EQUITABLE

Commercial premium financing producer guide

Advanced Markets

Leveraging assets to source premium dollars

Commercial premium financing strategy

This guide is designed to aid you in understanding this type of commercial premium financing and the mechanics involved in premium financing. For the purpose of this guide, commercial premium financing means the financing of life insurance premiums by a third-party lender, such as a bank.

In the wealth transfer markets, life insurance professionals encounter a number of challenges. The lack of liquid assets to meet wealth transfer costs is one challenge that, with proper planning, can be avoided. Large estates of wealthy individuals are generally subject to transfer and income taxes at death. After all non-insurance estate planning techniques have been employed, many wealthy individuals determine that life insurance can be an effective way to reduce the impact of transfer taxes. However, these wealthy individuals may be reluctant to convert high-performing investment portfolios or business assets into cash to purchase life insurance, creating a liquidity challenge. A premium financing plan can be designed specifically to create the necessary estate liquidity while preserving estate assets.

How does commercial premium financing work?

Premium financing offers your clients an alternative method of paying life insurance premiums. Rather than using or liquidating current assets, the funds needed to pay premiums are borrowed from a commercial lender so that the client's investment portfolio or other assets can remain intact.

Advantages

- Depending on the loan interest rate and the loan program, possibly reduced current net out-of-pocket cost for the needed life insurance coverage
- Little or no impact on current investment portfolio
- Potentially favorable gift tax consequences for a number of years

The goal of premium financing is to allow clients to obtain needed life insurance protection by borrowing to pay premiums rather than liquidating other assets.

Who would consider commercial premium financing?

Premium financing is designed for use in wealth transfer cases where the need for life insurance has been established, but the funds required to pay premiums might necessitate the liquidation of estate assets, or where direct premium payments by the policyowner would result in certain gift tax consequences. The plan allows clients to borrow funds to pay life insurance premiums, thereby potentially reducing their net out-of-pocket expenses.

The goal of premium financing is to allow clients to obtain needed life insurance protection by borrowing to pay premiums rather than liquidating other assets. This strategy is not intended to be used to generate tax benefits. In almost all cases, interest paid on borrowed funds will not be deductible for income tax purposes.

This strategy is designed for clients who can qualify for minimum net worth and minimum financed life insurance premiums set by the lender. Clients must qualify on a financial basis for premium loans. Loan underwriting is separate from any carrier medical or financial underwriting.

How does the loan work?

A lender will generally begin a financial review of the loan application when the related life insurance application is formally submitted.

At that time, provided all documentation is complete, the loan processing and review will begin. The minimum review and funding time is approximately 2 to 4 weeks.

Typically, the lender will review the future stream of premium payments required to purchase and maintain the life insurance policy and the loan performance projection reflected on a premium finance illustration. Lenders offer a variety of loans and terms will vary. Each application to borrow an annual premium may require a separate financial underwriting decision by the lender. The lender will periodically reevaluate the loan to determine whether changes in the borrower's financial condition or in the relationship between cash values and the outstanding loan balance may require other collateral, or may warrant discontinuance of the future loan installments due to increased risk. The lender's decision to extend credit for each new premium payment is separate and independent of the client's right to continue their life insurance coverage.

Most lenders offer various types of loans. In some cases, interest on the premium loan may be deferred for a period of years. The borrower may pay annual interest in advance or in arrears each year. In addition, the lender will require the life insurance policy as collateral for the loan, and may also require other collateral in addition to the policy. The loan can be repaid over time or may continue until the death of the insured, depending on the terms of the loan arrangement.

Loan interest rate

Loan interest rates are established on an annual basis for the immediately succeeding year, and will vary from year to year based on the fluctuation in the 1-year London Interbank Offer Rate (LIBOR) or the Prime rate.

