Why Every Advisor Should Regularly Review Permanent Life Insurance Policies

Many permanent life insurance policies are placed in force and then left unmanaged for decades, which can create a major blind spot in planning and present a potential ticking time bomb. Failing to meet the original projections in the sales illustration doesn't just mean there is less cash value; it generally means there is a significant likelihood that the policy will prematurely terminate.

Unlike many financial assets that receive annual reviews, permanent life insurance policies are frequently left unmanaged despite being influenced by changing interest rates, market conditions, options pricing, carrier performance, and payment timing. The result is unmet expectations and a financial and/or estate plan that doesn't meet its objectives (e.g. creating liquidity for the federal or state estate tax, funding a special needs trust, wealth replacement, etc.). All permanent life insurance policies have non-guaranteed projections that should be monitored.

A periodic performance evaluation can identify hidden risks, uncover opportunities for improvement, and ensure the policy continues to serve the client's current goals. In many cases, a review can save a policy from lapsing, reduce premiums, improve guarantees, or provide greater value through current market alternatives.

1. Save a Policy from Prematurely Lapsing

Many permanent life insurance products were sold using hypothetical assumptions that seemed reasonable at the time but have proven difficult to achieve in reality.

Consider a hypothetical Indexed Universal Life (IUL) policy issued in 2014. The sales illustration may have projected an 8% annual crediting rate for the life of the policy. At that time, the carrier's cap rate may have supported those projections.

Fast forward to today. Those same IUL policies commonly have crediting caps that are at or near the hypothetical rate used in the original illustration. Because the cap represents the maximum amount of interest that can be credited in any given year, the policy has little opportunity to meet the original expectations. The consequence is not simply less cash value than anticipated. Without corrective action, the policy may lapse years earlier than expected, despite the policyowner continuing to pay the originally scheduled premium.

Though credited differently, the same concern can be stated with Universal Life and Whole Life policies. Decades of declining interest rates have heavily impacted performance and most clients are unaware that an underlying issue exists.

Variable Universal Life policies provide a good example of why policy reviews remain important even when investment performance has been strong. Many policies issued years ago were illustrated at aggressive hypothetical rates of return that created an expectation of future policy values and sustainability. A policy illustrated at 10% that ultimately earns an average annual return of 8% may still be significantly underperforming relative to the original projections, despite producing returns that most clients would consider excellent. ***The issue is not whether the policy performed well in absolute terms, but whether it performed well enough to meet the assumptions upon which the premium funding strategy was based.***

When policies perform substantially below expectations, the client may outlive the coverage the policy was intended to provide, ***which means all of the premium dollars (and the cash value created by those premium dollars) are gone, as is the death benefit.***

In all cases, policyowners and advisors must remember that the original illustration was based on assumptions that may or may not be realized over time.

2. Determine the Premium Needed to Carry the Policy to Maturity

Recognizing many permanent life insurance policies rely on dividend assumptions, interest crediting rates, or investment returns to achieve their intended results, it's within reason to expect underperforming policies will require additional funding to maintain coverage… but how is the policyowner to know when to increase the premium and by how much?

A common misconception among policyowners is that if they continue paying the premium shown on the original sales illustration or the annual statement, the policy will perform as expected (meaning it will pay a death benefit). And, of course, why would they not think that? Payment of the billed premium is the condition for coverage for nearly every other type of insurance. Unfortunately, that is not always the case with permanent life insurance.

A necessary and critical part of an evaluation of a permanent life insurance policy is an in-force illustration. An in-force illustration provides a current projection using the policy's actual values. This allows advisors to determine:

- Whether the current premium is sufficient
- How long coverage is projected to last based upon the current premium
- The premium required to maintain coverage to life expectancy or maturity
- Potential corrective actions available today

Identifying a funding shortfall early often provides numerous solutions. Waiting until the policy is near lapse can significantly limit available options and increase costs.

3. Potentially Reduce Premium While Maintaining Guarantees

Not every policy review uncovers a problem. Sometimes it reveals an opportunity to save money.

