

COMMERCIAL PREMIUM FINANCING LENDING PROCESS

WHAT TO KNOW

Commercial Premium Financing (CPF) can look and feel like many other consumer loan transactions that your clients have experienced before. However, there are unique dynamics. This paper will describe the application and renewal process detailing what may happen and when.

PREPARING FOR THE APPLICATION PROCESS

CPF arrangements can either lend to an individual, a trust established by an individual or a corporate entity. To expedite the process, it is recommended that required documentation is collected early in the process and the necessary collateral is determined.

Some lenders prefer collateral assets to be held at their institution. Doing so could produce better lending parameters like a lower rate, but typically isn't a requirement for loan approval. Any amount financed that is not fully collateralized by the life policy's cash values will be required to be collateralized by another account, or sometimes a letter of credit (LOC).

Here's a rundown of what's required for the application:

INDIVIDUAL/TRUST

- Cover Letter - Include background (e.g., on client and loan structure)
- Signed Credit Application (insured, borrower, and guarantor signatures required)
- Insurance carrier illustration(s)
- Copy of valid government-issued ID from all parties to the loan

- Signed and dated personal financial statement (less than six months old)
- Bank and brokerage statements to support liquid assets on personal financial statement
- Previous two years' complete tax returns
- Complete copy of executed trust (not needed for initial financial underwriting) is required prior to loan documents to avoid potential redocumentation fees

CORPORATE

- Cover Letter - Include background (e.g., on client and loan structure)
- Signed Credit Application (insured, borrower, and guarantor signatures required)
- Insurance carrier illustration(s)
- Copy of valid government-issued ID from all parties to the loan
- Consolidated corporate financial statements for the previous two years, plus interim statements for cash flow, income, and balance sheet
- Previous two years' corporate tax returns
- Corporate formation documents (not needed for initial financial underwriting)

After receiving all or most of the documents required for approval, the lender will typically issue a commitment letter that will detail any outstanding verification requirements and the expected loan parameters, including the loan rate. The rate isn't locked until loan documents are issued, and any rate adjustments should be communicated during the period between the issuance of these two items by the lender. It's also recommended to ensure that any investment accounts that are going to be used for collateral allow for such an arrangement. Different financial institutions may have different rules and guidelines to establish an assignee to investment funds.

Each loan may have different and unique interest rates, rate lock periods, loan renewal guarantees, and collateral requirements. It is recommended that these important details are reviewed with the client to ensure the terms are acceptable before moving to the next step of issuing the loan documents.

COLLATERAL VALUATION

- Life insurance policy cash values are typically valued at 95%-100%.
- Cash/Cash equivalents (e.g., certificates of deposit, money market accounts, and LOC) are typically valued at 100%. If the investments are not held in one of the financier's accounts, it may discount the valuation depending on where they are held.
- Bonds are typically valued at 50%–80% depending on the type, and are subject to approval by the financier.
- Marketable securities are typically valued at 50%, however this is subject to the portfolio's diversification. If the portfolio is highly concentrated in one, or a few securities, a larger discount could be applied. A financier may also have share price trade minimums.

Once the premium financing is in place, there is an annual renewal process for each loan. Even if the loan has terms with guaranteed renewability, there is still a process for each additional premium loan. In addition to potentially having a different loan interest rate for the upcoming year, any collateral used, including the life insurance policy, must be reviewed based on investment performance over the previous year.

Below you will find guidelines and timelines to be aware of for the renewal process.

RENEWING LOAN TERMS

60 DAYS PRIOR

- Request in-force illustrations
 - Universal life policies without enhancement riders will be valued on the non-guaranteed cash surrender value based on the *current* crediting rate.
 - Indexed universal life policies without any cash value enhancement riders are valued using non-guaranteed cash surrender values. Any funds in an index account will be based on the guaranteed crediting rate (typically 0%). Any funds in the fixed account will be based on the *current* crediting rate.
 - Whole life policies, without any cash value enhancement riders, are valued using the non-guaranteed cash surrender value credited using the *current* dividend yield.
 - Policies with cash value enhancement riders are evaluated on a policy-by-policy, rider-by-rider basis.
- Financier will evaluate values and determine collateral requirements for the following year
- Financier will also evaluate any updated values to previously pledged collateral

45 DAYS PRIOR

- Financier will begin underwriting the transaction for the upcoming year

30 DAYS PRIOR

- New loan rate is set
- Renewal package prepared and issued to the borrower
- Renewal package prepared and issued to the insurance representative

This article provides information meant to serve as a guide to enter into and maintain a commercial premium finance arrangement. It is not an exhaustive list and draws from information collected through lenders and M. We recommend checking with your lender/financier to ensure compliance with their obligations and requirements. Below you'll find additional tips and issues to avoid while going through the lending process.

TIPS TO SECURE FUNDING

- Confirm collateral early.
- Submit trust and or formation documents as soon as possible.
- Confirm the brokerage account or bank accepts financier's control agreements.
- Provide contact information for the collateral holder at the brokerage house or bank.
- Ensure *all* tax returns and financial statements are signed and dated in initial loan packages.
- Ensure the client understands the details of the commitment letter thoroughly, and contact the account manager if any conditions are unclear.
- A sample rate is quoted in a cover letter. APR is locked when loan documents are issued.
- Return final documents (premium finance illustration and carrier illustrations) signed by the client.
- Obtain a printout screen from the brokerage showing the financier as the assignee to funds.

ISSUES THAT MAY ARISE

- Providing incomplete (signed and dated) documents, including but not limited to tax returns, financial statements, and other parts of the loan package.
- Once submitted, any changes to the illustration, borrower, collateral, or interest will cause delays.
- Trust, bylaws and articles of incorporation are essential for putting legal documents together.
- Before funding can take place, an original interest check from the counterparty and/or original LOC must be given to financier.
- Failure to carefully examine the final conditions to funding and fulfilling those conditions, stops the financier from paying the premium.
- If collateral is not approved and in place by the time your case gets to the financier's legal department, loan documents cannot be prepared.
- Index policies should be illustrated at the guaranteed rate with the current cost of insurance.

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