

It's About Your Business

A NEWSLETTER FOR LIFE AGENTS & FINANCIAL ADVISORS

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SECOND OF A TWO PART SERIES



What Doesn't Work in Premium Financing

ALLAN D. GERSTEN, CLU, CFP, ChFC

It only takes the mere mention of premium financing for life insurance to evoke an array of both positive and negative thoughts, feelings and expectations. At the same time, life insurance sales using premium financing concepts are exploding.

The market itself is both interesting and appealing since it includes individuals ranging in age from 35 to 85, although the available plans work much better when a client is healthy. In fact, there may be situations in which premium financing does not work at all if the client is not a standard risk.

It's worth noting that company executives and stockholder employees can participate in plans that can create value for the corporate entity.

Having said this, it's critical that both the broker and the client have an

understanding of leverage inherent in using other people's money and the risk-reward proposition inherent in the premium financing transaction.

Candidly, however, it is important to remember that the life insurance sales community has limited experience in this burgeoning marketplace of new ideas, strategies and solutions. It is well to remember that a thorough understanding of life insurance underwriting, carrier products, flexibility and design possibilities is the foundation for concepts that work for everyone involved, including clients, lenders and insurance companies.

As you might guess, lenders and funders have their own criteria for what represents an appropriate loan, and with the appropriate collateral required for their target market.

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Life Insurance Combined with an LTC Benefit

DAVID COLBURN, LUTCF, BROKERAGE MANAGER

As clients near retirement they need to know not only about investment and inflation risk, but the very real risk associated with death and the need for long-term care.

The risks are real: If a client has a defined benefit pension, the plan's benefits are usually reduced or eliminated when the pensioner dies. The client often needs to elect as much as a 30% reduction to guarantee an equal benefit for the surviving spouse. An \$8,000 monthly pension, for exam-

ple, may go down to \$5,600 a month, usually for life, even if the spouse dies first.

Social Security benefits are reduced when one spouse or the other dies. If the primary earner is receiving \$1,800 a month and the low wage earner spouse is receiving half (\$900/month), then the larger of the two is what's usually left for the survivor.

If a client has modest savings (\$300,000 in funds and bank accounts), investment loss, emergency spending,

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IT'S YOUR EXPECTATIONS THAT COUNT

President's Message

KENNETH A. SHAPIRO

Sometimes we find ourselves talking about how much First American does for producers. That may make us feel good, but I doubt that it does much for you. What's really important is this: *We want you as a producer to know exactly what you should expect from us.* We like to think of them as our "Best Practices."

Here is what you should expect from us before the sale and in managing your case.

First, before the sale. You can expect the members of our brokerage staff to be proactive. You can count on them to find the best markets for your case, not just an easy one or a "favorite." You can also expect them to bring you comprehensive solutions to real issues.

We also understand you want fast action. That said, you can expect us to turn around proposals in a matter of hours, not days. We can do this because we have the in-house staff available that understands your urgency.

You also expect unique, carefully crafted solutions from us that have client appeal and that set you apart from the competition. And that's what you'll get from us.

Second, case management. Our new business team has one mission: *to get the case approved as quickly as possible.* That's one way we measure their performance. We're serious about getting cases approved fast.

They also keep producers in the loop with at least weekly updates, if not more often, or as new information becomes available. That's not all. You can always view the status of your case online. Finally, you can speak directly to the head of the department if you have questions.

We are not perfect, but we have the processes and the experienced personnel who can and will exceed your expectations. If we don't, I want to know about it.



Seven Ways to Increase the Average Premium on Life Insurance Sales

GREGORY E. SCHWABE, FLMI, NATIONAL MARKETING DIRECTOR

When working on a life insurance case, producers are often so involved they can forget to look at the bigger picture. Even though the particular recommended solution is sound and satisfies the client's needs, quite often there are other possibilities that may be even more appropriate. Keeping them in mind can be difficult at best.

Here are seven ways to increase the average premium, while, at the same, serve clients even more successfully.

