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Choosing the Best Insurance Distribution Option for Your Clients (Part 1)

Insurance proceeds can be provided to our families in various ways. Choosing the best way for your clients requires skill and care.

In this 2-part series, Joshua Lee shares his experience with us on some of the challenges your client might face when the wrong choice is made.

In Part 1, Joshua will go back to basics on our insurance nomination framework to examine the differences between revocable and irrevocable nominations.

In Part 2, Joshua looks at how insurance proceeds can be distributed without nomination and how a trust can be used to stagger proceeds over a period of time based on conditions you set today.

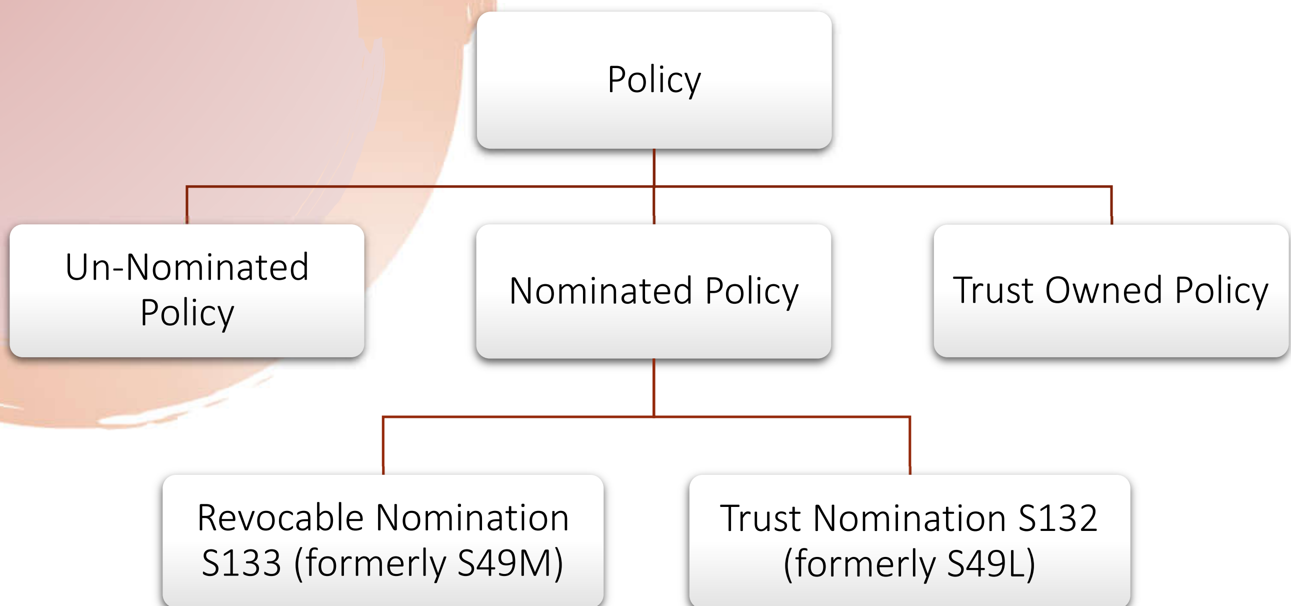
Author's Profile

Joshua first joined the financial services industry in 2004 and focused his work on assisting families with risk management as a financial consultant.

In 2017, having witnessed the issues faced by surviving family members when no proper estate planning is done by the deceased, Joshua started to study about estate planning and has been advocating the importance of financial planning with estate planning in mind since then.

Currently, Joshua is an Assistant Vice-President in Manulife Financial Advisers Pte Ltd, managing a team of 10 consultants.

Overview



Section 133 of the IA (formerly Section 49M)

A policy owner above the age of 18 may nominate anyone as a beneficiary of the full or any portion of the death benefit. This is formerly known as Section 49M (Form 4 Revocable Nomination). The policy owner can do a revocable nomination on his policy to bypass the ISA or the Will and allows the nominee to receive the death benefit in the absence of any Grant.

This can be used to provide immediate liquid for the family and is commonly used as it is flexible. The policy owner can make changes anytime as long as he is still of sound mind, but there are some potential issues to note.

Issue 1: Only 1 nominee in the nomination

A married man names his wife as the sole nominee to create immediate funds for his wife to take care of herself and their newborn upon his demise. Unfortunately, both pass away in an accident without a Will.
Under Section 133(5)(a) of the IA, the nomination is deemed to be revoked as there is no surviving nominee and the distribution will be based on the ISA. Even though the child eventually receives the payout, prior application to the Court to appoint a legal guardian for the child before applying for a Grant of Letters of Administration is time-consuming and costly. Family members taking care of the child would only have access to the funds after the process is concluded.

Issue 2: Lack of review

Policy owners commonly make a nomination but overlook the need to review their nominee from time to time.

