Will Your Life Insurance Policy Terminate Before You?

Hi Tony,

Is your life insurance policy risk-free? There are many different types of life insurance: term life, whole life, universal life, variable life, equity indexed life, etc. **If you have any type of life insurance other than term, then the information in this lengthy newsletter is well worth your time and can mean the difference between maintaining or losing your life insurance.**

If you don't have a cash value life insurance policy, you can still sign the petition to support The Insurance Consumer Bill of Rights (click here) and wait for the next edition of the Insurance Literacy Newsletter which will take an in-depth look at what's going on with Long Term Care Insurance.

Rube Goldberg Anyone?

At it's core a cash value life insurance policy consists of three components: interest rates/dividend rates, mortality costs (cost of insurance) and expense charges.

Life insurance has grown increasingly complex over the years and has become increasingly difficult to manage. Every time a new feature is added to a policy, it adds one more variable that has to be understood, and that can have a positive or negative impact on the performance of the policy.

What's The Fuss?

Over the last ten years, interest rates have been at historic lows and are oftentimes lower than the guaranteed interest rates on universal life insurance policies. Insurance Companies traditionally have invested their funds in debt-related investments (mostly bonds). As the Insurance Companies are not earning enough interest to meet the projected interest rates on Universal Life and other cash value life insurance policies, they have had to lower the interest rates they credit to their policy owners. On some of these older policies, the guaranteed interest rate is higher than what the companies are earning. So the insurance companies are losing money on interest rates.

What happens when an insurance company is losing money? Well, they're not charities, so they look for the money in other places. Some companies have been able to make up some of the difference by changing their investment portfolio, however by regulation they are restricted to some degree in what they can invest in.

Why Am I Reading About Universal Life Policies Terminating?

Keeping in mind that almost every Universal Life Insurance policy is crediting the guaranteed minimum interest rate, then the insurance companies really only have one other component that they can change to continue to maintain profitability. And, that's the mortality costs also known as the Cost of Insurance.

A number of companies have recently announced increases in their mortality costs though they do not typically disclose what the actual change is (dollar amount or percentages). These companies include AXA Equitable, Banner Life, Security Life of Denver, Transamerica Life, Voya Life and William Penn Life. It is important to note that the companies are only raising mortality costs on some universal life policies not all of them.

It is highly likely that other life insurance companies will follow especially if they are feeling the need to do so and there are no repercussions (regulatory, media, consumer, etc.).

Universal life insurance policies were originally promoted and designed to be transparent life insurance policies where the components were unbundled and therefore could be monitored. Transparency has not been the case as changes to mortality rates are not usually disclosed and a number of companies have not advised of these changes. Changes in mortality rates can have a more significant impact on the performance of a Universal Life Policy than a reduction in interest rates.

If you have a whole life policy, you may be thinking, well, I'm safe, I'm getting my dividends. Dividends are trickier as these are opaque and companies do not provide full disclosure on their dividend scales. Companies with Whole Life policies have reduced dividend scales, however, this is usually not disclosed anywhere, you just receive lower dividends and that's all the info you have. On a whole life policy where your original projection was to pay premiums for x number of years, you'll find yourself paying premiums for much longer periods without ever being told. Most people don't even realize that their premium payment periods have been significantly extended.

Also you won't be building up the cash value that was on the original projection - so if you bought a policy using the "Missing Money concept", "Be Your Own Banker concept" or similar concept, you are almost certainly not going to end up where you expected. This is setting aside the issue of whether or not these concepts really make sense. A topic for another newsletter/article.

What's This Mean For You?

If you have a cash value life insurance policy, especially one purchased over 10 years ago, your policy has a very high chance of terminating without value. In order to avoid this unwanted outcome, higher premiums are needed on almost every older Universal Life policy (traditional universal life, variable universal life or indexed life), basically on any life insurance policy where the premiums are not fixed. And if your premium is guaranteed such as on a whole life policy, you may be paying premiums for significantly longer than expected or will be receiving a lower cash value.

So you ask, why hasn't my insurance company and/or insurance agent told me about this? Good question. The answer could be any or all of the following: the insurance companies are not facing facts, the insurance companies would prefer to not face the issue, they do not realize that the issue exists, the agent doesn't understand this and the regulatory system is not addressing it yet.

This is definitely a matter of concern as Life Insurance Companies are not detailing the impact on premiums and the life of the policy. And companies are not required to do nor are they even required to notify policyholders of increases in their costs of insurance (mortality costs).

How Do I Find Out About My Policy?

Recently, Bottom Line Personal interviewed me for a story on this topic: "Your Life Insurance Policy May Be Terminated" (click to read)

As mentioned in the interview, the only way to determine the impact of this increase in mortality costs is through an in-force illustration. An in-force illustration is a projection of future values based on current assumptions. The Insurance Literacy Institute has free "Insurance Annual Review Guides" that include a form letter to request in-force illustrations in the Resources Section (click here).

Your in-force illustration request should include a projection based on current premiums and assumptions along with a request for the required premium to continue your policy to maturity (maximum length). The difference in premium may be significant.

What Should I do?

A couple things to consider are your health & life expectancy along with your current need for life insurance. Most people find that they don't have a need for permanent life insurance as they have other assets that they accumulate and replace the need for life insurance. Remember, life insurance is for protecting those who are financially dependent upon you.

If you do need your life insurance policy, then consider if you can pay the higher premium that would be required to keep your policy in force to maturity or consider if a reduced death benefit would meet your needs.

And take a look at the ratio of premiums to death benefit. If you're paying in 10% of the death benefit each year in premiums, then the policy doesn't provide you good leverage.

Surrendering the policy is an option to consider especially if there is a sizable surrender value.

Another option is selling a policy in the secondary marketplace (life settlement), though this needs to be approached carefully and you must be fully

Big Question:

How many other companies have increased their mortality costs and how many other policies are impacted?

The most concerning news came from Transamerica who issued an announcement that illustrations requested by policyholders will no longer include information about the current Cost of Insurance Rates or Interest Rates. Yes, that's right. Policy holders with Transamerica will possibly not be able to have any idea of the premium required to fund their universal life policies. According to a recent report, Transamerica may have changed their minds on this.