• Three Term Life strategies

Always show the next available level term period in addition to the period requested by your client. Providing options changes the applicant's mindset from "Should I buy this proposed plan or not?" to "Which of these plans should I consider?"

For 20- and 30-year level term sales, propose Return of Premium term as an alternative. A client may prefer "renting" a life insurance policy and then getting all of their money back later, rather than "buying" it at a lower cost and having nothing in return should they live for the level period.

When quoting amounts also show the next band break as an alternative. If you're showing face amounts of \$200,000, \$400,000, for example, include proposals of \$250,000, \$500,000 and \$1 million. This strategy often provides a much better pricing option for a client as well as additional coverage. It also makes it possible to engage the client in a conversation rather than a "sales pitch."

• Four Universal Life strategies

When quoting secondary guarantee no lapse UL products, also consider the benefits of presenting "Plus" type products that offer the same guarantees, but have significantly better accumulation values for only slightly higher premiums. We all know that the insurance industry is constantly improving products and there is no sense in taking the client out of the 1035 market in the future by selling them a "no frills" policy. The cash that would accumulate in a "plus" type policy could be rolled into a newer and better plan and offset future premiums caused by buying a new policy at an older age.

When proposing current assumption UL cases where the focus is on accumulation, consider a non-par Whole Life product that affords the client much better accumulation and takes the moving parts, such as interest and expenses, out of the equation. This may increase the premium by 20% to 25%, but when you compare the return on the additional policy value, your client will clearly see the advantage of paying the extra premium and may prefer this option. If you don't show this alternative, the client will never know.

When proposing no lapse coverage for applicants under the age of 50, consider showing two sales scenarios: one being a lifetime payment schedule and the other a limited pay to age 65 or 70. Today, many clients are concerned with their

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and systematic withdrawals could deplete those funds for a surviving spouse.

The solution to all these problems is permanent life insurance. The retiree, knowing that a large sum will appear at their death, can elect to have a no survivor pension. By using the saved 30% reduction to purchase a substantial life plan, they can be assured that the income from that benefit could replace lost pension and Social Security income and savings could be spent on travel and other enjoyable pastimes knowing once again that a large tax free sum would be available after their death.

A super healthy 60-year-old male can purchase \$450,000 of Universal life with a lifetime guaranteed premium for \$6,571 with John Hancock, a major carrier with top financials.

If he has a 55-year-old spouse, also in excellent health, she can acquire a similar benefit for an annual premium of \$4,239. If one of them has a large defined benefit plan and the other doesn't, then one or the other could purchase a lesser amount.

Despite life insurance, the need for long-term protection is needed to protect married couples from all of the same issues.

If either goes into nursing care, the bill will be paid first from the income of the spouse needing care (average cost in Mass. is \$9,000 a month and in New York an alarming \$12,000 a month).

In this example, the primary income spouse's pension (\$5,600 or \$8,000) plus Social Security benefits of \$1,800 would be used to pay for care. If the cost was \$9,000 and the pensioner had selected the no survivor pension then \$800 plus the at-home spouse's own income of \$900 from Social Security

would be left to pay for the individual's personal and living expenses.

If this occurred in New York and the monthly nursing home cost was \$12,000, then all pension and Social Security benefits (\$9,800 total) could go to pay for care. While the at-home spouse would probably be able to keep more income due to spousal minimum rules, the difference would be paid for out of the family's cash assets. The at-home spouse can keep approximately \$101,000 in cash assets and the in care person, \$2,000. Medicaid would pay the difference over income and put a lien on their home for the Medicaid paid portion above available income.

Prudential offers an excellent LTC plan for \$8,997 annually if both are well. The other major carriers such as Genworth, John Hancock and MetLife offer plans at a similar cost.

The need for both Life and Long-Term Care Insurance is obvious and undeniable. A premature death or lengthy nursing home stay can devastate the financial life of all but the most affluent of clients.

Unfortunately, most clients are either unwilling or unable to pay \$6,571 plus \$4,239 for life and \$8,997 for Long-Term Care coverage, totaling \$19,807, even if taking the \$8,000 pension instead of the \$5,600 gave them \$28,800 more in pre-tax spendable income.

