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Your life may not be worth what you think

Lower interest rates gutting current value of old insurance plans

By CLAUDE SOLNIK

Billions of dollars worth of life insurance policies may not be worth the paper they're written on.

Policies whose worth is tied to interest rates are losing value fast, as rates remain low over the long haul. And policyholders who've made the same annual payments for years are finding their policies are paying out less, expiring sooner or requiring steep premium increases to stay active.

The policies in question, known as unguaranteed universal life policies, date back to the early 1980s. For 22 years, until the insurance industry began issuing less-risky guaranteed policies in 2005, insurers issued unguaranteed policies with payouts based on higher interest rates that no longer accurately apply.

As a result, according to industry estimates, more than a third of the active unguaranteed universal policies issued between 1982 and 2004 – 38 percent – are underperforming, a casualty of relatively low rates held down by the Federal Reserve since the 2008 economic crisis.

According to St. Louis-based TOLI Center, a third-party risk-management platform for trust-owned life insurance policies, at least 1 million people still hold some $3 billion worth of the unguaranteed policies.

When they were invented in the 1980s, the unguaranteed universal policies were designed to let holders benefit from interest rates that soared as high as 15 percent. Basically, the policies were investments reaping high-interest gains.

But tying them to interest rates put the policies on a risk-and-reward footing that's stumbling now.

Because the insurance industry has remained largely mum on the effects of interest rates on unguaranteed policies, the risk goes largely unnoticed. Many policyholders are unaware that the value of their policies has dramatically declined.

HENRY MONTAG: Insurers are not always the policyholder's best friend.

"The insurance industry never bothered disclosing to the general public that there was no guarantee associated with these policies," said Uniondale-based financial adviser Henry Montag, who recommends that anyone holding an active unguaranteed policy review it immediately to "see what lower interest rates have done to their contract."

Christine Hallahan, a CPA at Floral Park-based accounting firm Wagner, Ferber, Fine & Ackerman, agreed the risks are exacerbated by the fact that many people haven't reviewed their unguaranteed universal policies in decades.

"People just let them sit," said Hallahan, chairwoman of the New York State Society of CPAs' Estate and Personal Financial Planning Committee. "The person who sold them the policy years ago hasn't got in touch to let them know the changes going on."

More policyholders are becoming aware of the problem now, but not because they're checking up on sometimes 30-year-old policies that they've poured hundreds of thousands of dollars into they're learning about the lost value because the policies are about to terminate.

Montag referenced a 91-year-old woman who's been paying $12,000 per year for 20 years for $300,000 in coverage. The policyholder recently learned her insurance is set expire in 2 1/2 years – unless she pays an additional $6,000 annually to keep the policy for another four years or another $7,500 per year for seven years.

"This is the point where people are beginning to receive letters that their insurance is geared to expire," Montag said.

That 91-year-old is not alone – many policyholders are receiving notices indicating they must increase, sometimes double, their payments for coverage to remain at existing levels.

"Often, the first time a trustee recognizes a problem is when they get a lapse notice," said E. Randolph Whitelaw, head of the TOLI Center and managing director of Trust Asset Consultants, also in St. Louis.

While insurers are required to send annual statements to policyholders describing policy values, they're not obligated to provide performance data – the kind of information that might explain the need for premium increases.

"It isn't necessarily looking out to make sure the insurance doesn't expire prematurely," Montag said. "The insurance company stands to gain."

If an insurance company doesn't ultimately pay a death benefit because a policy lapses, the premiums it collected over the policy's term are pure profit.

Some advisers have suggestions for leveling the playing field. Customers shopping for life insurance policies are routinely shown illustrations defining premiums and payouts, for instance, but updated illustrations reflecting interest-rate changes aren't typically included in annual notices.

Requiring that would be ideal, Whitelaw said.

All is not lost for unguaranteed universal policyholders. If and when interest rates rise, more value will be pumped into their policies – probably not enough to undo all the damage incurred since 2008, but enough to regain some of the low-rate losses, Montag said.

"If interest rates go up, they'd be in a better position," Montag said. "But they'd have to go up for a number of years."

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