Why Premium Finance Transactions Collapse and What Brokers Can Learn From Litigation

Jonathan M. Deer
Peyman Cohan

ABSTRACT

Premium financing for high-net-worth clients frequently fails, sparking a steady rise in litigation due to systemic flaws rather than policy performance. Disputes typically stem from volatile loan mechanics, including short-term maturities, variable interest rates, and unexpected collateral calls that restrict client liquidity. Furthermore, optimistic policy illustrations and unrealistic lifelong exit strategies create false expectations. Legal claims usually target how advisors framed these transactions, focusing on minimized risks and selective explanations. To mitigate liability and protect clients, brokers must adopt conservative assumptions, communicate transparently, and ensure structures are grounded in realistic loan and market conditions.

Vol. 80, No. 4 | pp. ##-##

This issue of the Journal was published June 2026.
Copyright © 2026, National Association of Insurance and Financial Advisors. All rights reserved.

Premium financing has long been positioned as a sophisticated planning technique for certain high net worth clients, but it is frequently misused in ways that cause significant harm. Litigation over failed premium finance transactions has increased steadily, and the cases share strikingly similar fact patterns. Understanding why these transactions collapse offers important lessons for brokers and advisors who want to protect clients and themselves.

Litigation outcomes typically depend on how the transaction was explained, documented, and executed over time.

The Collapse Often Starts with an Inappropriate Loan, Not the Policy

In disputes, policy performance is often blamed first, but litigation shows that loan mechanics are usually the initial pressure point. Premium finance loans are typically short-term, commonly 5 years, while policy premium schedules extend much longer. Interest rates are usually variable. Loans are recourse obligations, frequently backed by personal guarantees.

When rates rise or loan terms mature, borrowers face repayment or refinancing decisions that were not fully anticipated. Illustrations may show loans remaining outstanding for decades, but refinancing lenders do not offer those terms. When maturity arrives, the transaction reaches a breaking point long before policy performance can matter.

The lesson for brokers is straightforward. If the loan cannot stand on its own terms, the structure is already unstable. Specialized premium finance loans are often the wrong solution.

Interest Rate Sensitivity Is Often Underestimated

Many transactions are illustrated during low-rate environments and assume minimal change over time. Litigation reveals how quickly those assumptions unravel. As rates rise, loan servicing costs increase, collateral requirements grow, and accrued interest accelerates the borrower's exposure.

In some cases, clients are told that interest can accrue without immediate impact. In practice, principal balances increase substantially each year while capitalized interest further increases the loan balance and magnifies future collateral calls. That combination makes premium finance loans particularly susceptible to interest rate increases. Borrowers may tolerate increases in early years of the plan but quickly reach a point where carrying costs exceed their comfort or capacity.

Brokers should assume that interest rates will change and should ensure clients understand how sensitive the structure is to even modest increases. Specialized premium finance loans may not be the right solution.

Collateral Calls Are the Moment of Truth

Few events drive disputes more consistently than collateral calls. Clients are often told collateral is a one-time requirement or that pledged assets remain effectively accessible. Litigation shows otherwise.

As loan balances grow and policy values lag, lenders demand additional collateral. Collateral is typically cash or marketable securities and is controlled by the lender. Clients cannot use it for other needs, even though it remains their asset. Annual, or even more frequent, collateral calls are a common feature of these loans. Since the client loses access to the funds, the client is effectively having to pay the premium even if it is nominally pledged as collateral.

Repeated collateral calls force clients to confront the true cost of maintaining the transaction. Many deals collapse at this stage, when clients refuse or are unable to post additional assets to meet collateral calls.

The broker takeaway is that collateral should never be treated as a technical detail. It is a central feature of the transaction and must be explained as such.

Policy Illustrations Create Unrealistic Expectations

Indexed universal life and variable universal life policies appear frequently in disputed transactions. These policies allow illustrations showing early cash value growth, which can make premium financing appear self-sustaining.

