HNW Families and Life Insurance

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Why do wealthy families and UHNW clients need life insurance?

Very early on in my career, which was some time ago, one of the many things I didn't understand was exactly that. You would have a very wealthy individual, a very wealthy family, with more wealth perhaps than they would need for that generation, and perhaps more wealth than is even needed for the next generation, yet they're interested in buying life insurance. I was very puzzled by this. Why would they need to create more wealth? And then I realised, of course, that it's not about creating wealth, it's all about liquidity.

You've heard the expression, concerning wealthy families, and particularly wealthy Asian families, that they tend to be "asset-rich and cash-poor". And there's a reason for that. Wealthy people haven't made their wealth by sitting around on piles of cash; they put their money to work. They put their money to work in businesses, in property, in private equity, in the financial markets. And not only do they put their money to work, so that they don't have much cash sitting around, but they also borrow money. And there's a reason for that, too. They borrow money because they know, or at least they believe, that they can make better returns from their investments than the cost of that borrowing from the bank. They get in a position where they have a lot of illiquid wealth and a lot of borrowing, and that is fine while the patriarch and matriarch are alive and well.

But it's when they pass on that the problems become apparent. Questions arise like, "Have they made a will," or "Are they passing away intestate?" Either way, there are difficulties. (And by the way, it's estimated that about 40-50% of people pass away without even making a will.) If they have made a will, the assets and everything that's in their name gets frozen while the probate process goes ahead. That can take anything up to a year, or sometimes even more, which means that your heirs and your executor cannot deal with those assets until the grant of probate has been received. That doesn't stop loans being recalled, it doesn't stop interest needing to be paid on financing. It just stops you being able to liquidate investments or manage the assets until probate has been granted. And if you haven't made a will, then you have even more difficulties, because you're subject in Singapore to the intestacy rules of Singapore, which can be rather complicated in terms of who's going to inherit. And again, more and more delays.

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What is needed in many of these situations is some way of paying off these liabilities. Your personal guarantees no longer have any value. If a businessman has given a personal guarantee for his corporate loan, that personal guarantee is worth nothing when he passes away. That's a problem, and maybe the corporate loan can get withdrawn. Many families who've invested in the US, the UK, or Japan, in real estate or in securities, find that they have estate taxes to pay. (In the US and the UK, for example, this could be as much as 40%.) And that's a liability for the next generation. It must be paid in cash.

The thing to think about is what legacy are you really leaving your family? You've built up all this wealth. You think you're doing a good thing for your family, which you are, but at the point when you pass away, perhaps unexpectedly (and not many of us know exactly when we're going to pass away) what problems are you actually leaving? Am I leaving a mortgage liability to my spouse? If I am elderly maybe my spouse who's inheriting now under the intestacy laws or under my will may be incapacitated in some way. Or my children inherit, and when they finally get probate, they've got to deal with all these expenses and loans. What the family really needs at the point when the patriarch or matriarch passes away, is a huge lump of cash to appear to take care of the estate taxes, to take care of paying back mortgages and loans and not leaving problems to the next generation. And that's where life insurance comes in. It's all about having that liquidity. After you've spent your whole life without it, when you pass on, that's just when your family need it. That's really the big driver.

There are other advantages, too, if you cannot divide your estate easily between your beneficiaries. (And this can affect even people who are not high net worth). You may have substantial value in your property, especially in countries like Singapore and Hong Kong, but you've got two or three children. How do you divide your wealth between the children? Life insurance, with the liquidity arising, can help you to equalise the legacy that you're leaving. There are many, many reasons, and it's mainly all about liquidity, although there are sometimes also tax planning advantages in using life insurance if high tax jurisdictions are involved.

What kind of life insurance is best for them?

There are many different types of life insurance in the market. Whole life Insurance has been around a long time, as has Term Insurance, and Savings and Annuity products. More recent arrivals include Universal Life Insurance, which came to Asia in 1997 in Hong Kong, and 1998 in Singapore. There's a new variant on this which is Indexed Universal Life. And Variable Universal Life, which is a subset of the broader concept of Private Placement Life Insurance, which is incredibly interesting, particularly for international tax-planning situations. It has been very common in the US and Europe for a number of years and is relatively new in Asia. It's taking a little bit of time for people in the Asian market to understand the power and the potential of Private Placement Life Insurance, but the interest is growing. In terms of the Whole-Life space, there's even variants now where you can have a Whole Life policy with a Terminal Illness rider as well. You can get paid out before passing away, which can be quite nice.

So, you have all these different products in the market, but then underneath the products, you get variations by carrier. You don't just have a Manulife whole-life product, you could have an AIA whole-life product, and you can have whole-life products from many different carriers. To really understand how they work in detail, you must get the carrier-issued

term sheets and information, and really understand the detail of how each one works, and what specific terms and conditions they have.

You asked which of all these products is best, or even which type of product is best. I think there is no best product. There's just the one that best suits you, that best suits the client. There will be an optimal solution for each client, depending on their need, but that presupposes that the person they're talking to, the broker or whoever is their advisor, takes the time to really understand what the client's particular circumstances and needs are. And there will be a very good, optimal solution taken from this range of possibilities.

Does a client need an adviser and, if so, what should they look for in an adviser?