The insurance industry seeing the need for an affordable simple

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What doesn't work in premium financing

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There are dozens of funders in the premium financing business with numerous programs that are available from time to time through particular lenders.

Lending underwriting criteria can include a minimum and a maximum age, a minimum net worth, the restriction to the use of approved insurance companies only, as well as restrictions to use only approved products, and, as to be expected, what is to be considered as valid collateral.

Without question, valid collateral is where the rubber meets the road for the lenders. For example, some conventional high net worth individuals may be asked to provide a letter of credit for the entire loan, while other lenders may allow the letter of credit to be as little as 25% of the loan.

Hybrid premium finance programs permit the intrinsic value of the policy to serve as collateral for 75% of the premium and interest deferred, and a personal guarantee from the policyholder to complete the remaining 25% collateral requirement.

Here are issues to consider when developing a successful premium finance sales strategy:

• **Appropriate product design.** Here are the guidelines for selecting the right product:

- Use of Current Assumption UL over a Guaranteed UL product.
- Introduction and evaluation of Indexed UL.
- Use of Return of Premium rider or riders, as appropriate.
- Strategies for carrier riders to develop high early cash value.
- Limited premium paying periods, i.e., seven or 10 payments.

• **Understanding and securing a premium funding lender and plan design considerations.**

1. Evaluate the client's net worth in conjunction with the lender's collateral requirements.
2. Compare lender's requirement for personal guarantee, letter of credit or intrinsic value derived from life expectancy reports.
3. Use longer notes, whenever possible, i.e., five years, 10 years or even lifetime.
4. It might be recommended that the client contribute some portion of the transaction, such as the interest expense.
5. Going into the transaction, it is important to know the exit strategy. These exit strategies might include: 1) repayment of the debt using a GRAT strategy; 2) sale of a business; 3) retirement of an employee; 4) death of the insured; or 5) a sale into the secondary market, if appropriate.

• **Sales and marketing tactics that don't work for the life insurance industry, the consumer or the lender.**

- Clients with marginal net worth and minimal understanding of the transaction.
- Selling clients more coverage than they can afford and not basing it on appropriate collateral requirements.
- Stealth or "Stranger Owned Life Insurance Plans" in which the true purpose of the transaction is not transparent and there is no "insurable interest." This is referred to as a non-recoverable transaction. Simply put, this is toxic for all concerned.
- Unhealthy risks such as senior adults without a short exit strategy.
- Variable Universal or Variable Whole Life will not work because of banking and collateral issues.
- Seniors who are entering hybrid premium financing transactions with expectations with regard to getting specific cash returns from a sale of their life insurance policy.

Life sales professionals have become aware of the opportunities presented by selling large life policies. This is the result of a confluence of three key factors: a lower interest rate environment, Wall Street's recognition and imagination when it comes to valuing a life policy, and a huge reservoir of clients with very large estates.

This type of client is discovering the inherent value in the insurance contract and how it is able to provide a return that is uncorrelated with other financial assets.

The premium financing revolution began with senior adults who recognized that it was to their benefit and that of their heirs to maximize their insurance buying capacity. Today, the revolution continues with younger clients who grasp sophisticated concepts for maximizing their estates, as presented by trusted advisors who know and understand premium financing.



Case Study: Asking the Right Questions

DENISE M. DESAUTELS,
VICE PRESIDENT OF BROKERAGE SALES

Situation

A broker came to First American after attempting to place a case with his primary company.

The client was a male age 68 (N/S) rated Table C by the insurance company. However, he was not willing to accept the rated policy. In fact, he was very clear with the broker—he would not even consider the rated policy.

The case was salvaged with a STND offer by simply asking the right questions.

Assessment

When the broker brought the case to First American, the first task was to develop a complete understanding of the issues. What has caused the rating? After having the client sign a HIPPA and an authorization, we obtained the medical records, which revealed two major areas of concern:

Slightly abnormal ECHO Cardiogram; and, some mention of Depression in his APS, starting about 2 1/2 years ago.