Consider a client who owns a traditional whole life insurance policy and whose primary objective is a guaranteed death benefit. The client may be contributing substantial annual premiums to support cash value accumulation they no longer need or desire.

In some cases, that policy can be repositioned into a Universal Life policy with a No-Lapse Guarantee, which offers:

- A premium with a contractual guarantee to remain level for a specified period of time.
- A comparable or increased guaranteed death benefit
- Contractual guarantees extending to a specific age (commonly lifetime)

- Potentially lower premium requirements
- Better alignment with the client's current objectives

A review helps determine whether the client is paying for features they still value or features they no longer need.

4. Confirm the Financial Stability of the Insurance Carrier

Life insurance promises are only as strong as the company making them. Carrier financial strength can change over time due to market conditions, investment performance, reserve requirements, acquisitions, or strategic shifts. While highly rated insurance companies generally remain financially sound, periodic monitoring is prudent, particularly for policies expected to remain in force for decades. A policy review should include an assessment of:

- Financial strength ratings
- Capital adequacy
- Lapse rate trends
- Recent rating agency actions
- Changes in product competitiveness

Understanding the current stability of the carrier helps advisors and clients maintain confidence in the long-term viability of the policy.

5. Identify Hidden Policy Inefficiencies

Many permanent life insurance policies contain inefficiencies that go unnoticed for years, including:

Term Blends Beyond Their Intended Duration

Some policies were designed with term insurance riders to reduce early premium requirements. As those term components become more expensive over time, they can create significant drag on policy performance.

Unintended Policy Loans

Policy loans can quietly accumulate interest and compound over many years. Clients may be unaware that the loans exist because they didn't directly take cash out of the policy. These loans generally come with 7-8% interest that can compound quickly behind the scenes. Clients are often unaware of the impact these loans are having on policy sustainability.

Dividend Misallocation

A dividend option selected decades ago may no longer be the most effective use of policy dividends. Redirecting dividends toward premium reduction, paid-up additions, or other policy enhancements may improve overall efficiency.

A detailed policy review can uncover these hidden issues before they become major problems.

6. Reevaluate the Client's Insurability

The life insurance marketplace has evolved dramatically over the past decade. Product design improvements, underwriting advancements, and increased carrier competition have created opportunities for many clients.

One of the most overlooked opportunities involves clients who received a less favorable underwriting classification due to their medical history when their policy was originally issued. Many health conditions are viewed differently today than they were years ago.

For example:

- Cancer survivors with favorable follow-up results may qualify for significantly improved underwriting outcomes.
- Individuals with a history of heart disease may receive more favorable consideration due to advances in treatment and long-term management.
- Improvements in overall health, weight, blood pressure, or lifestyle habits may improve insurability.
- Those who formerly used tobacco or nicotine products may be able to find significant premium reductions.
- Individuals who previously paid higher premiums due to marijuana use may qualify for more favorable underwriting today, as many carriers have adopted significantly more flexible guidelines than in the past.

Additionally, every insurance carrier has its own underwriting philosophy and underwriting manual. A client who was table rated by one carrier years ago could potentially qualify as Standard (or even better) with another carrier today depending on the circumstances.

A review of current market options can determine whether the client may obtain:

- Lower premiums and/or shorter premium durations
- Improved contractual guarantees
- Higher death benefits
- Product features that better align with current objectives (e.g. a guaranteed death benefit, long term care insurance, etc.)
- More appropriate ownership structure or beneficiary designations

The Bottom Line

Permanent life insurance should not be a "set it and forget it" asset. Clients should be encouraged to reassess their need for coverage to be sure that it still meets today's planning objectives. When the need is still present, a proper evaluation of coverage is essential every few years.

Policies are influenced by changing economic conditions, carrier performance, product design, underwriting standards, and client objectives. Regular reviews help ensure the policy continues to perform as intended and remains aligned with the client's overall financial plan.

For advisors committed to delivering comprehensive planning, reviewing permanent life insurance policies should be a standard part of the client review process.

As many policyowners discover, the cost of reviewing a policy is minimal. The cost of not reviewing it can be devastating.