

Life Settlement Tips & Techniques

History of the Life Settlement Industry.

In 1911, the Supreme Court ruled in *Grigsby v. Russell* that life insurance policies were freely assignable for value. Viatical settlements were born in the early 1990s as a solution for those terminally or chronically ill lacking the funds for the expense of medicine, treatment and hospice care. Rising out of the viatical business, life settlements took hold by focusing on individuals who were *not* terminally or chronically ill but, instead, had experienced a change in their financial needs subsequent to the issuance of their life policy. Since the late 1990s, life settlements have evolved into their own industry that is, according to a June 2005 Bernstein Investment Research and Management report, expected to “grow more than tenfold to \$160 billion over the next several years.” Industry sources estimate that over \$20 billion of transactions will take place in 2009, alone. According to Stuart Hersch, CEO of Cantor Fitzgerald’s Cantor Life Markets, the value of policies traded is likely to reach \$100 billion in the next five years.

What is a Life Settlement?

The Life Insurance Settlement Association (LISA), the national trade association for the life settlement industry, defines a life settlement as “the sale to a third party of an existing life insurance policy, generally by seniors over the age of 70, for more than its cash surrender value (CSV), but less than its net death benefit.” Simply stated, a life settlement enables older individuals, businesses, trusts, and other organizations to sell a life insurance policy they currently own—but no longer want or need—for a lump sum cash payment in an amount greater than the CSV.

For years, life insurance companies held monopsony power over the repurchase of their own issued policies. In cases where a policy owner could no longer continue payment of the premiums, the policy just lapsed with no economic benefit to the owner. Those with term policies or those seeking CSVs on their universal or whole-life policies met with an equally disadvantaged return on their investment. With life settlements averaging 22% of their policy’s face value, policy owners now have a vehicle to produce liquidity and an appropriate return on their policy.

Who are the Players in a Life Settlement Transaction?

Most life settlement transactions involve a policy owner, an insured, the policy’s insurance carrier (the “insurer”), a life settlement provider (the “buyer”), an institutional funder, a life expectancy provider, and a life settlement broker.

The policy owner actually owns the policy and is the only one authorized to sell the policy. The policy owner can be an individual, a trust, a bank, a corporation, or a charitable organization.

The insured is the individual life that is covered by the life insurance policy. An insured, who is not the policy owner, cannot sell the life insurance policy but must cooperate in signing certain releases if the sale is to be executed.

The insurer, or insurance carrier who issued the policy, collects the premiums required to keep the policy in force and pays the death benefit to the beneficiary upon the death of the insured. For most life settlements, only carriers with a rating of BBB or better are considered.

The life settlement provider is generally referred to as the buyer. Using internal funds or those from institutional funders, the provider will solicit, underwrite, and extend offers to acquire policies that meet their investment guidelines. For policies acquired, the provider ensures that the ownership and beneficiary changes are executed, settlement amounts are paid to the selling policy owners, commissions are paid to the life settlement brokers (if applicable), future premiums are paid on the acquired policies, the life of the insured is monitored for all policies, and the death benefit claim is promptly filed and collected upon the death of the insured. A list of suggested providers is furnished to life settlement brokers when they register with Life Settlement Administrators (LSA).

Institutional funders continue to provide the majority of funds used to purchase life settlement contracts. Starting as early as 2001, institutions such as Deutsche Bank, Berkshire Hathaway, and American International Group became buy-and-hold investors, serving to open the door for the entry of German closed-end funds in 2003. Life settlements are attractive as an asset class due to their lack of correlation to other financial instruments. Some recognizable names who have participated as funders include Berkshire Hathaway, Citibank, Credit Suisse, Deutsche Bank, Dresdner Bank, DZ Bank, Fubon Bank, KBC Bank, Goldman Sachs, and Morgan Stanley.

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Life expectancy providers, using mortality tables, generate an average life expectancy on the insured. Almost all life settlement providers now require one or two life expectancy reports to be submitted with each case. Currently, the four most common life expectancy providers used are AVS, 21st Services, EMSI, and Fasano Associates.

