

Emerging Industry: The Purchase of Life Insurance Policies

By Dennis F. Gorman, Esq., CPA

Have you decided that you no longer need your seven-digit life insurance policy, and would you like to receive significant cash for it? A new industry has emerged mainly involving hedge funds, investment speculators and large investors who acquire life insurance policies with the hope of collecting hefty policy payoffs upon the insured's demise.

The price at which investors may be willing to acquire your policy is a combination of your age (life expectancy), the face value of the policy, the strength of the life insurance company, and the future premiums that are actuarially projected to your estimated year of death. Where the insured's health is an issue and where the insureds are advanced in age, these factors may lead to a sale price significantly more than the cash surrender value of your policy. You will have to report a capital gain on the sale of your life insurance policy. People typically decide to sell a life insurance policy either when it is no longer needed in the context of their estate plan or when the cost of maintaining the policy exceeds their financial means.

LIFE INSURANCE TRUSTS

In some cases where insureds have multiple policies, it may be possible to sell one or more policies and use the sale proceeds to cover future life insurance premiums on the retained policies. Where multiple life insurance trusts are involved, it may be possible to merge one or more trusts together to combine policy

sales proceeds with retained policies so that the future policy premiums can be paid by the trust on a gift-tax-free basis. The market for purchasing life insurance policies has somewhat contracted in the near term due to credit conditions and increased scrutiny by Congress and the SEC. However, unless we see legislation significantly regulating this industry, it is unlikely that it will disappear in the near future.

CAUTION

It is important to deal with a reputable insurance broker in this area who is knowledgeable with the market. Many states do not require brokers to disclose their broker's commission on these transactions. However, there is no reason why the broker you select cannot voluntarily disclose this arrangement up front.

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www.fletchertilton.com

Dennis F. Gorman

P: 508.459.8037

F: 508.459.8337

E: dgorman@fletchertilton.com



THE GUARANTY BUILDING

370 Main Street, 12th Floor
Worcester, MA 01608
TEL 508.459.8000 FAX 508.459.8300

THE MEADOWS

161 Worcester Road, Suite 501
Framingham, MA 01701
TEL 508.532.3500 FAX 508.532.3100

CAPE COD

1579 Falmouth Road, Suite 3
Centerville, MA 02632
TEL 508.815.2500 FAX 508.459.8300