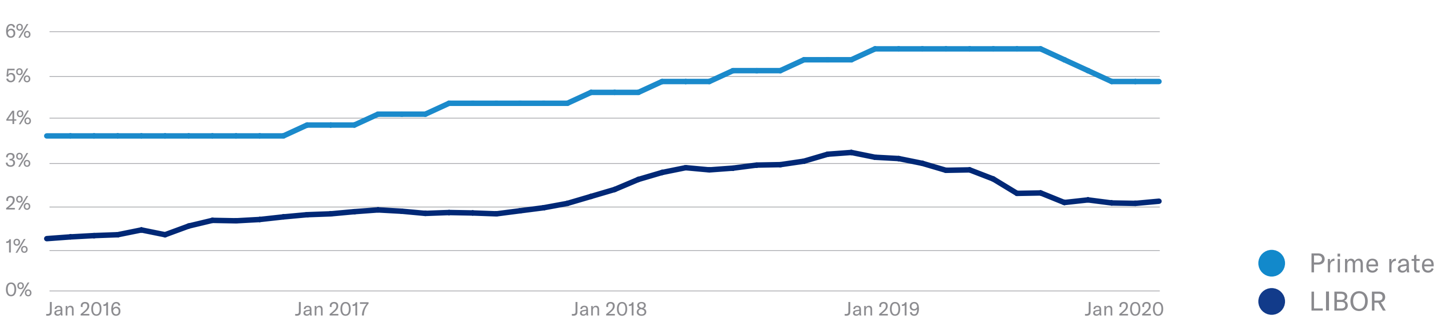
Both LIBOR and Prime rates fluctuate and, therefore, the interest rate at the time the loan closes may differ from the rate that was initially presented in the sales process. The lender will base the loan rate on the 1-year LIBOR or Prime, adding a spread of 50 to 400 basis points. The *Wall Street Journal* publishes both money rates. Actual loan interest rates are determined on a case-by-case basis, taking into consideration the loan amount and the lender's exposure. Typically, a lower rate is charged on larger loans or on loans where substantial collateral is available. Smaller loans and loans where the lender assumes a higher risk are typically charged higher rates. Once initially established, the spread for a particular loan is fixed and will not change. There is no guarantee that future loans will be made to pay premiums due under the policy.

2016-2020 1-year LIBOR and prime rates

2016	LIBOR	Prime	2017	LIBOR	Prime	2018	LIBOR	Prime	2019	LIBOR	Prime	2020	LIBOR	Prime
Jan	1.14%	3.5%	Jan	1.71%	3.75%	Jan	2.27%	4.5%	Jan	2.98%	5.5%	Jan	1.81%	4.75%
Feb	1.18%	3.5%	Feb	1.76%	3.75%	Feb	2.5%	4.5%	Feb	2.87%	5.5%	Feb	1.38%	4.75%
Mar	1.21%	3.5%	Mar	1.8%	4%	Mar	2.66%	4.75%	Mar	2.71%	5.5%	Mar	1%	3.25%
Apr	1.23%	3.5%	Apr	1.77%	4%	Apr	2.77%	4.75%	Apr	2.72%	5.5%	Apr	0.87%	3.25%
May	1.34%	3.5%	May	1.72%	4%	May	2.72%	4.75%	May	2.51%	5.5%	May	0.67%	3.25%
Jun	1.23%	3.5%	Jun	1.74%	4.25%	Jun	2.76%	5%	Jun	2.18%	5.5%	Jun	0.55%	3.25%
Jul	1.43%	3.5%	Jul	1.73%	4.25%	Jul	2.83%	5%	Jul	2.19%	5.5%	Jul	0.45%	3.25%
Aug	1.56%	3.5%	Aug	1.71%	4.25%	Aug	2.84%	5%	Aug	1.97%	5.25%	Aug	0.45%	3.25%
Sep	1.55%	3.5%	Sep	1.78%	4.25%	Sep	2.92%	5.25%	Sep	2.03%	5%	Sep	–	–
Oct	1.58%	3.5%	Oct	1.85%	4.25%	Oct	3.08%	5.25%	Oct	1.96%	4.75%	Oct	–	–
Nov	1.64%	3.5%	Nov	1.95%	4.25%	Nov	3.12%	5.25%	Nov	1.95%	4.75%	Nov	–	–
Dec	1.69%	3.75%	Dec	2.11%	4.5%	Dec	3.01%	5.5%	Dec	2%	4.75%	Dec	–	–

Please note: The above rates are historical and are not guaranteed of future rates or trends.

1-year LIBOR and Prime rate history



Loan collateral

In all cases, the loan must be 100% collateralized. The policy cash value will be collaterally assigned to the lender to serve as some or all of the collateral.

The cash surrender value of any universal life or indexed universal life policy issued by Equitable Financial Life Insurance Company, NY, NY (Equitable Financial), or by Equitable Financial Life Insurance Company of America (Equitable America), an Arizona stock corporation with its main administrative office in Jersey City, NJ. Equitable America may currently be used as collateral in a lending program. Depending on the type of policy being financed, a maximum of 100% of the non-guaranteed cash surrender value of the policy may be used as collateral for the loan.

The collateral assignment grants the lender a security interest in both the life insurance death benefit and the policy cash value. If the cash value is not sufficient, the lender may require additional collateral. If the policy cash value in later years exceeds the loan amount, the client cannot access the policy cash value until the lender releases its claim on the policy. The collateral assignment includes the borrower's representation and warranty to the lender that no bankruptcy proceedings are pending, and that none of the borrower's property is subject to assignment for the benefit of creditors. In the majority of cases, the policy values are the lender's primary source of collateral. If they are illustrated as diminishing over time, then the lender's security may similarly be projected as diminishing. Consequently, it is unlikely the lender will approve a case where collateral will be significantly impaired.