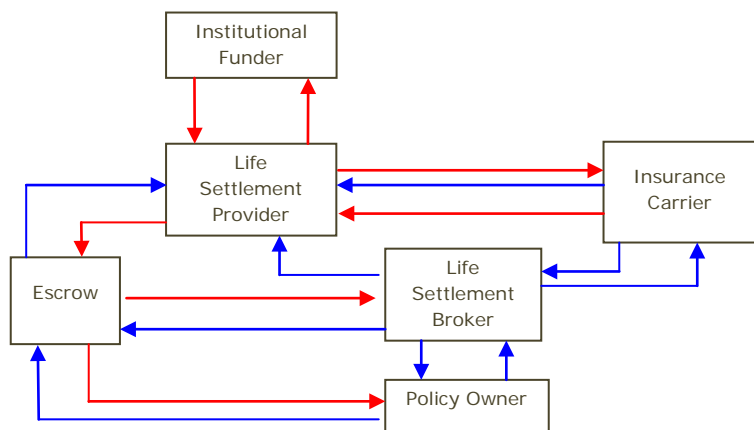
A life settlement broker maintains a fiduciary responsibility to their policy owner client. That duty, in part, is to ensure that a life settlement is in the best interest of the client and that efforts have been made to achieve the best available market value for their policy. The life settlement broker is charged with carrying out the duties of preparing, submitting, negotiating, and settling the client's case. Under the direction of the life settlement broker and the terms of its LSA Licensing and Servicing Agreement, LSA provides these services on behalf of the life settlement broker.

How Does a Life Settlement Transaction Work?

Figure 1 below illustrates the flow of funds (red) and documents (blue) in a typical life settlement transaction.

FIGURE 1: THE FULL CYCLE OF A LIFE SETTLEMENT TRANSACTION

The policy owner engages the life settlement broker for representation in the transaction. The life settlement broker (or LSA under their direction) (a) compiles all necessary forms, and information, including a request for information from the insurance carrier; (b) prepares and submits a proposal to multiple life settlement providers; (c) receives and negotiates multiple offers to achieve the best available market price for the policy; (d) after approval from the policy owner, accepts final negotiated offer from winning life settlement provider; and (e) continues to provide data to the life settlement provider and escrow (optional) until close. The life settlement provider (a) arranges for funding through the institutional funder who transmits funds to the provider; (b) transfers the gross settlement amount to escrow; and (c) upon close of escrow, continues to service the life contract by paying the insurance carrier the scheduled premium payments. The policy owner sends escrow the executed change of ownership documents that evidence the sale of the policy to the new owner. Escrow then proceeds to (a) remit the settlement amount to the policy owner (less broker's commissions); (b) remit the broker's commission to the life settlement broker; and (c) close escrow. The life settlement provider secures the revised ownership policy from the insurance carrier. Upon the policy owner's death, the insurance carrier remits the death benefit to the life settlement provider, at which time the life settlement provider remits the agreed upon principal and return to the institutional funder. The cycle has now been completed.



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How Long Does It Take to Process a Life Settlement?

Notwithstanding a number of variables that can enter into a transaction resulting in a delay, on average, a life settlement transaction should fund within 6 to 10 weeks from the time a completed application package is received.

Who Qualifies for a Life Settlement?

This is a question with a wide-ranging answer. For the most part, the actual answer depends upon the market you choose to target and the buying parameters of your life settlement providers. As an example, you may decide to focus on individuals owning policies where the insured is as young as 55. There are a few providers who will look at policies in that age group. Alternatively, you may decide to target the contestable or "wet" paper market (policies that are still within their 2-year contestability period). There are a few providers who will consider policies of that age, as

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well. The majority of institutional providers, however, will generally look for life policies having the following characteristics:

- The insured has attained a minimum age of 65.
- The life insurance policy has a death benefit of at least \$100,000.
- The insured has a life expectancy between 24 and 180 months.
- The life insurance policy is universal life, convertible term, whole life, second-to-die, or survivorship.
- The life insurance policy was issued at least 24 months prior to its expected sale.
- The life insurance policy is renewable without contingencies except for continued payment of premiums.
- The life insurance policy was issued by a U.S. based carrier with a rating of BBB or better.
- The policy owner must reside, be situated, or domiciled in a state that is unregulated or in a state in which you and the provider are licensed to conduct life settlements.

Most institutional providers stay clear of variable universal life (VUL) products due to their classification as a security. Unless you are a broker-dealer licensed to sell securities, you will want to decline the representation of these policies.

What is Premium Financing and Can Premium Financed Policies Be Sold?

