

Consumers Drive Innovation in the Secondary Market for Life Insurance

by David Cherkas

Healthy markets are built on consumer choice. For proof, look no further than the burgeoning secondary market for life insurance. The market was founded on the principal that policyowners have a right to know about the fair market value of their life insurance assets and have the right to access that value. The market has delivered close to \$2 billion over surrender value for unwanted or underperforming policies. Clearly, consumers have embraced the new financial planning options that the market provides. Just as importantly, they continue to push for even greater flexibility.

Often mischaracterized as “the life settlement market,” the secondary market has sparked a burst of innovation, which has far surpassed the original life settlement transaction. The result is an increasingly broad range of financial solutions available to savvy advisors. Instead of simply selling an unneeded or underperforming policy for cash, advisors are leveraging the market value of a client’s policy to get much more flexible and cost-effective coverage, such as a paid-up benefit based on market value rather than cash surrender value.

Until recently, such options were largely limited to universal life or whole life policies. Now, even that is changing. The arrival of term settlements is good news for policyowners who find that their term policies are no longer meeting their needs. For years, the “pay as you go” mindset surrounding term insurance obscured the real value that accumulates in term policies. Without a cash-surrender option, policyowners who allowed their term policies to lapse have had no choice but to forfeit significant value.

The secondary market now provides several vehicles for consumers to convert the value in their term policies into something more effective. Of course, the simplest solution is a life settlement that provides a cash payment to the policyowner. A six-figure cash payment may seem like an extraordinary windfall compared to walking away from a term policy without a

penny when the premiums become too expensive. But, the simplest option is not always the most appropriate, especially if cash is not what’s really needed.

Consider the client who holds a large, but too expensive term policy and still needs a significant amount of coverage. Advisors now have several options for transferring the policy’s market value into something that addresses the client’s needs. Consider the case of a 61-year old male with a \$500,000 term policy that was no longer performing up to expectations. His advisor sold the policy and used the proceeds from the life settlement to get much more efficient coverage.

Increasingly, advisors are using these vehicles to create truly personalized solutions tailored to their clients’ needs. This customization reflects the most exciting impact of the secondary market. Today’s increasingly sophisticated consumers have come to expect higher and higher levels of individualization. In the hands of skilled advisors, the flexibility of secondary market transactions provides an almost unlimited range of options for putting the value in life insurance to maximum use.

Perhaps the best example of this is the explosion in popularity of premium finance programs based on market value. Consumers can now get loans based on the secondary market value to get new policies or finance in force policies -- term or otherwise. In other words, the policy’s market value provides the required collateral. For estate planning professionals, this development provides an exciting new set of tools for maintaining coverage in an uncertain tax environment.

Indeed, the range of new solutions speaks to the power of an open marketplace that is free to respond to consumer demand. With the help of skilled and dedicated advisors, consumers now view life insurance as an asset that can address an ever-widening range of financial planning needs. In this way, the market is greatly expanding the way life insurance is being used. And that is a good thing.

For perspective, think back to the home

mortgage marketplace of the 1990s when borrowers had only a handful of loan products to choose from. Today, lenders offer dozens of variations that allow consumers to design their own loan programs, which touched off a spectacular real estate boom. It is no coincidence that it all began with the creation of a secondary market for home mortgages.

Life insurance is following a similar course. A one-time static asset has become a dynamic planning tool. Consumers have far more favorable alternatives than surrendering a policy or allowing it to lapse. They can settle, receive a paid-up benefit, or finance the premiums – all on the basis of the policy’s market value. Not surprisingly, clients are responding to the new range of options with open arms. And advisors are continuing to seek out additional strategies to deliver new value to their clients. In short, the market is doing what healthy markets do. Providing choice, expanding value, and creating opportunity. □

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Beyond Life Settlements

The secondary market for life insurance gave birth to the life settlement transaction. Now, the market has opened the door to several new options that allow consumers to leverage the market value of unneeded or underperforming policies, including the following:

- Term Settlements – Life settlements aren’t just for universal life or whole life.
- Paid-up Benefit – Receiving a paid-up benefit based on market value does double duty by providing more appropriate coverage and no on-going premiums.
- Premium Financing – Consumers can now get loans on in-force coverage based on the future value of the policy so they can finance premiums without liquidating other assets as collateral.