Premium Financed Policy: The Process to Fix

The Situation:

We were asked to help an attorney investigate the viability of a $50MM joint life premium finance arrangement entered into five years ago between her client and a wealth management firm. The trustee was a local trust company of the Irrevocable Life Insurance Trust. A related entity provided the funding, held the compensating balance, and acted as placement agent for the life insurance. The fiduciary standard relating to conflicts of interest was an obvious problem that needed addressing.

Details:

- Insured were older individuals
- Health was impaired on both individuals
- Face amount - $50,000,000
- Type of policy – Universal Life (interest sensitive)
- Policy Arrangement – Finance premiums and roll up the interest with minimal gifts
- External Financing – LIBOR + 2%
- Outstanding Loan - $7,800,000 (and growing)
- Client feels they misunderstood the arrangement, now the collateral calls on the policies are growing

Phase 1:

- Using actuarial models, we assessed the long-term viability of the original arrangement
- Decision option matrix for Remediating the policies developed:
    - Premium funding scenarios
    - Collateral call growth
    - Loan and gift analysis
    - Loan documents reviewed
    - Libor rate impact analysis
    - Interest crediting rate analysis
    - Options for maintaining full death benefit and reduced death benefit modeled

Phase 2:

- Case strategy development
- Assessment of original premium finance structure and the documentation used to support original assumptions of performance
- Provided support litigation services
- Rescission Strategy
    - Is this even a possibility for the client?
    - Strategy for negotiation with the institution
    - Was there any misrepresentation during the sale?
    - Were all possible scenarios explained to client?

- Life Settlement Assessment
    - Personalized actuarial life expectancy on both individuals completed in order to make a judgement as to viability of possible sale
    - How would a sale optimize the client's result?
    - If sale is possible would the after-tax cash settlement be enough to secure some of the balance of the life insurance or provide a way to unwind the current arrangement?
- Underwriting Analysis
    - Capacity issues
    - Reinsurance concerns
    - Health impairment issues

Final Phase:

- Litigation support was provided due to us uncovering possible fraud as application indicated the sale was made in Delaware when in reality it was signed in Maryland! The proverbial "smoking gun".
- Initiated negotiations for an additional $20 MM of coverage while the current premium financed $50MM was still in force
    - Negotiated with ten carriers before application process began
    - Successful completion of product placement of $17.5MM of coverage
    - Negotiated Standard Health Rating despite health impairment, which provided significant premium savings
- Advised on new insurance trust structure with legal team
- Advised on Estate Planning options with legal team
    - Gifting
    - Lending
    - Premium Funding Issues
- Counseled clients and legal team re: negotiations with the institution to optimize client policies
    - Froze interest rate on loan
    - Gave back some death benefit to funder due to possible fraud
    - Death Benefit was then used as collateral for what was now a $10,000,000 loan
    - Negotiated interest return on compensating balance
    - Compensating balance returned at a future date ($5,500,000)
    - Strategy for funding of premium on new insurance developed
    - Net death benefit based on Personalized Life Expectancy + new insurance will give family close to $30MM at an 85% probability of death

Fee:

The fee to accomplish the client's goals of unwinding the premium finance situation they found themselves involved with was $30,000