

**"FREE" INSURANCE:
SOME THINGS I'D TELL MY MOTHER**

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The elderly (typically 70 or older) parents of some of my closest friends have been approached by insurance agents selling what some call SPIN-LIFE and others call investor-initiated life insurance, or stranger-owned life insurance.

These senior citizens and their families come to me because I've written two major text books on life insurance, lectured since the '70s in the graduate divisions of two law schools, throughout the country on life insurance topics for over 40 years, and provided advice and consultation to Forbes, Fortune, the Wall-Street Journal, and the New York Times, and BusinessWeek on insurance and estate planning.

They also come to me because they know I have a better than average sense of "smell" - an exceptional record predicting "too good to be true" schemes that ended up in trouble.

Although the scheme takes many forms and is constantly mutating, "free" insurance is pitched essentially this way:

We ask that you do two things for us:

The first is for you to make certain medical and other personal information available to us.

The second is that you do something which we can't legally do directly. We can't buy millions of dollars of new insurance on your life. That would be illegal. So we'd like you to take out the insurance for us by pretending to take it yourself out for your own needs. Just tell the insurer you are buying it for "estate planning purposes." (We may "puff up" your wealth and/or income so you can qualify for a multi-million dollar policy and make even more money. And don't tell the insurer about other policies you may be applying for - we want to get all we can)).

In return, we'll provide you with millions of dollars of "free" coverage for two years. We'll do that through no-risk ("non-recourse") financing which we'll arrange.

We know you don't really want any new insurance. That's fine - because we both know, that's not what this is all about. At the end of the two years, you can sell this two year old insurance to us and make a heck of a profit! Most sellers have been getting more than enough to easily pay off the premium loans, interest, and - even after brokerage costs - make a very handsome return. That's in addition to your two years' free insurance.

But wait - there's more! If all that's not enough, we will offer you a "sign-up" bonus of – say 2% of the death benefit! So if you buy \$1,000,000 of insurance, you get a check for \$20,000! Buy \$5,000,000 of insurance, we'll write you a check - today - for \$100,000.

And if you don't get an offer you like, in a worst case scenario, we've arranged for the lender to agree to take the policy in full payment of your debt. You'll owe nothing - no matter how large your debt or how little the policy is then worth. And of course, you can always keep the policy. You just have to pay back the loan, the interest, and other charges and pay premiums from that point on.

You have no outlay, no risk, and you may pocket hundreds of thousands, maybe millions of dollars - merely by allowing us to take advantage of your "unused insurance capacity."

My friends want me to tell them this free lunch will taste as good as it looks.

So what do I say?

For openers, investor-initiated life insurance is **FRAUD**. It's **theft by deception** of the insurer - AND it's a **VIOLATION OF THE INSURABLE INTEREST LAWS** of every state in this country. It starts with a purchase the investors can't legally make on their own. Ask them - they'll tell you! It's unlawful for strangers to buy insurance on your life. **So your participation makes YOU complicit in helping them do something illegal - something the law clearly prohibits!**

In fact, in every state, insurance fraud is a serious misdemeanor or felony and in many cases will be punishable by jail time! So Mom, fudge the facts on your application and I'll bring you a file in your next birthday cake!

If that's not enough, here are **more things I'd tell my mother:**

1. You are selling away your "life." Once investors get the policy on your life, no matter how much your family or business needs new coverage (and the insurance company wouldn't issue the policy if they *didn't* think your family or business really *did* need it), you may never be able to get more or replace what is gone.
2. **If this is such a great deal for investors, why isn't it an even better deal for your family?** If insurance is *really* needed, why not buy and keep it for your family - rather than have it go to strangers? Have you checked to see if your family or business *really needs* the coverage?
3. **Any incentive** (car, cash, trip, or other "gift" to get you to buy the policy) will be **taxable to you immediately as ordinary income.**

4. **The "free" insurance isn't free at all! You may have to pay \$30, 40, or 50 thousand dollars or more in tax each year on the economic value of the coverage that's provided for you.**
5. If you decide to turn over the policy to the lender and "walk away" from the loan, it's highly likely that the IRS will treat discharge of indebtedness as ordinary income. In other words, **you will incur significant income tax - and will have no cash to pay for it.**
6. **If you sell the policy to a settlement company, your gain will be all or mostly all taxable at ordinary income rates.**
7. **Your family may never get any insurance - even if you die within the first two years.** Why not? Because if the insurance company discovers that the intent from inception was to sell the policy to investors, the insurer may rescind (take back) the policy. If you "shade the truth" or misdirect, or omit essential information, your failure of candor may amount to what lawyers call a "material misrepresentation" **Now you are (at best) involved in expensive and aggravating litigation. Worse yet, you may have engaged in insurance fraud; in many states, as I noted before, that's a felony (criminal) offense.**
8. **Your estate is potentially liable to investors for millions of dollars!** You are going to be asked to sign many many documents. Those highly complex legal papers are designed to protect the investors' and lender's interests (That's a polite way of saying that the provisions you agree to are stacked in favor of *them* – the investors and the lenders - and not you!). You may be asked to make certain guarantees about your insurability to the lenders and investors. **If after the investors have purchased the insurance on your life, for some reason they can't collect, those investors may sue your estate for the millions in insurance they expected to receive - but didn't.)**
9. **No matter what you think you've been told, the investors are not bound to purchase the policy. You may not get anywhere near the amount of the money you expect. After taxes, you may suffer a sizeable overall loss!**
10. **After you sell the policy to the investors (or let the bank take it and sell it to investors), you are the *only* party to the contract that hopes you live a long time.** Make no mistake; **this scheme is nothing less than financial speculation on your life.** Someone you don't know and have never met can profit by your *early* death. You may receive calls as often as once a month; the person at the other end will be disappointed – if you answer the phone! **You will be told (and will want to believe) that the odds are small of some investor taking steps to profit by your early death. But no one in this deal will - or *can* assure you - that it *can't* happen.**

The original investors have the legal right (and often the intent) to sell the policy on your life - immediately - to other investors. There's no legal limit to how many times the policy on your life can be sold - or to whom. You will neither know nor have any control over who profit from your early death.

- 11. Sell your life insurance policy on a secondary market and you will have to agree that the purchaser (including any subsequent purchaser if the policy is resold) has a permanent power of attorney to access your medical records.**

So what would I tell my mom to do about SPIN-LIFE?

One word will do.

It's **“DON'T!”**

Stephan R. Leimberg, Esq. is CEO of Leimberg Information Services, Inc., an e-mail and database service providing information and commentary on tax cases, rulings, and legislation for financial services professionals. The 1998 Edward N. Polisher Lecturer of Dickinson School of Law and 2004 recipient of the National Association of Estate Planners and Councils Distinguished Accredited Estate Planner award, Leimberg was also awarded the Excellence in Writing Award of the American Bar Association's Probate and Property Section. He is Editor, Keeping Current, a quarterly publication of the Society of Financial Service Professionals, has served as Adjunct Professor in the Masters of Taxation Programs of both Villanova and Temple University Schools of Law, and is on the Editorial Board of The Estate Planning Journal.