longer fit her financial plan so she planned to let the policy lapse. The advisor suggested an appraisal, which yielded two options: a \$660,000 life settlement or a \$3.5 million Settlement With a Paid-up Policy (SWAPP). Instead of surrendering the policy for no value, the client chose the paid-up policy, eliminating her premium payments while addressing her estate planning needs.

Such case examples reflect the power of policy valuation. By informing clients of the real value contained in the policies, it gives them significantly more control over their assets and their financial planning, as well as significant new tools for meeting their financial goals. And these opportunities are not limited to



POLICY VALUATION gives older consumers new power to make financial planning decisions.

urance policies have been excluded from such evaluations because there was no market for them. But times have changed.

policies with face values in the millions. Clients with \$100,000 policies now are benefiting from access to the secondary market as well.

WHEN IS VALUATION IN ORDER?

The very real material benefits of secondary market transactions suggest that policy valuation should be a standard component of any ongoing wealth management strategy. In particular, a valuation should be conducted whenever there is a change in the need for insurance, such as the sale of a business, retirement, or a decrease in estate value. In addition, a valuation is in order any time clients age 65 or older experience a change in health. And certainly it should be recommended when a client is considering surrendering a policy or letting it lapse.

Obtaining a valuation is a straightforward process. A valuation questionnaire is completed and submitted with a signed authorization. Medical exams typically are not required. The advisor then receives an offer detailing what the policy is worth. Some companies even provide advisors

with an online "quick-qualifier" to see if a policy is a likely candidate for a settlement.

Considering that obtaining a valuation requires only a few minutes of an advisor's time, and that it can yield a tremendous financial opportunity, it's easy to see why advisors in all sectors of financial planning have incorporated valuations into their practice. There are, of course, important due diligence issues to address. Throughout the process, the advisor's first responsibility is to protect the client's interests during the transaction.

This begins with selecting a company with the strongest background in secondary market transactions and the valuation of life insurance policies. In particular, it is important to verify that the company issuing the valuation is well versed in all the complexities, nuances and technicalities of the life insurance industry, especially when valuing a policy with high face value. Also important is the firm's source of capital. Advisors should be sure to confirm up front that the transaction is backed by institu-

tional capital (as opposed to individual investors). Finally, given the speed with which the market is developing and new opportunities are arising, does the firm have a proven background in secondary market transactions?

By addressing these issues ahead of time, advisors not only obtain the most accurate valuation but also assure that the funds will be available at the conclusion of the transaction, that the client's privacy is protected, and that the end solution best meets the client's objectives.

A NEW WORLD

Advisors now have the ability and opportunity—not to mention the responsibility—to evaluate regularly the worth of their clients' insurance. By doing so, they not only determine the value contained in a given policy, but they can increase significantly their own value to their clients. And that is an opportunity that should never be passed up. ■

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