INCREASING INCOME THROUGH INSURANCE SERVICES

By Lee Slavutin

CPAS THAT SELL VARIABLE LIFE INSURANCE AND VARIABLE ANNUITIES also need to be sponsored by a broker-dealer registered with NASD and pass the Series 6 and 63 examinations.

What a difference 10 years can make. During the past decade, many accounting firms have gone beyond offering traditional accounting and tax services to developing significant financial and estate planning practices. In addition, in the fall of 1999, the Group of 100 (an advisory group formed by the AICPA to help map out the future of the accounting profession) recommended that the profession position itself to provide one-stop shopping for clients. Thus, it is not surprising that some accounting practices now offer investment advisory services and, in states where it is authorized, investment and insurance products.

The Opportunity

Life insurance is a planning opportunity. The transaction can mean additional income and the chance to provide a valuable service. CPAs can be involved in several ways:

Policy audits. By ensuring that insurance policies have the proper ownership and beneficiary designations (e.g., designations that keep the insurance out of the insured's estate and avoid having a beneficiary such as a former spouse who may no longer be the intended beneficiary).

Insurance trusts. By reviewing any existing insurance trusts in order to guard against gift tax problems, protect the estate tax benefits of the trust, and confirm that *Crummey* notices are being sent to beneficiaries.

Buy-sell agreements. By reviewing existing buy-sell agreements to determine whether businesses are adequately funded (e.g., by life insurance).

Maximize retirement funds. Where a substantial IRA or retirement plan interest will generate income in respect of a decedent (IRD), by determining whether life insurance should be used to provide liquidity to the estate and heirs for paying estate and income taxes on IRD (so they don't have to prematurely withdraw funds from the retirement accounts). This could allow the client's retirement funds to grow tax-deferred (or in the case of Roth IRAs, tax-free) for much longer.

Other insurance needs. By discussing the related insurance coverage (such as long-term care and disability insurance) that should be part of every client's financial plan.

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The Transaction

Clients can purchase life insurance from their own insurance agent (or one recommended by a CPA) or directly from a CPA licensed to sell insurance. Obviously, if the insurance were purchased through a CPA, compensation for work performed on behalf of the client would normally come from the commissions. This may also be true when the insurance is purchased from someone with whom the CPA has a commission-sharing arrangement. In fact, when presented with the various choices, clients often have no problem with their tax or financial planning advisor sharing in commissions (especially if the advisor would otherwise be sending a bill).

Traps and Pitfalls

State accountancy boards. Most states permit CPAs to accept commissions and contingent fees (for guidance on state rules, see the list at www.aicpa.org/states/uaa/commfees.htm). Still, the decision to participate in insurance sales should be based on a firm's marketing philosophy and degree of comfort with product sales. As might be expected, certain requirements must be met to maintain objectivity and independence.

CPAs cannot sell insurance products to attest clients. But can they sell to an employee, shareholder, or employee benefit plan of such a client? Yes, according to a recent AICPA ethics ruling ["Commission and Contingent Fee Arrangements with Nonattest Clients" (ET 591.383-384)]. Nevertheless, it is important to consult with state regulations and an attorney knowledgeable with these rules to determine whether a different answer applies at the state level.

Based on AICPA Code of Professional Conduct Rule 503 (ET 503.1), CPAs are required to disclose their compensation to clients at the onset of an engagement if the possibility exists that they could sell an insurance product and receive commissions. Again, it is important to consult an attorney familiar with appropriate state accountancy laws for guidance in drafting a proper disclosure statement and determining whether any restrictions apply on entering into a fee-splitting (commission) arrangement.

State insurance departments and the National Association of Securities Dealers (NASD). To sell life insurance, CPAs normally must be licensed by the state in which they practice. Licensing requirements usually include completing a course of study (often about 40 hours), passing an examination, and receiving sponsorship by an insurance carrier.

CPAs that sell variable life insurance and variable annuities also need to be sponsored by a broker-dealer registered with NASD and pass the Series 6 and 63 examinations. Many insurance companies own a broker-dealer.

The licensing, compliance, and continuing education requirements of state insurance departments and NASD are voluminous and beyond the scope of this article. The most practical way to deal with this issue is to be affiliated with a reputable insurance broker and broker-dealer that can guide the practitioner through the maze.

Risk management. As with any new practice area, requisite steps should be taken to lessen the chance of mistakes or legal problems. For example, CPAs will want to—

- be properly licensed with the state insurance department and NASD.
- receive training in life insurance products and know how they are taxed, mar-

keted, and sold. In other words, learn to ask the right questions about insurance products without necessarily knowing everything. Ideally, a firm should have a strong background in estate and financial planning and should be prepared to provide appropriate partners, managers, and staff with the necessary education, training, and preparation for licensing.

- review their firm's professional liability insurance policy and any affiliated life insurance agent's professional liability policy to be sure that the policy covers the sale of insurance products.
- develop and document operating procedures. For each client, the CPA should carefully document how the amount and type of life insurance are determined, how the needs are established, what other options were considered, and why they were eliminated.
- perform appropriate due diligence on any third-party vendors and consult an attorney to draft any legal contracts and agreements.
- draft an engagement letter for new insurance clients that spells out the CPA's responsibilities and what the CPA has (and has not) agreed to do.
- develop a commission disclosure statement that complies with the applicable state and AICPA rules.

Practice Tips

Business structure. Tax practitioners that sell life insurance have three primary options regarding these services:

- Train existing staff,
- Hire specialists, or
- Form an alliance with an insurance agency, broker-dealer, or insurance carrier.

Most firms choose to form an alliance (which may start as a joint venture and then get formalized if the firm forms an LLC subsidiary). Many CPA firms that provide attest services also form an alternative practice structure to provide commission-based services to these clients.

A Valuable Opportunity

Tax practitioners are uniquely positioned to help clients choose appropriate life insurance products as part of their financial plans. They have the client's trust, see the client relatively frequently, and often know more about the client (financially and otherwise) than any other advisor. Practitioners can also profit by earning commissions on the sale of these products but face two major challenges: how to market the new services effectively and how to properly manage the risks associated with these services. ❑

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