Individuals obtaining a new life insurance policy may have the option to borrow cash and use it to pay the life insurance premiums. This is commonly known as premium financing. Premium financing is not an insurance policy; it is a means of financing the purchase of insurance. The premium finance company will lend the premiums to the policy owner in exchange for the policy owner's obligation to repay the loan plus interest. When the loan matures or the insured passes away, the loan amount plus interest is paid back to the premium finance company. The policy owner may retain the life insurance policy, sell it, or collect the death benefit of the insured less the outstanding loan value.

There are two types of premium financing—recourse and non-recourse. Recourse financing enables the premium finance company to reach the policy owner's other assets, if needed, to keep the loan in good standing or to repay it upon maturity. Non-recourse financing, however, restricts the premium financing company's actions only to its collateral for the loan—the policy. Many premium finance transactions are structured through the creation of an Irrevocable Life Insurance Trust (ILIT), a unique legal document to help keep the proceeds of a life insurance policy outside of the estate and thus potentially free of estate tax and income tax.

Premium financing—both recourse and non-recourse—are legitimate practices that can be used legally and wisely to maximize benefits to the policy owner. Over the years, premium financing has been abused by some in their creative attempts to circumvent insurable interest laws. As a result, proper premium finance transactions are, at times, mistakenly characterized as improper transactions. The industry is currently experiencing a growing trend where providers are reluctant to consider premium financed policies for a life settlement.

What Role Does the 'Age 65 and Over' Population Play in the Marketplace for Life Settlements?

Past industry practice suggests that life settlement brokers and providers have historically concentrated their marketing outreach on high net worth individuals. The abundance of prepared marketing materials and techniques targeting financial planners, stockbrokers, accountants and attorneys demonstrates this fact. According to the U.S. Census Bureau in July 2006, only 6.8 million individuals age 65 and over had a median net worth, excluding home equity, of \$125,000 or higher. These high net worth individuals, however, only accounted for 18% of the total population over 65.

Continuing to remain a significantly underserved segment of this total senior population is the 30.8 million or 82% of seniors age 65 and over. Unlike their more affluent counterparts who might be restructuring their estates, these seniors may find themselves with greater motivation to sell their life policies in the life settlement market due to tight economic conditions, loss of retirement funds, burdensome long-term care, and higher living costs. These are needs that have only become more imperative during these challenging economic times.

Commenting on this virtually untapped market, one individual from a national life settlement trade association drew this correlation to the growth in mutual funds: "The middle-income insured is virtually untapped for life settlements, not unlike the beginnings of mutual funds that at one time were limited to high net worth individuals."

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Bernstein Investment Research and Management reported that individuals over age 65 are growing at more than three times the rate of the total U.S. population. Soon, one can add the aging "baby boomers" to that growth, the youngest of which will turn 65 years of age in 2011.

Why Would a Policy Owner Consider Selling Their Policy in a Life Settlement?

Reasons for selling a life insurance policy are numerous. Below are just some reasons why others have sold theirs:

- Change in insurance needs triggered by the estate or financial planning process and/or estate taxes.
- Policy's underperformance coupled with a need to alleviate escalating premium payments.
- No longer a need for the policy due to the death or divorce of beneficiary.
- Create proceeds to build or replenish retirement programs.
- Create cash resources and restructure their life insurance coverage.
- Provide cash resources for use in seizing current investment opportunities.
- Provide for unexpected or escalated long-term care, assisted living, or health care expenses.
- Term policy was approaching maturity.
- Policy was being surrendered or lapsing due to non-payment of premiums.
- Term policy premiums were becoming too burdensome.
- Generate funds for donating to a charitable organization without impacting donor's existing liquidity.
- Charitable organization selling a donated life policy to eliminate premium costs and generate cash.
- Corporation selling its corporate-owned life insurance (COLI) to recover business assets for reinvestment.
- Retired or terminated executive selling a key man life policy received as part of a separation package.
- Business owner seeking to monetize his company-owned or personal life policy to save his business.
- Generate funds to help a family member suffering financial hardship from unemployment or foreclosure.
- Create funds to pay for a grandchild or adult child's higher education.
- Create funds to travel, purchase a home, or acquire a long-desired luxury item.
- Create liquidity to resolve a current credit crisis or start over in a post-bankruptcy condition.

What are Some Benefits to Policy Owners Who Sell Their Policies?

- Creation of value from an asset previously thought to have little or no value to the policy owner.
- Generation of a lump sum cash settlement to be used for any purpose.
- No future policy premium obligations.
- Cash received by the policy owner exceeds policy CSV.
- Increased wealth generated from reinvestment of settlement proceeds in other investment vehicles.

