

Protecting Clients With Proactive Policy Monitoring



A 12-pack of soda at the supermarket is around \$5. So a 6 pack should cost maybe \$3, or \$4 at the most, right? You'll find that to be the case. **Life insurance pricing doesn't work that way, though.**

If you reduce a \$1,000,000 guaranteed universal life in half, the premium could go up, or go to zero. We have seen both of those outcomes before. We have seen a policy run for fewer years because of paying early, or cost double going forward for paying 90 days late. As policies become more and more complex, unintended consequences occur within them.

These variations will not be so apparent on policy statements, so monitoring policies and making adjustments is more crucial than ever. Slight adjustments or catching policies before they get too out of control can make a world of difference for the policy owner. Let's discuss some common issues and ways to resolve them together.



THE FOUR CORE RISKS DRIVING POLICY PERFORMANCE

Cost of Insurance, expenses, and interest rates. These are the 3 main risks that have to be managed in an insurance policy. A properly designed policy can minimize these risks by having guarantees or being designed with an optimal death benefit-to-premium ratio. For as necessary as these 3 risks are, perhaps the most significant risk, and the one that a policy owner is most in control of, is often overlooked, and that is the funding of the policy.

Often referred to as the 4th risk in an insurance contract, the simple idea of paying your premium isn't so simple anymore, at least not in most contracts. This is not a massive risk in term contracts, because if you fail to make your payments, you'll know. The policy will terminate, or you'll get a grace notice and lapse notifications. Permanent contracts, though, are a different story. Early on, they will be as easy to manage as term policies, because with today's high minimum premium requirements, you have to make substantial contributions to permanent contracts.

After the initial minimum premium period in contracts, though, policy owners start to disregard the premiums due. Once adequate cash value is in the contracts, they miss payments, or have the policy cost on automatic premium loans. Worse yet, they start taking loans or withdrawing before originally scheduled. If structured properly, policy distributions can be tax-efficient and may not have to be repaid during an insured's lifetime. If taken in conjunction with missed payments and accrued interest, they can be catastrophic, risking losing the insurance policy altogether and creating a significant tax liability upon lapse.



AVOIDING HIDDEN TAX PITFALLS IN LIFE-INSURANCE LOANS

The IRS hasn't changed its position on the taxation of life insurance. What you've put in, minus what you took out, if that number is positive, you don't owe taxes. If you pass away, you don't owe taxes. If that number is negative, and you've taken out more than you put in, you owe taxes if that contract surrenders or if you access that money improperly.

Interest accrued on loans counts as phantom interest, so a simple set of automatic premium loans and years of non-funding can eventually be a gigantic 1099. Internal policy management techniques exist to minimize the potential for this tax problem. If a client is insurable, there may be value in a new policy, with better loan terms that can save the client from this outcome through a 1035 exchange with the loan.



WHY "GUARANTEED" POLICIES STILL NEED ACTIVE CARE

Even the most assured of contracts have variables to consider. Whole Life policies have dividends that vary from year to year. Guaranteed Universal Life has the timing of payment sensitivity and the potential to trip and lose a no-lapse rider. Tripping the guarantees of a universal life contract substantially changes the contract. This is why maintenance is required.

Slight adjustments in the short term can get a policy back on track. If there is overperformance or positive anomalies, the policy owner can have savings. A great example of this was recently in an older guaranteed universal life contract that was reviewed. The policy had a death benefit of \$1,000,000 and was fully paid, with no further premiums running guaranteed for life. The policy had \$150,000 of cash value, and the policy owner could take a \$100,000 withdrawal from the contract, and the remaining \$900,000 of coverage continued guaranteed for life. The point is that even the best policies that should never be replaced and are in great standing can be reviewed for optimization.



INTEREST-RATE SHIFTS & CARRIER CHANGES: EXTERNAL PRESSURES TO WATCH

External market conditions, most notably treasury interest rates and volatility in the equity markets, can also significantly impact life insurance contracts. Interest rates affect a policy in direct and indirect ways. Interest rate volatility directly impacts credit rates inside universal life contracts and dividend rates in whole life policies. Interest rates also impact the reserves from insurance companies, as treasuries are a big part of reserving for life insurance carriers.

The low interest rate environment of the 2010s put strain on company's profitability, which led to not only the elimination of policies offered, but also some movement of companies leaving the market entirely. While some carriers left the individual life insurance space, staying in the same company structure, others sold to private equity. Not all policyholders are affected equally by insurance companies changing ownership, but it's a genuine concern and something worth reviewing and discussing with clients.

