

Robin & Peter on LIFE SETTLEMENTS



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Confronting Underfunded Universal Life

The current extended period of historically low interest rates has left many universal life policies in deep trouble. No one foresaw the current low interest rate environment and so universal life policies without secondary guarantees, that were funded based on prevailing interest rates at the time of purchase, are now drastically underfunded.

Further compounding the problem is that a number of insurance companies have increased cost of insurance charges to make up for the losses they are taking on having to credit policies with their interest rate guarantee.

Many producers are wary, and perhaps even a little scared, of contacting clients with this bad news. This makes matters even worse as early detection of an underfunding problem can help to minimize the damage and reduce the size of the premium increase required to maintain the policy going forward.

It's a difficult conversation to have with a client when you have to notify them that a substantial increase in premium is required to keep their policy going. The client is often faced with only unpleasant options: pay a higher premium, reduce

the face amount, or surrender or lapse the policy. In some cases, a healthy insured may be able to qualify for new, more favorable coverage. For others, however, the only affordable option might be lapse or surrender.

Older insureds, especially those with some health issues, may have a more favorable alternative than lapse or surrender – a life settlement. While having an underperforming policy is still, undoubtedly, a painful experience for both producer and client, a life settlement may partially ameliorate the situation.

If lapse or surrender is the only viable option, a life settlement can help maximize the salvage value for the policy. While a life settlement isn't a panacea for these unfortunate situations, it can certainly ease some of the pain.

Furthermore, when, as is often the case, more than one policy is involved, the proceeds of a life settlement on one policy could be used to offset the required premium increase on another. A life settlement could actually help preserve at least some of the client's insurance.

To keep the life settlement option feasible, it is essential to stay alert to these potential lapse situations. A policy that has already lapsed or is in the grace period is generally not a candidate for a life settlement.

While the outlook for in-force universal life policies without secondary guarantees is quite gloomy, a proactive producer can help to minimize their client's financial pain by addressing premium shortfalls sooner rather than later. However, if a lapse or surrender appears to be the only way forward, the possibility of a life settlement should not be overlooked.

As situations come up, be sure to give us a call. As we are often heard to say, "it can't hurt to try – it can only hurt not to!"

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