Are There Tax Implications to a Life Settlement?

The IRS issued Revenue Ruling 2009-13 providing guidance on the tax treatment afforded life settlement proceeds. Dependent upon the type of policy and the policy owner's tax basis, proceeds received from a life settlement may be partially or wholly exempt, partially taxable, or wholly taxable. Taxable portions of a life settlement may be taxed at ordinary or capital gain rates.

This information is not tax guidance. As with any tax-related matter, you should consult your professional tax advisor.

Can a Life Settlement Affect Public Assistance the Policy Owner May be Receiving?

Receipt of a life settlement may affect their eligibility for public assistance programs such as medical assistance (Medicaid), Aid to Families with Dependent Children (AFDC), supplementary social security income (SSI), and drug assistance programs. If they are concerned about how the receipt of a life settlement payment will affect them, their family, and their spouse's eligibility for public assistance, they should contact their social service agency before entering into the life settlement transaction.

What if the Insured Wants Another Life Insurance Policy After The Policy Owner Sells the Current Policy?

The underwriting process for issuing new life insurance policies varies according to the individual insurance carrier. An insured's health may have changed since the first policy was issued. Consequently, there is no guarantee the insured will be able to obtain a new policy or one of acceptable terms. Should the insured desire to maintain a life

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policy of some denomination, the insured should notify the policy owner and then proceed in obtaining the new policy before entering into the life settlement transaction.

Is a Life Settlement Broker Required to Keep Personal Information Confidential?

Yes, any financial, medical, or personal information obtained by a life settlement broker about the policy owner, the insured, their family members, their spouses, or significant others may not be shared with anyone unless the life settlement broker has received written approval that the information may be shared. Brokers using LSA receive this written approval when their clients complete the application process.

If a Policy Owner Enters Into a Life Settlement Contract, When Does He Get His Money?

Some providers use an escrow agent or trustee to handle the money paid to the policy owner and the life settlement broker. If an escrow agent or trustee is used, the escrow agent or trustee will send the policy owner their money usually within three business days of the date the insurance carrier confirms the completed transfer of ownership to the provider. If an escrow agent or trustee is not used, the provider will typically send the policy owner the money after the policy owner has signed the life settlement contract, the papers needed to transfer or assign their policy to the provider, and the provider has received verification of the change from the insurance carrier. You will most likely receive your commission from the provider within 10 to 15 days after the close of the settlement.

What if the Policy Owner Has a Change of Mind?

If the policy owner has a change of mind about selling the policy, the policy owner can cancel the life settlement contract at any time before the end of the rescission period—a period that varies by state. To cancel the life settlement contract, the policy owner will return any money the provider paid to the policy owner for the purchase of the policy along with any premiums the provider paid to keep the policy in force. If the policy owner rescinds the transaction, you will be expected to return all commissions and fees earned and collected on the sale of that policy.

What if the Insured Dies Shortly After the Sale of the Policy?

If the insured dies at any time during the rescission period, the life settlement contract will automatically cancel. The provider will pay the policy owner, or beneficiaries designated by the policy owner in the life settlement contract, any proceeds it receives from the policy, minus any money it already paid for the purchase of the policy and any premiums it paid to the insurance carrier to keep the policy in force. The insurance carrier or the provider should refund any unearned premiums paid.

What Happens After the Policy Owner Gets His Money?

After a policy is sold, all rights and obligations of the policy are transferred to the provider. The policy owner is no longer responsible for paying premiums and is free to use the cash proceeds however desired. After the provider has paid the policy owner for the sale of the policy, they may begin calling to check on the insured's health status.

What if the Insured Does Not Want to be Contacted About His Health Status?

If the insured does not want to be contacted about their health status, the insured may appoint an adult person or persons to be contacted on their behalf. That person must be in regular contact with the insured and the insured must give the provider the contact's name, address and phone number. Once the insured has given the provider this information, the provider may not contact the insured unless it has tried and has not been able to reach the insured's contact person for more than 30 days. If the insured needs to, the insured can change the contact person at any time by sending a written notice to the provider.

How Will the Insured Know Who Will be Calling About Health Status and How Often Can They Call?

The provider must give the insured the name, address, and phone number of the person who will be contacting the insured or the designated contact person(s) about the insured's health status. If the insured's life is later determined

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to end in one year or less, contacts to check on the insured's health status are limited to once every 30 days. If the insured is expected to live for more than one year, contact is limited to once every three months.

