

Meeting Today's Challenges with Premium Financing

CMS – Succession Capital Alliance held its third annual traditional premium financing conference in Las Vegas in August sponsored by Pacific Life. More than 100 advisors attended the two-day invitation-only event. Experts described ways that advisors can take advantage of traditional premium financing to maximize estate and business planning for high-net worth clients.

A premium financing conference could not have come at a better time. Premium financing is gaining popularity in today's environment with lenders charging very low interest rates and insurance companies offering more competitive products.

With traditional premium financing, the client enters into a fully collateralized loan arrangement with the intention of holding the life insurance policy to maturity. Traditional premium financing arrangements are generally utilized for estate liquidity needs and offer the most advantageous loan rates, fees, and spreads. With premium financing, high net worth individuals borrow money to pay the premiums of a large life insurance policy that is needed for estate and business planning purposes. "Premium financing is not a product, but an alternative funding method for life insurance premiums," explained Julian Movsesian, MBA, president and founder of CMS & Succession Capital Alliance.

So why would a wealthy client want or need to finance the purchase of a life insurance policy? There are a multitude of reasons including the following:

- The client wants to retain ownership of their liquid assets.

- A significant portion of the client's wealth may be tied up in a business that they plan to pass on to the next generation.
- The client has assets that are not easily liquidated. For example, they may not want to sell real estate in today's depressed market to purchase a life insurance policy or they may want to avoid the potential capital gains tax related to the sale of their property.
- The client wants to provide an income schedule to their beneficiaries.
- The client wants to retain assets for charitable giving.
- The client has business needs, such as key person, buy-sell funding, and deferred compensation.
- The client wants to take advantage of discounted cash flow associated with premium financing instead of paying premiums in cash.
- The client wants to retain the use of capital that would otherwise be used to pay premiums.
- The client wants to minimize or eliminate the drain on current investments that would have been used to pay life insurance premiums.
- The client wants to take advantage

of favorable interest rates and terms on borrowed funds.

- The client wants to take advantage of potential gift tax savings.

For these reasons and more, Alisha Zaayer, director of premium financing for Pacific Life reports that traditional premium financing is alive and well. "The market has changed. We are post STOLI, IOLI, and hybrid; traditional premium financing remains a popular strategy for high net worth individuals and businesses."

Andre Blaze, director of Marketing and Training for Succession Capital Alliance said that premium financing is talked about by many, but is done successfully by very few. He stressed that it is essential to have expert support from case inception to closing, and more importantly, service future loan renewals. Ron Shuley, Divisional Vice President of Pacific Life said that a lot of producers want to do premium financing themselves, but without the expertise, it's not as likely to be a successful sale. He added that marketing is important and having multiple lenders is a must.

Leveraging Your Book of Business

Julian Movsesian explained how advisors can identify clients from their existing book of business who may be good candidates for premium financing:

- A high net worth individual or business with a minimum of \$10 million in assets.
- The client has established a need, and has the ability to pay the non-financed premium for permanent life insurance.
- The client's first year premium is at least \$100,000.
- The client has greater investment opportunities they could take advantage of if they didn't have to pay premiums in cash.
- The client understands the value of leverage.
- The client is able to post additional collateral using liquid assets or a bank letter of credit.

Communicating With Clients

Andre Blaze said that communicating with clients is important when it comes to premium financing. In fact, advisors face liability if they do

not fully disclose the loan strategy before it is implemented. The advisor needs to explain the following:

- Why a multi-lending platform is important to clients and advisors.
- Changes in interest rates or fees and how they may affect future performance.
- Projected collateral needs in the future to maintain the integrity of the strategy.
- Loan exit strategies as a safety net if desired.

Julian Movsesian said, “We see cases where the producer does not ask the right questions of the client. The client’s biggest fear is a liability on their balance sheet. Tell them that you will be creating an asset on their balance sheet, which is the policy’s cash value growth.

Using Indexed Universal Life Insurance

One popular strategy is to use premium financing to purchase an indexed universal life (IUL) policy. IUL offers several advantages including a guaranteed minimum annual interest rate, the potential for long-term cash accumulation, as well as death benefit protection. Stephan Mitchell – IUL Product Marketing Specialist for Pacific Life said, “IUL has taken hold. IUL protects against the downside of the market while offering tax favored gains.”

However, he urged advisors to be aware of insurance carriers that illustrate unrealistic rates and returns. He explained, “IUL is hot and regulators have not caught up with the product yet...The cap rate is based on three elements (policy changes, options prices, and bond yields) and an insurer can manipulate any of these elements to drive the cap rate higher than it should appear. Companies that initially had very high cap rates have dropped them.

Premium Financing for Baby Boomers

“Baby Boomers are the future of our business,” said Bill Bell, JD, MBA, Director of the Advanced Designs Unit for Pacific Life. In fact, he called Baby Boomers the best market for premium financing. Only 60% of Baby Boomers have life insurance and a large portion of them have term

insurance. Baby Boomers have diverse reasons to purchase life insurance:

- Family protection
- Pure insurance planning.
- Business Succession planning.
- Retirement income planning.
- Estate planning.

For a limited time, high net worth Baby Boomers can take advantage of the recently increased lifetime gift and generation-skipping tax exemption. “You can also use the cash value of a life insurance policy to provide a supplemental retirement income,” he said.

Bill Bell also described several other planning tools for Baby Boomers, including split funded defined benefits, which can provide an annual benefit defined by the plan itself as well as a sizable tax deductible benefit.

He noted that there is a real future in phantom stock arrangements using life insurance. The business can reward key executives with the success of the business without giving up ownership of the business.

Steve Oshins, JD, stated a dynasty trust will last 360 years without transfer taxes. Julian Movsesian noted that asset protection is a huge market with potentially huge savings in gift taxes.

In conclusion, experts at the conference revealed that premium financing is more relevant than ever. Only a very specific type of client will benefit from this strategy, but it behooves advisors when identifying these clients that getting the right kind of support to assist them is paramount. □

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