JAMIESON
FINANCIAL SERVICES

DUE CARE BULLETIN

Comparing WL and UL: Common Questions and Answers

Life insurance due care requires an understanding of the factors that impact policy performance and drive product selection.

M Financial Group continues to lead the industry in life insurance due care and client advocacy, providing valuable insight and analysis that delivers significant value to clients.

Whole Life (WL) and Universal Life (UL) are two different types of life insurance products that provide death benefit coverage for an insureds entire life (versus a specified term). The products are different, but have many similarities. No one product is superior for all cases, with the specific case and client risk/reward tolerance driving the best product solution. In addition, there are some popular myths (i.e., misunderstandings) regarding both products. This Bulletin is designed to provide a high level overview of the similarities/differences, myths, and strengths/challenges when comparing WL and UL. A more detailed M Due Care Bulletin, which covers product mechanics and provides illustration competitive comparison examples, is also available.

What are the Similarities Between WL and UL?

- The underlying building blocks that drive performance for WL and UL are the same (mortality, investment, expense, and persistency).
- Both WL and UL provide non-guaranteed product performance based on current experience for the building blocks.
- Current performance for both WL and UL is not guaranteed and may change (better or worse) as emerging experience deviates from past experience.
- Both WL and UL provide some downside risk protection as product loads may not exceed guaranteed loads and interest credited may not be lower than the guaranteed minimum interest rate.

What are the Differences Between WL and UL?

- The policy contract and mechanics are different for WL and UL.
  - WL starts with guaranteed assumptions: The cost (i.e., premium) for lifetime coverage in WL is guaranteed, but may be reduced if non-guaranteed dividends (based on emerging experience that is better than the guaranteed assumptions) are credited.
  - UL starts with current assumptions for interest credited and policy loads: UL performance is based on non-guaranteed current assumptions that reflect current experience. The actual performance over time may be better or worse than originally illustrated due to changing emerging experience that drives current assumption changes. However, performance is guaranteed to be no worse than the guaranteed assumptions.
- UL product mechanics are transparent, while WL product mechanics are "black box." Unlike WL, the charges and credits for UL are explicitly defined.
- Premium Funding:
  - WL requires funding levels that endow the policy by age 120.
  - UL has virtually unlimited funding flexibility (subject to DOLI and MEC testing), including endowment funding like WL and funding at less than endowment (such as $1 of cash value at age 120).

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What are the Differences Between WL and UL? cont.

¤ Coverage:

- WL will not allow the contract to lapse if dividends decrease or premiums are not paid. Either additional premiums are required or the death benefit is reduced in order to maintain coverage for life.
- The coverage period for UL is flexible. Additional premiums or reduced coverage are not required to keep the policy inforce. The policy simply lapses when the account value goes to zero.

What are some Myths?

¤ WL has superior risk protection compared to UL: WL may appear to have better downside risk protection due to the required higher funding levels. However, because UL has funding flexibility, many UL policies are funded at a lower level than WL, and therefore may have less cushion for downside assumption changes. Downside performance risk (i.e., additional premiums to maintain coverage) is similar between UL and WL when UL is funded at the more conservative WL level. In addition, UL provides more flexibility in managing downside performance through flexible premiums and coverage, while WL requires either additional premiums or reduced coverage.

¤ The WL dividend interest rate is the actual crediting rate: WL will disclose a dividend interest rate (DIR), but it is usually not the actual interest rate credited to the policy. A dividend interest rate will be based on interest earnings, but the DIR is typically also based on expense, mortality, and persistency experience. As an example, it is possible that even if interest earnings are reduced, that offsetting better mortality experience will maintain the dividend interest rate. How the dividend interest rate relates to the actual dividends credited to the policy is "black box." Therefore, comparing DIRs between WL products, or comparing a DIR with a crediting rate from a UL product, is not appropriate for assessing actual policy competitiveness.

¤ WL premiums are inflexible: This is not true with participating dividends, and even more so with term blending. However, premium levels are still required to endow the policy by age 120.

What are the Strengths and Challenges of UL?

Strengths

¤ **Transparent mechanics which allow the policyholder to better understand and evaluate/audit policy performance.**

¤ **Competitive performance as compared to WL when matching funding target and commissions.**

¤ **The option to reduce the premium cost by targeting lower than endowment funding levels, such as $1 of cash value at age 120.**

¤ **Virtually unlimited flexibility with premium payments (subject to DOLI and MEC testing).**

¤ **Flexibility in death benefit coverage. As an example, an insured may be comfortable with the risk of funding coverage to age 100 as that is past his/her life expectancy. Or a policyholder may be low on funds, and choose to stop scheduled premium payments and let the existing coverage run for as long as possible (coverage ceases when the account value goes to zero), taking the risk that he/she outlives the coverage.**

¤ **Downside risk protection that is similar or better than WL when funding at similar levels.**

Challenges

¤ **Premium and coverage flexibility can provide situations of misunderstood policyholder risk, such as lapse, due to low funding and worse policy assumptions (loads and/or interest credit).**

¤ **Lower safeguards to keep the policy inforce, as there is no requirement for additional premiums or reduced face amount when funding falls behind or assumptions are worsened.**

Comparing WL and UL: Common Questions and Answers (continued)

What are the Strengths and Challenges of WL?

Strengths

- **Whole Life is particularly competitive for heavier funding and cash accumulation.**
- **Dividends and term blending provide competitive non-guaranteed performance similar to UL when compared on a level playing field (i.e., same solve target and matching commissions).**
- **Dividends and term blending can provide some premium funding flexibility.**
- **WL requires higher funding levels, which may provide better downside risk protection as compared to UL when funded at lower levels. However, UL risk protection is similar to WL if UL is funded at the same level as WL.**
- **WL provides stronger safeguards than UL to automatically keep a policy inforce, such as required additional premiums or reduced coverage.**
- **The increasing death benefit from PUAs may be a good match for policyholders who have an increasing death benefit need.**

Challenges

- **The policy loads and credits for WL are not transparent to the policyholder. The "black box" nature of the policy mechanics makes it difficult for a policyholder to understand, evaluate, and audit actual performance.**
- **Higher required funding levels that always endow the policy. As an example, unlike UL, there is no flexibility with WL to lower the premium cost by targeting a lower funding level such as $1 of cash value at age 120.**
- **Less flexibility with actual premium funding. If premiums are not paid according to schedule, then additional premiums will be required or the face amount will be reduced.**
- **Less flexibility with death benefit coverage. WL does not allow the policy to lapse. This can be considered negative when either the policyholder does not have the cash to pay premiums and/or wants to maintain the full death benefit for as long as possible. Note that WL may provide the option for Reduced Paid Up and/or Extended Term.**
- **Term blending may be more susceptible (i.e., more leverage) to relatively worse performance than UL when assumptions are worsened.**

For More Information

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