In drilling down into the case, we were able to provide additional information to give insight to the underwriter regarding the references to Depression.

As we delved into the Depression history, we discovered that it had occurred about the same time that his wife was diagnosed with early Alzheimer's Disease. The client had been the caregiver for his wife for approximately two years, which had been a very difficult period for him.

The wife's situation, however, had changed recently. She was placed in a 24/7 facility. This made it possible for the client to visit her daily. This relieved the stress since he no longer was the primary caregiver.

An updated letter from the client's physician was very positive. The doctor made note that he was feeling much better and that "the stress had been lifted."

Results

The new information from his doctor provided First American with the current information necessary that helped negotiate a STND N/S offer from three insurance companies.

The case was salvaged with the STND offer by simply asking the right questions.

Life Insurance Combined with an LTC Benefit

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solution have developed plans combining Life and Long-Term Care Insurance in a single plan. Genworth, Lincoln Financial and John Hancock offer these plans, while other companies such as Nationwide and others are introducing similar products.

John Hancock has an interesting way of dealing with the problem. If a 60-year-old male wants to add the right to take \$9,000 a month from his death benefit to pay for Long-Term Care coverage, then he needs only elect a 2% access rider at an additional cost of \$507 a year (total cost \$6,571) and \$9,000 can be distributed for 50 months to pay for long-term care from his \$450,000 life policy.

A similar minimal annual expense of \$285 (total cost \$4,514) will give the healthy 55-year-old spouse the same type of benefit. In effect, the death benefit will be spent for Long-Term Care insurance, if necessary. The Hancock plan, like others, offers richer benefits for additional premiums.

This is a simple solution and comes with a guarantee that the price will never change. *The client knows that eventually either through nursing home payout or death benefit, money will be paid to someone at some point.*

The advisor can take into consideration present life plans and perhaps even use old underperforming life policies' cash values through 1035 exchanges or lump sums from CDs to either increase coverage or discount premiums.

The total protection cost will be lower and guaranteed to never change and the clients can go into retirement knowing they are protected up to the amount they thought necessary.

If an advisor wanted to increase the life insurance protection to totally protect the survivor spouse and keep costs reasonable, then an additional \$550,000 20-year term plan is available for approximately \$2,800 a year for a male age 60. The additional \$550,000 would create more than enough money to replace the primary pension if the 60-year-old spouse died young (life only SPIA for \$5,600 for female spouse at 65 is \$883,000) and the \$450,000 permanent benefit will work perfectly for the client spouse if she receives only the permanent face amount after her age 75.

A 55-year-old woman can have the same coverage for about \$1,300 a year. To provide both with \$1 million death benefit with \$9,000 a month long-term care for five years would cost \$7,078 plus \$4,514 plus \$2,800 plus \$1,300, totaling \$15,692, which is considerably less than the \$28,800 reduction in the client's substantial defined benefit needed to purchase a 100% survivor pension with no certain payment to anyone.

The cost of course is simply a negotiation and can go up or down depending on the client's tolerance for risk and premium payments. The cost with no additional term is \$11,592, not very different from the \$8,997 cost for Long-Term Care coverage alone. The combination plan makes it possible to deal with death and long-term care risks in an affordable and attractive way.

Seven Ways to Increase the Average Premium on Life Insurance Sales

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post-retirement expenses and may see this as a way to eliminate one of those costs.

Be aware of target premiums when proposing UL plans to clients. Several carriers offer rolling targets and may pay additional first year premium in the second year of the policy. This is especially important when a sale is being proposed where the coverage is not designed to last to age 100. There could be commission dollars left on the table that rightfully belong to you.

While these strategies offer ways to increase premium, they do so by engaging clients in a discussion of choices. In effect, they help the client become more aware of how life insurance can benefit their financial future.

Producers who take advantage of these seven strategies will be rewarded for their extra effort.

**First American has
moved to new offices at
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