Why You Need a Policy Review of Your Life Insurance

And why it should be part of your estate planning process

This article clears up many of the common misconceptions about life insurance and introduces a process for your advisor to add significant value to your financial planning by incorporating policy reviews of life insurance.

Although life insurance is a common planning vehicle for high net worth individuals and families, relatively few policies ever meet their initial projections. Industry studies reveal that life insurance portfolios rarely receive the required vigilant fiduciary oversight routinely associated with other assets such as equities, real estate, etc.

Seven Common Misconceptions - and Facts - about Life Insurance

Misconception #1: Unlike other assets, life insurance policies do not need management and regular review to avoid risk and optimize performance.
Fact: Policy performance can change dramatically over time. Without regular review by an insurance expert, policies - especially older ones - can pose very significant risk or not achieve their original goals.

Misconception #2: If the policy owner pays premiums according to the schedule in the original insurance illustration, the policy will pay at death.
Fact: Even with regular payment of premiums projected from the original policy illustration, policies can fail if not monitored properly.

Misconception #3: If the policy was in jeopardy, the carrier would notify the policy owner in advance.
Fact: Carriers will not necessarily provide advance notice of policy problems to policyholders.

Misconception #4: If one carrier has turned down an individual for insurance, it is not possible to get adequate coverage from another carrier.
Fact: The competitive nature of the insurance industry means that it is often possible to secure appropriate coverage from a highly rated carrier even if another carrier has already rejected the individual.

Misconception #5: Premiums will remain level for the life of the policy regardless of economic conditions or interest rates.
Fact: Premiums are always a reflection of the insurance carrier's cost of providing coverage, current interest rates, and other economic conditions. Any of these changing factors can cause the premium rates to change.

Misconception #6: Policies purchased many years ago are cheaper than current policies because the insured is older.
Fact: Improved mortality rates as well as better underwriting and policy features created by industry competition often produce less expensive coverage on new policies (or increased coverage for the same premium).

Misconception #7: If the policy owner no longer needs the insurance coverage provided by a policy, the only option is to surrender it to the carrier for relatively little value.
Fact: A variety of alternatives, including improved life settlement opportunities, make it possible to gain substantially greater value than that provided by cash surrender to the carrier.

Why should you be interested in the idea of a Policy Review?
Nobody likes paying premiums and very few people understand life insurance. When your advisor suggests an objective "audit" of insurance policies, he is recommending a process to determine if you

could reduce your premiums and/or improve your coverage. Policyholders do need to recognize that life insurance is an asset that must be periodically reviewed by an independent expert to avoid risk and to optimize asset performance.

Planning Tip: Your advisor's guidance can help you better understand both the risks and the greatly improved opportunities of life insurance as an essential aspect of financial and estate planning. Both the potential risk and the possible benefit are substantial.

What is a Life Insurance Policy Review?
A policy review is an objective evaluation of life insurance to ensure that the policy performs as the policyholder originally intended. A comprehensive policy review also examines options for reducing premiums or selling policies that the policy owner may no longer need because of changed circumstances, increased exemptions, etc.

Why are trust companies rushing to implement policy reviews of trust owned life insurance?
Since the late 1990's banking journals have been publishing articles on the fiduciary issues related to Trust Owned Life Insurance as institutional trust companies try to develop "best practices" to manage and monitor trust owned life insurance policies. Research indicates that over 40% of institutionally managed trust policies reviewed have serious deficiencies or problems. Many institutional trustees lack the necessary level of insurance expertise and resources for proper policy review. Trust companies may fear lawsuits for improper management of their trust owned insurance policies.

What are the results of reviewing Trust Owned Life Insurance policies?

Facts about policy reviews - there is a high likelihood that:

1. The life insurance policy represents a considerable percentage of the insured's total estate.
2. The policy has not been reviewed or managed since purchase.
3. The policy is not performing as originally projected.
4. The policy owner must pay additional (unexpected) premiums before death.
5. The insured can get more insurance coverage for the same premium (despite being older).
6. The insured can get the same insurance coverage for less premium outlay.
7. The policy owner/trustee has never reviewed the policy.
8. The agent who sold the policy is no longer in touch with the policy owner.
9. The insurance coverage is no longer appropriate for the insured.
10. The policy provisions and guarantees are obsolete.
11. The insured and the trustee do not really understand the impact of falling interest rates since policy inception.

Planning Tip: The average non-institutional trustee (for example, brother-in-law, friend, etc.) is even less well informed than is an institutional trustee - and even less likely to audit policy performance. Therefore, the insurance risk is even greater with non-institutional trustees, but they may be less apt to act upon that risk. Additionally, your life insurance policies not held in trusts almost certainly face the same level of risk as trust owned policies.

What features are important in a reliable provider of policy review service?

- Insurance expertise
- Independence
- Objective advice
- Ability to offer cost-effective solutions to policy problems

Planning Tip: Look for a turnkey service that can provide not only an expert policy review and a clear comparison of all policy solutions, but also a cost-effective, comprehensive program to implement those solutions. The program should also offer a system to manage life insurance policies and portfolios.

Conclusion

Requesting an independent policy evaluation provides you with significant value added and peace of mind about your wealth planning: it increases the likelihood that your planning will achieve its stated objectives. Consider working with an advisor who can perform an objective policy review to accomplish this much needed - and often overlooked - service.

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