Will the Provider Be Calling the Insured's Doctor to Check on the Insured's Health Status?

Some providers will use the insured's signed medical release form to check with the insured's doctor for updates on the health status. The medical release form tells the insured's doctor that the insured authorizes the doctor to give medical information to the provider, the policy owner's life settlement broker, or the provider's representative. If the insured decides against the provider contacting the doctor, the insured may withdraw his consent.

Why are So Few Providers Willing to Buy Contestable Paper?

Life insurance policies contain contestable clauses that give the insurer the right to contest a claim or void a policy within a two-year period following the policy's issue date. This period is intended to protect the insurer from high-risk applicants trying to game the insurance carrier. Creating a risk to anyone buying the policy within that two-year period, most providers and their institutional funders prefer to wait until after the contestability period expires.

As a Life Settlement Broker, How Do I Market New Clients Who Want to Sell Their Policy?

If you do not already have one, you will most likely develop a marketing strategy that enables your new life settlement brokerage to build its client base. You know who is eligible for a life settlement. The question now is how do you find them? One such source is the agent and advisor group made up of financial and legal professionals. This group includes insurance producers, financial planners, accountants, lawyers, stock brokers, and other professional advisors. These professionals hold their clients' trust and, if a life settlement is appropriate, would be willing to present the opportunity to their client. Another source for clients will be through direct-to-consumer marketing.

How Do I Find Agents and Advisors and Why Would They Refer Their Clients to a Life Settlement Broker?

Finding agents and advisors may be a great deal easier than one might imagine. Your state department of insurance probably has a database that you can access which will provide you the names of those licensed in the state. If not, Agent Media has a great list of [emails](#) as well as [full addresses](#) that you can purchase for a reasonable price. Professional trade and networking associations such as the [Financial Planning Association](#), [The National Association of Personal Financial Advisors](#), the [Family Office Exchange](#), the [Advisors In Philanthropy](#), [The Advisors Forum](#), [Certified Legacy Advisors](#), and [LinkedIn](#), to name a few, may have directories that you can consult. Other marketing techniques or suggestions you may want to consider include:

- Join a local business networking group with members who are in the financial planning, insurance, estate planning, or elder law professions.
- Launch an email campaign that targets agents & advisors in those fields.
- Author a simple article for insertion in a trade newsletter or publication.
- Place a small print or online ad where agents and advisors are likely to be reading.
- Issue newsworthy press releases about your company that bring attention to your website.
- Consider participating in an industry trade show as an exhibitor or sponsor.
- Think outside the box. For example, realtors need home buyers with cash to make their down payments. Reach out to your local realtors with your value proposition—a life settlement will enable their client to close the sale, the realtor to earn his commission, AND the realtor to possibly earn a small referral fee from you. The realtor's client may not qualify for a life settlement but their older parents might.
- The same logic applies to senior care facilities, in-home care providers, retailers who might want to display a tri-fold brochure of yours (LSA can provide you with these, if you choose), and anyone else who can benefit from having their customer or client better equipped to pay for their services. The possibilities are endless.

Recognizing their fiduciary responsibility, most agents and advisors will suggest a life settlement to their client if they believe it is in the client's best interest. Some additional incentives might also apply, as illustrated below:

- A settlement provides another financial tool for clients to meet their financial plan.
- The original insurance producer "locks-in" renewal commissions on the original policy.
- Cash from a life settlement can be redeployed to generate cross-selling opportunities for other insurance or financial products, resulting in fee income.

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- Cash from a life settlement becomes available for other business investments.
- Cash from a life settlement enables the realtor's client to close the transaction generating a commission.
- Fulfills the advisor's fiduciary responsibility of presenting all appropriate opportunities to the client.
- If allowed, fee income may be paid by the life settlement broker in consideration for the referral.

You Mentioned Direct-to-Consumer Marketing. Can You Share Any Tips?

