

# Are You Reviewing Your Insurance Policies?

By Matthew B. Anderson, CFP®, ChFC, CLU

## Understanding your policy

Not all permanent life insurance policies are created equally. Yet, of the many different types available, all are impacted by two main components when it comes to performance: expense and investment. The expense component comprises all costs associated with servicing and issuing policies, as well as the costs associated with mortality (the pure cost of insurance). The investment component is, essentially, the performance of the insurance company's underlying investment portfolio. From year to year, both of these components may increase or decrease and, over the life of an insurance policy, these changes can have a significant impact on the policy's ultimate value to your financial plans.

Fluctuations in the expense and investment components can pose a problem for permanent insurance policies that do not offer no-lapse protection. Most of these policies are constructed and sold under the assumption that these components – based on expenses, interest rates and/or dividend rates as they stand when the policy is written – will stay the same over the life of the policy. If these assumptions aren't met, problems will occur. If expenses end up being higher and/or interest and dividends are lower, there is a possibility that the premiums paid won't be enough to support the policy.

## Time changes things

Looking back over the last 10 years, the potential ramifications of these assumptions become apparent. Interest rates are low and the stock market return, as measured by the S&P 500, an index comprised of 500 large cap domestic stocks frequently used as a measure of the U.S. stock market, has been volatile, trending negative overall. An insurance policy that based its premiums on higher interest rates or anticipated investment returns has most likely not performed the way it was expected. Policies issued 15 or 20 years ago, when interest rates were much higher than where they are today, are probably in even worse shape. Unfortunately, insurance agents aren't required to inform you when your policy is in peril. The first time most people realize this is when they receive the premium notices.

It's very important to review your policies periodically to make sure they're performing appropriately. You should request a policy illustration from your agent and review it with your financial advisor or planner. This document projects how the policy is expected to perform in the future based on contractually guaranteed and current (non-guaranteed) assumptions of expenses, interest and/or dividend rates. If the illustration shows the policy lapsing (there is no more insurance) early on a guaranteed basis, then some kind of corrective action should be discussed. This may entail increasing the premium, decreasing the face value or replacing the policy altogether. The right course of action depends on many factors including your current financial situation, your health and the role you expect insurance to play in your long-term plans.

## The bottom line

In short, problems may arise from insurance policies that rely on the performance of non-guaranteed assumptions such as older universal life policies that didn't offer a guaranteed death benefit or whole life policies where premiums are paid by policy dividends or from the cash value. As a general rule, it's good financial planning to annually review all permanent policies regardless of their structure.



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