In some cases, a personal guarantee by an individual such as the trust grantor may be required. The personal guarantee of the loan may involve gift- or estate-tax consequences that should be reviewed by the guarantor's private counsel.

Types of collateral

In most instances, a lender may require collateral in addition to the life insurance. In these instances, only liquid collateral will be accepted and can be liquidated at any time without consequences to the borrower, if the borrower is in default.

Acceptable collateral may be:

- A letter of credit from a bank approved by lender
- A Certificate of Deposit or Money Markets
- An insurance policy
- Cash equivalents
- Marketable securities (valued at lender's discretion)

Collateral maintenance

The lender will monitor collateral continually through receipt of policy and portfolio statements. If the collateral fails to meet the standards set forth in the loan documents, the client will be informed of the shortfall and may be required to provide additional collateral. Note that when financing an indexed universal life policy, it is important to determine the lender's approach to coordinating the timing of loan renewals, collateral shortfall calculations and the crediting of an index segment.

Typical outline for client eligibility

Eligibility requirements vary by lender.

Here is a general guideline for client eligibility:

- Has a net worth that meets the carrier's and lender's minimum requirement.
- Qualifies both medically and financially for a life insurance contract.
- Signs an acknowledgment and disclosure premium financing statement.
- Signs a final premium financing illustration.
- Purchases a policy with the minimum premium requirement set by the lender.
- Borrows in the name of a trust, corporation, partnership, limited liability company, similar entity or individual, as approved by the lender.
- Supplies appropriate and reliable financial documentation to assist the lender in determining loan eligibility, and cooperates with annual credit and financial checks performed by the lender.

Financial professional requirements

Financial professionals implementing a commercial premium financing funding strategy must provide Equitable Financial or Equitable America with certain documentation related to the proposed loan. Requirements vary depending on the insured's age and policy face amount involved. Details are provided in the April 3, 2015, field bulletin titled "*Guidelines and Financial Underwriting Requirements for Commercial Premium Financing of Life Insurance.*" In all financed cases, Equitable Financial and Equitable America require a signed acknowledgment and disclosure premium financing statement.

Some additional tax considerations

Loan interest is not deductible for income tax purposes

For individuals, interest accrued on borrowed money to pay premiums on a life insurance policy is considered personal interest and is not deductible.

For businesses, however, interest on borrowed money to pay premiums on a life insurance contract may be deductible in certain circumstances. These circumstances are narrow and will be inapplicable to most financing cases. Consequently, premium financing must not be marketed or implemented with loan interest deductions.

No illustration or spreadsheet will reflect such a deduction. Clients should consult with competent tax counsel.

Estate tax consequences

When determining the amount of estate tax, life insurance proceeds are included in the gross estate of the insured if, at any time during the 3 years immediately preceding death, the insured possessed any incidents of ownership in the policy.

In a situation where a personal guarantee has been made, the issue arises as to whether the personal guarantee could be considered an incident of ownership in the policy, or interest in the policy that could cause estate inclusion under Internal Revenue Code Sections 2033 through 2045. Premium financing is commonly used in situations where life insurance is intended to be purchased outside of the estate in order to provide a source of liquidity with which to pay wealth transfer costs. Use of premium financing presumes that the grantor's guarantee of loans to an irrevocable life insurance trust (ILIT) does not cause inclusion of the policy proceeds in the grantor's estate for estate tax purposes. Potential clients should be told to seek the advice of their own counsel.

Commercial premium financing submission

Premium financing can be a viable planning tool and can be effectively implemented when you understand the needs not just of your client, but of the finance lender as well.

Each lender will have its own requirements in place and should be contacted early in the process. The first step is to confirm collateral as soon as possible. When submitting the loan, you must know the borrower, guarantor and the holder of collateral; if collateral cannot be confirmed, loan documents cannot be prepared. Any changes made to borrower or collateral will result in delays.

As with any life insurance application, a cover letter submitted with the credit application will go a long way in clarifying the needs of the borrower. A complete, well-organized cover letter will help the various departments of the lender understand the loan strategy of your client. For example, does your client want to pay the loan interest in advance, arrears or do they wish to defer? Who are the participants in this particular arrangement: borrower, owner, guarantor and beneficiary? Is there collateral to be pledged, and if so, what is it? Your cover letter will hopefully give a comprehensive view of your client's overall estate planning strategy. The lender will advise the client of any additional information it may require based on the particulars of a given case.

For more information, contact Advanced Markets.

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