Litigation often exposes the gap between illustrated assumptions and actual policy behavior. Crediting rates are not guaranteed. Cost of insurance increases over time. Cash value that initially grows may later be consumed to keep the policy in force.

When policy performance underdelivers, clients feel misled, even if disclaimers were technically provided. Courts look closely at how illustrations were used, what assumptions were emphasized, and whether clients were guided to rely on projections rather than mechanics.

The Exit Strategy is Often Illusory

One of the most damaging assumptions in premium finance transactions is the belief that the loan will be repaid at death. Litigation consistently shows that death is not a viable exit strategy.

Loans mature years before death. Interest and collateral obligations accumulate during the insured's lifetime. Maintaining the structure until death would require sustained payments that many clients were never prepared to make.

When clients fall into distress long before the predicted life of the policy, either through loan maturity or collateral exhaustion rather than death, trust erodes quickly.

What Litigation Teaches About Broker Risk

From a litigation perspective, disputes often focus on how the transaction was framed rather than on the technical legality of the documents. Claims frequently involve alleged misrepresentations about risk, collateral, personal liability, and longevity. Disclosure documents do not always insulate advisors when courts find that urgency, complexity, or selective explanations undermined informed consent.

Importantly, some cases do not involve malicious intent. They involve optimistic assumptions, incomplete explanations, and reliance on materials prepared by others.

The most consistent lesson from litigation is that the structure must be grounded in reality and highly likely to work as presented. When the plan cannot or is unlikely to function and the risks are not clearly explained, exposure follows.

A More Durable Approach

Premium financing can sometimes play a role in appropriate circumstances. But durability depends on conservative assumptions, transparent communication, and alignment between the client's liquidity, risk tolerance, and the realities of the loan.

Litigation shows that transactions collapse when complexity is minimized rather than managed. Brokers who learn from these cases are better positioned to serve clients thoughtfully and to avoid becoming part of the dispute when a structure fails. ■

This material is for educational purposes only. Premium financing is a strategy that uses borrowed funds from a third-party lender to pay life insurance premiums. This approach involves significant risks, including interest rate changes, loan renewal or repayment risk, collateral requirements, and the possibility that policy performance may not meet expectations. If loan obligations are not met, additional collateral may be required, the policy may lapse, and adverse tax consequences may occur. Premium financing is complex, may not be suitable for all individuals, and there is no guarantee the strategy will achieve its intended objectives.

Guardian and its subsidiaries do not endorse or have any direct or indirect responsibility with respect to this activity. Not practicing law for Guardian or its subsidiaries or affiliates, Quantum Law Group is not an affiliate or subsidiary of the Guardian Life Insurance Company of America or Pacific Advisors.

Peyman Cohan is a Financial Representative of The Guardian Life Insurance Company of America® (Guardian), New York, NY. Pacific Advisors is not an affiliate or subsidiary of Guardian. Pacific Advisors is not registered in any state or with the U.S. Securities and Exchange Commission as a Registered Investment Advisor. Insurance products offered through One Pacific Financial & Insurance Solutions LLC, DBA of Pacific Advisors LLC. Pacific Advisors LLC is not registered in any state or with the U.S. Securities and Exchange Commission as a Registered Investment Advisor. CA Insurance License #0F47171. 8901000.1 Exp 4/28

Jonathan M. Deer is a seasoned litigator and business attorney with more than 30 years of experience guiding clients through high-stakes disputes and complex transactions. He is known for his ability to deliver practical solutions while vigorously advocating for his clients in court. He has tried cases before state and federal courts, arbitrations, and mediations, while also structuring multimillion-dollar real estate and business deals. He can be reached at Deer@QuantumLawGroup.com.

Peyman Cohan is a founding partner of Quantum Law Group and a trusted advisor to executives, professionals, and closely held businesses. For more than two decades, he has helped clients protect their assets, structure succession plans, and implement sophisticated estate and insurance strategies designed to secure long-term financial stability. He can be reached at PCohan@QuantumLawGroup.com.