INTEREST-RATE SHIFTS & CARRIER CHANGES: EXTERNAL PRESSURES TO WATCH (CONT'D)

Carrier financial ratings are impacted, and generally speaking, when a company no longer offers new coverage, they tend to make harsher adjustments to the existing portfolio, since there's no fear of pushback from the market affecting new sales. Some of my favorite companies, with great products, are no longer in the business now. These contracts must be reviewed and aggressively managed to ensure any unexpected contract changes are accounted for.



MARKET-LINKED POLICIES: MANAGING VARIABLE AND INDEXED UL VOLATILITY

Equity markets also have direct and indirect impacts on life insurance policies. The most apparent effect is on variable universal life contracts whose separate accounts are comprised primarily of equity or bond funds. Index universal life, promoted as a lower risk policy than variable universal life, can be that. Still, due to some of the aggressive assumptions allowed in illustrations, and the changes in how the policies credit interest, they may be as risky, or even more dangerous than variable universal life in some scenarios.

The industry has done a good job in the past 5 years regulating the illustrative assumptions and eliminating a lot of the wild scenarios, but even a routine index universal life contract may be at risk if not monitored, even one that up until this point has performed well. Like all universal life contracts, the internal expenses of a contract get higher as an insured gets older. In scenarios where a policy has outperformed expectations early, the contract has seen excess interest credited in years where insurance costs were not overly impactful.

As IUL caps become lower though, when an inforce illustration is run today, using the new regulations that restrict the assumptions of multipliers, and also require a lower interest crediting rate going forward, due to both lower cap rates and different ways in which the maximum illustrative rate can be shown, the performance of the contracts going forward can be dramatically different. It's not all bad, like the other risks and review tactics discussed.

Part of the most recent regulatory changes, some of which were retroactive, allow for significantly higher funding. The additional funding allows for both corrective additional contributions to be made for policies that are underperforming or excess funding for well-performing contracts to be even better. We won't know until we look at it and stress test it.



SIMPLE OWNERSHIP, BENEFICIARY & ASSIGNMENT REVIEWS THAT MATTER

We've discussed many issues that can arise in the life span of a policy, but some policies require little to no maintenance and have performed great, with no changes to payments or management required. A single pay 1035 into a guaranteed universal life contract, or a multi-year guaranteed annuity crediting well over the current interest rates offered, could be two examples. Maybe it's a term policy with many years remaining, and the insured has had health changes.

Even contracts like these have at least one reason to review with clients. It's a review type that I've seen open up so many new sales opportunities and helped many clients avert many potential problems, and that is doing ownership, beneficiary, and policy assignment reviews. Things change in people's lives: they have more children, leave their jobs, draft a buy/sell agreement.

As simple as it sounds, doing beneficiary checks with clients opens up insurance discussions, and while insurance companies do not pay commissions for managing policy changes like this, the act of staying on top of these non-revenue generating items for your clients is appreciated, and keeps life insurance top of mind, which may stoke interest in obtaining more coverage. It's an age-old strategy for creating same-store sales that is just not practiced enough.



POLICY SERVICE AS AN ENGINE FOR CLIENT VALUE & FIRM GROWTH

Every discussion with your clients can create an opportunity. Policy service has a 100% closing rate if the goal is to help the client. Educate them on what they have, modify their current lifestyle, lower their costs, and get more income or benefits from their insurance policy. As discussed above, there are many reasons to do this, and several resources are available.

The policies will not monitor themselves, and while some insurance companies are better than others with notifying clients and helping them through this process, the industry has a long way to go in that area, so the advisors that we see leading with this and making it a priority in their practice, happen to be the ones that end up doing the most new business and that is a philosophy that we take very seriously at Life Brokerage, and look forward to helping you implement some of the best practices we've used in your organization.



HOW LIFE BROKERAGE PROACTIVELY MONITORS AND PROTECTS CLIENT POLICIES

The average life insurance consumer buys 7 policies from 6 insurance agents. It's a transactional business. That transactional nature is on all levels of the industry as well. Insurance carriers will terminate contracts for lack of production, sometimes within as little as 18 months of not submitting more business.

At Life Brokerage, we take this area very seriously. Internally, we have multiple systems in place to monitor policies proactively. If we catch things, we notify our advisors, which sometimes generates new opportunities to improve coverage and make a new sale. Technology has also advanced, along with third-party vendors, some of which we have invested in and have available to our clients that can automate the policy service process. Protect the collective futures of your clients and grow your practice — contact LIFE Brokerage today.

lifebrokeragellc.com

2 CENTRAL AVENUE | HAMMONTON, NJ 08037
T. (609) 613-4000 | E. TEAMLIFE@LIFEBROKERAGELLC.COM

Your partner in life planning.