For example, an individual who nominates his parents as beneficiaries and fails to change his instructions after marriage, even though he intends to benefit his spouse. Despite his marriage, the insurance nomination is not revoked, unlike Central Provident Fund (CPF) nominations and the Will. As such, his parents remain the beneficiaries of his policy.

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Issue 3: Assumption

During happier times in the marriage, a wife previously made a revocable nomination in favour of her spouse for her insurance policies. Over the years, the relationship deteriorated, but the wife stayed on in the marriage for the sake of her young children. She makes a new Will to distribute all her estate to her children in equal shares, assuming that a later Will overrides an earlier nomination. Unfortunately, the nomination stands and upon her death, her estranged husband benefits.

It is important to note that while a later insurance policy nomination revokes a previous one, a Will does not revoke an earlier insurance policy nomination unless specific requirements are met.

Trust Nomination Section 132 of the IA (formerly Section 49L)

To use this nomination, the nominee must be a spouse or child of the policy owner. Once the policy owner has made a trust nomination on the policy, the policy's living and death benefits do not belong to the policy owner. Essentially, the policy owner has given away his rights to the nominee.

However, such a nomination gives a distinguishing benefit of credit protection to the policy owner's family. Since the policy no longer belongs to the policy owner, the death benefit will not form part of his estate. Therefore, it will not be subjected to the policy owner's debts. However, one should be fully aware of the limitations that come with the unique benefit.

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Issue 1: Difficulties in revocation of nomination

When the relationship between the policy owner and his nominee turns sour, the policy owner may face a deadlock situation. For example, I have seen a couple who could never see eye to eye for years. Eventually, they ended up fighting an ugly divorce. The man had nominated his ex-wife as a nominee under Section 73 of the Conveyancing and Law of Property Act 1886 ("the CLPA"), not knowing the potential implications. Both moved on with their lives and remarried. When the man passed away, his new family found themselves left with nothing from his nominated policy, as all benefits were paid to his ex-wife instead.

Issue 2: Living benefits form part of the nominee's estate

Any changes made to the policy while the policy owner is alive, must be with written consent from the trustee, nominee, or legal guardian other than the policy owner after a trust nomination is made. What happens when a nominee passes away before the policy owner? In such a scenario, the consent from the representative of the nominee's estate is required.

I recall a case where one of my clients, Mdm Chua, had made a CLPA Section 73 trust nomination of her life insurance with critical illness benefits in favour of her spouse. When Mdm Chua's husband passed away due to Covid-19, Mdm Chua was stuck in a situation where her insurance payout would be paid to her late husband's estate if she becomes inflicted with critical illness. In that event, as her husband had died domiciled in Malaysia, Mdm Chua would likely have to incur additional time and costs to deal with her husband's

estate, in order to receive her critical illness insurance payout. We can only pray that critical illness does not strike her now.

Issues 3: Young beneficiaries

Early this year, a couple who each run a successful business approached me. They each had a loan of S$10 million and were both personal guarantors for their respective loans. To achieve credit protection against their creditors, they considered making a trust nomination in favour of their only son, for their insurance policy.

However, once their son attains the age of 18 years, the couple will need his written consent to make any changes to their insurance policies. In the event there is a payout soon after the child attains the age of 18 years, it is his to control and manage directly. At that age, he might not have the financial wisdom to handle the large sum of money. Instead of giving him an asset, they might be indirectly destroying him.

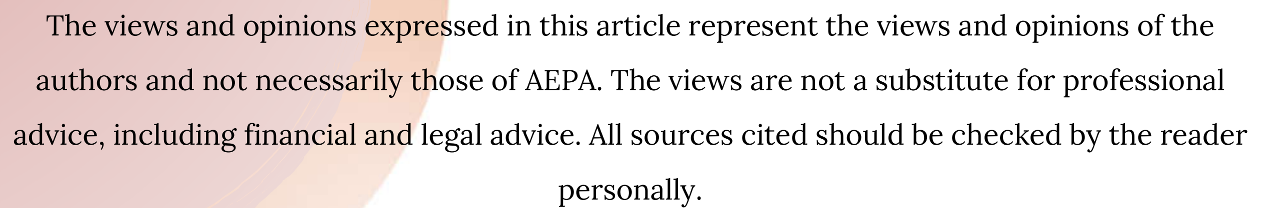
In such situations, a trust-owned policy may be more appropriate than making a trust nomination.

Conclusion

There are various ways to distribute payouts from insurance policies, as illustrated above. Each has their pros and cons.

Therefore, financial consultants must understand each client's unique family situation and their intentions, to suggest the method that best suits their needs. When doing our regular

reviews, we must focus on more than just coverage shortfall; The quality of their family relationship, family structure, and changes in the policy owner's life stages can severely impact our overall advice and must be properly considered.



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