Given the complexity of the possibilities of types of life insurance and different products, I think one is highly recommended to take an advisor. If you are a Singaporean and your assets are all in Singapore and you want a very simple life-cover solution, you can go online and search online for a product. But I think if you're talking about High Net Worth clients, and Ultrahigh Net Worth clients for sure, then you really do need some sophisticated advice. You need to know exactly which type of product is best for you, and sometimes you would need to avoid the possibility of a miss-sale -getting something that you didn't fully understand or that has features you don't want. You need an advisor who takes time to understand your situation and then takes time to explain the products properly.

I've met clients who have purchased Universal Life Insurance, which is not a bad thing- there is nothing wrong with it - but clients who use it have got to understand that these policies can lapse. They may not last your whole lifetime. They may lapse before you lapse. And you need to understand these things. It doesn't mean they're bad, but they've got to be properly explained. You need an advisor who takes time to understand you and takes time to explain the advantages and disadvantages of the different products.

And you also need an advisor who has a certain technical competence. Why do I touch on this? Because with HNW clients who are looking to put fairly significant policies in place, one must consider, for example, questions like, should you have a trust involved, should you have a trust as the beneficiary of your policy. You need an advisor who can actually talk about trusts, not just insurance. Why would you have a trust as the beneficiary of your policy? Because we don't know when we're going to die. I know I'm going to pass away, but I don't know when. And if I have a substantial policy that is coming to my beneficiaries, I don't know whether my beneficiaries may be incapacitated at that time, or they may be living in a high-tax jurisdiction, or they may be in the middle of a divorce case, or they may be in the middle of business litigation. It may be highly inconvenient for them to receive a large cash distribution just when I pass away. Having a trust as the beneficiary or a trustee as the beneficiary gives that flexibility of timing as to when the benefits will go to my heirs.

Another example where technical understanding is needed is when leverage is taken. For example, a lot of people have bought whole life or universal life policies with bank borrowing. What happens here is you assign the policy to a bank in Singapore and the bank becomes

the policy holder. After your lifetime, the assets go to the bank, and the bank will take back its loan. The question is, what happens to what's left? In many countries around the world, what's left in the policy proceeds after the bank has taken its borrowing will go to the beneficiaries you've named in your policy. Not in Singapore. In Singapore, the assignment that you make to the bank is an absolute assignment. What that means is that the bank will take its loan repayment from the insurance proceeds, but what is left will be in your estate. And then you're back to the question of, have you made a will? And then you've got the probate delays.

One of the benefits of insurance is usually that insurance proceeds can be paid out without going through a probate process. They usually come straight out to your beneficiaries. But if you assign that policy to the bank in Singapore with a Singapore assignment, then be aware that it's going to fall into your estate. And then you've got to think about all the issues around that. There's a lot of technical detail that your advisor needs to be on top of, more than just selling you a product.

So, for me if you're looking for an advisor, you need someone who's prepared to listen to you, someone who is knowledgeable about the different types of life insurance, even knowledgeable about the different products. If you're interested in universal life, can your advisor tell you about the slight differences between universal life policies of different carriers? And are they on top of issues around trust as beneficiaries, legal issues around the assignment of policies if you're leveraging? What is the level of competence of the person you're talking to? Finally, if you have some connection with overseas jurisdictions, especially high tax jurisdictions like the US, UK or Australia, your adviser should have at least some understanding of the tax issues involved. A red flag for me would be somebody who starts talking to you straight away about a specific product. There are plenty of people out there who will be happy to talk to you about life insurance and they will have a product they want to sell. They may be an agent, tied to a particular carrier. This is okay, but they should still take the time to find what is the suitable product for you and not be presenting to you very early on a product without first understanding exactly what you need.

How would you describe the state of the HNW life insurance industry in Singapore?

Singapore has a very well-developed life-insurance industry. It's been around for a long time. It was well-developed, of course, primarily for Singaporeans and for Singapore carriers. And the regulator does a very good job of protecting the interests of these two groups. What we're seeing in Singapore, particularly now that when you look at the growth of family offices, is that Singapore is starting to change from being more of a very well-regulated local market to a global hub in certain areas. For example, these family offices opportunities are attracting businesses and clients and wealth from around the world. I think this is also going to impact the insurance industry. More and more, very wealthy foreigners will be coming here. And it raises a couple of issues. For example, in Singapore at the moment, if somebody is resident in Singapore, they can only be sold, by a Singapore advisor, a Singapore insurance product. Now, that simply doesn't work for many foreigners. If you're a US client, you need a US-compliant policy. If you need what's called a non-MEC policy, a non-moderated endowment contract policy, you can't find it here. You need to be able to be introduced to a carrier overseas. If you need a Canadian-compliant policy, which is rather a complex thing to provide, you won't find a carrier here that can provide that and monitor it properly for you. If you're coming from continental Europe and you want policies in your own language, or you need to have an EU-issued policy to be compliant locally for tax reasons, you won't find it here.

My hope is that as Singapore evolves, the insurance industry, which is starting from a very strong base, starts to evolve more to accommodate Singapore as an increasingly global hub. I'm hoping that we will see a little bit more flexibility in terms of advisors who cannot find suitable local products being able to introduce the best, most suitable products for clients from outside, where necessary, and at least for non-Singaporeans. It can be done now, but only with case-by-case approval from the MAS, which is not the smoothest process. So, I'm hoping that we'll see something evolve in this space. ■