Depending upon your budget and desire to build your brokerage, this can take the form of anything from leveraging your personal and professional contacts to direct mail to broadcasting your own 30-second commercials on radio or cable stations of your choice. These are just some suggested marketing ideas you might want to consider:

- Conduct a direct mail campaign with 4X6 postcards.
- Speak at local senior organizations.
- Place a small ad in printed publications, newspapers, and other media that seniors or caregivers will read.
- Consider authoring a small article to publish on senior-oriented websites, retirement community newsletters, magazines, and newsletters provided by senior care facilities and in-home providers.
- Online advertising, using Google or any other search engine.
- Many providers have marketing materials on their website that you can use free of charge.
- Partner with other related businesses to see if they will place a link to your website on their website page.
- Consider charitable and religious organizations as a source of business. They are in need of donations and a life settlement from one of their donors or members could amount to a large sum of money. You might also want to "sweeten" the donation by agreeing to donate a percentage of your commissions to the organization, too. Public school, college, and athletic support programs run by parents should also be considered. A life settlement can be a great fundraiser.
- Find a partner and engage in some cooperative mailing programs with your community financial institutions, stockbrokers, real estate brokers, commercial and casualty insurance brokers, and financial planning firms.
- 30-second spots on radio.
- 30-second spots or infomercial-type commercials on local cable stations.

What Does It Cost to Process a Life Settlement Case?

In addition to the employee costs you will incur to process a case (an expense not incurred if you are an LSA client), there are a variety of third-party costs that usually require payment at the time the service is provided. By far, the largest expense is for life expectancy (LE) evaluation reports. Most providers now require two LE reports which, in total, can cost in the range of \$600-\$700. Other additional third-party expenses can result from APS & medical record fees, duplicate policy fees, copying & scanning services, overnight courier costs, long-distance phone service, and other miscellaneous costs. Third-party costs can total between \$700 and \$1,000, depending upon the case being processed. LSA's basic [Processing Fee](#) is a flat \$800 which includes the cost of two LE reports and all other costs mentioned here. Although rarely encountered, LSA's Processing Fee excludes any trust-related costs, costs of any professional advisors (CPAs, financial advisors, or lawyers) who may be engaged by and on behalf of your client, and any extraordinary costs that may arise in the context of processing the case.

What Range of Commissions and Fees are Customarily Charged Policy Owners?

Before getting into what the industry generally charges for commissions and fees, it is fair to mention that some life settlement brokers do not disclose, to their client, the actual amount of the offer that was received for the sale of the client's policy. Instead, these brokers determine how much they want to retain for commission and only pass-thru an amount that they believe the client will accept. We discourage this method of operation and, instead, support full disclosure and transparency throughout the entire transaction.

Life settlement brokers usually use one of three methods to arrive at the commission charged to clients for the services they provided in a life settlement: (1) a percentage of the policy's face value, regardless of the offer amount received; (2) a percentage of the gross offer received for the sale of the policy, regardless of any cash value the policy owner would have secured by just surrendering the policy; and (3) a percentage of the net settlement amount, determined by deducting the policy's cash value from the gross offer to arrive at a "value created" for the client. Although there are life settlement brokers who still charge in the range of 4%-6% of the policy's face value or 30% of the gross offer, the industry appears to be leaning toward the "value created" method where life settlement brokers have been known to charge anywhere from 15%-30% of that net settlement amount.

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In addition to the commissions charged, some life settlement brokers also charge their clients a flat processing fee ranging between \$1,000 and \$2,000. This fee enables the life settlement broker to offset their third-party costs and the risks associated with the processing of 100% of the cases, but where a lesser percentage is actually sold. Industry convention calls for revenue to be generated only from those policies actually sold. Cases processed but not sold become a cost of operations.

LSA wants its clients to have a high closing ratio. To assist them toward this goal, free of charge, we provide an LSA Preview of each case submitted to determine our opinion of the case's potential marketability. As a benefit of this free Preview, LSA's clients are better able to control their overall processing costs by mitigating the number of cases processed but not closed due to conditions known at the beginning of the case. Although LSA cannot render any guarantee that the case will attract a price in the marketplace or, if so, what that price will be, it does provide an additional layer of review before any expenses are incurred by the life settlement broker.

Should Agents or Advisors Receive Compensation For the Referral and, If So, How Much Should It Be?

If you are operating in an unregulated state, unless prohibited by law, you may compensate anyone you choose for the service of providing you a referral. This amount is strictly determined by you. In the industry, although some receive no compensation, those agents and advisors who do receive compensation are receiving approximately 6%-10% of the net settlement amount. Part of this may be paid as a percentage of your commission as a life settlement broker and part of it may be paid from the client's sale proceeds as an additional commission paid by the client at the time of the sale. The rule to keep in mind here is, "What is reasonable?" For example, if you are charging your client a 30% commission, it might be deemed unreasonable and greedy if you added another 10% to pay the agent or advisor who referred the client (making it a total 40% commission to the client). In this case, you may want to pay the agent or advisor some agreed amount out of your commission received.