Crossing The Great Divide

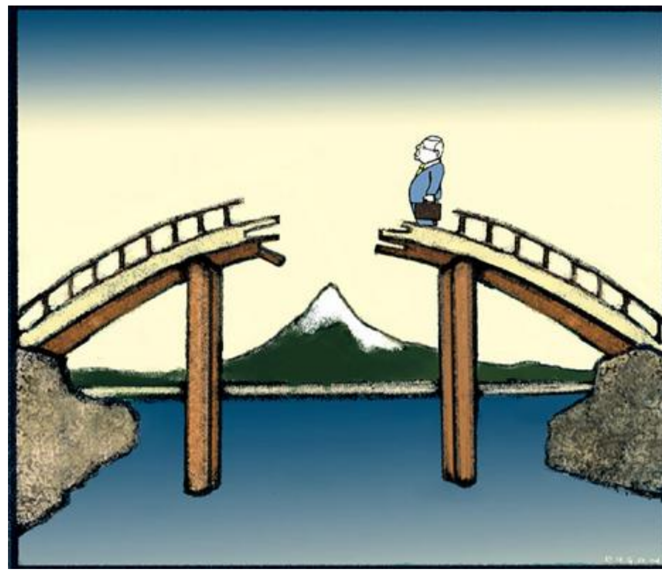
The untold history of life insurance underperformance
By T. Mark Pace

OBJECTIVIEW
The Life Insurance Performance Management System™
Life Insurance At Its Very Best

Everything changed in 1979

For 240 years prior to 1979, the Life Insurance Industry had successfully sold one type of permanent coverage known as whole life. Whole life policies were simple; the premium and death benefit were guaranteed and if you paid the premium, you got the death benefit… no matter when you died. The only thing that could potentially cause a whole life policy to fail, other than neglecting to pay the premiums, was misusing the right to borrow from the policy.

Up until 1979, permanent life insurance, in the form of whole life policies, was a buy and hold asset.



In 1979, the carriers crossed **The Great Divide** with the introduction of a new type of policy called **Universal Life** (UL) signaled the beginning of a new era for life insurance. The concept of pay a premium, receive a death benefit, was quietly replaced. You no longer had to pay the same premium year in and year out, you could adjust your premium to meet your changing needs and financial situation.

In exchange for this flexibility, the decision of what the premium should be, and the responsibility to ensure life insurance policies were funded adequately, was transferred to policy owners and their advisors.

In 1979, the carriers crossed **The Great Divide** as they went from selling guaranteed products exclusively to selling products that could fail due to an ever growing number of circumstances. Ever since then, the industry has experienced an accelerating evolution and expansion of product types.

What were the companies up to? Like all rational businesses, they were in pursuit of profit. They realized that because interest rates were so high, UL policies were able to show a much lower premium while promising the same death benefit as traditional whole life. With this competitive advantage, a vast flow of new policy purchases went from established Whole Life carriers to the upstart providers of UL.

Unfortunately, life insurance owners did not cross The Great Divide along with the insurance companies. They weren't invited. They didn't know then that The Great Divide existed. And, they still do not know it exists today. Instead, life insurance owners and their advisors have blithely remained on the old Buy and Hold side. They continue to believe that paying the premiums called for in the illustration used to sell the policy, guarantees they will receive the death benefit when it was needed most.

The Great Divide becomes The Greater Divide

Starting in 1981 interest rates dropped precipitously and, in a response driven by the need to protect or increase profits, the industry created **Variable Universal Life products (VUL)**. VUL enabled them to once again illustrate high interest potential – with the resulting benefits of

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lower premiums for the same death benefit. Needless to say, a large amount of new policy purchases began to flow in this direction. In response, traditional whole life carriers took steps to staunch the flow of premiums to carriers offering UL by adding a vast selection of "riders" that enabled their products to mimic UL. And in doing so, they crossed The Great Divide.

The stock market tanked in the 90's taking with it the performance of VUL products. In response, sometime around the year 2000, the industry began offering **Guaranteed Universal Life** (GUL) products. The guaranteed premium provisions of this *new and improved* product in some ways mimicked whole life and, in doing so, further obscured the fact these carriers had crossed The Great Divide without the owners and would-be purchasers of life insurance.

Today, with interest rates at historic lows, we are now being offered **Index Universal Life** (IUL) and are being tempted with another great story about how high crediting rates and bottom end caps means the premiums you pay result in a larger death benefit or greater cash value.

And now, a word from our sponsors

At this point it wouldn't be unreasonable for you to sense that we do not like life insurance. Rest assured, nothing could be further from the truth. **We believe that when there is an acknowledged need and desire for cash when someone dies, life insurance is the best asset anyone can own.** We are staunchly product agnostic and believe every type of life insurance has a purpose.

As champions of rational decision making, we find it extremely unfortunate that life insurance is all too often sold and managed as if it were a simple commodity, one you can buy and hold; simply pay the premiums and receive the death benefit. In reality, because of the accelerating evolution and proliferation of product types since 1979, life insurance has become an increasingly complex asset.

The good news is that each policy comes with a unique set of powerful, flexible and highly beneficial performance management rights. And, when these rights are understood and taken advantage of, when you treat it as a buy and manage asset, life insurance is the best asset you can own for the immediate creation and transfer of wealth when it is needed most.

In 1979, life insurance became a *Buy and Manage* asset

The Great Divide is now almost 35 years old and most policies sold since 1979 fall into an asset category best described as ***buy and manage***. The only remaining form of life insurance that is truly buy and hold, are the whole life products that have not been borrowed against, have not been blended with term, and do not have any of the many riders popular attached to them.

When the insurance companies crossed the great divide, they didn't take the agents with them. Agents were left on the old, whole life side and were only trained to sell product features and benefits and to perform policy maintenance… no word of life insurance

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performance management was spoken.

The other major phenomenon that has occurred during this entire period is one that takes advantage of the pervasive myth that life insurance is a commodity and ownership is a simple matter of paying premiums and receiving a death benefit. While this was more or less true in the earliest days, in the face of increasing complexity, this **Myth of Simplicity** fosters two significant dangers: underperformance and unnecessary replacement.

Underperformance occurs when owners and advisors believe they are dealing with buy and hold assets and subsequently ignore or underutilize the Performance Management Rights within a policy or portfolio of policies. As a result, more than 90% of all policies underperform and almost 50% are at risk of failing and may die before the insured.

Treating life insurance as a simple commodity also creates an ideal environment for **unnecessary replacement** of existing policies. The argument agents make is simple; since life insurance is a commodity and one policy is much the same as another, doesn't it just make sense to replace old, seemingly expensive and poor performing policies with something new? While review and replace practitioners are recommending replacement 90% of the time, looking past *The Myth of Simplicity* reveals replacement is only necessary 25% of the time. This means most existing policies outperform new ones ***if they are properly managed***.

Building a bridge

To this day, the industry uses the same illustration system it always has, even before it crossed The Great Divide. Which is one reason why agents and insurance owners did not make the journey along side them.

However, if you **realize that most policies have performance management rights**, and if these rights are exercised throughout the life of the policy, you can cross The Great Divide, optimize the performance of your life insurance, and make sure you get the best returns possible for all money invested.

(NOTE: You need to know which side of The Great Divide you are on. If you own anything other than a whole life policy that has never been borrowed against and hasn't blended with term or has any of the many riders popular in the past several decades, you are on the buy and manage side.)

Dual Probability Analysis

The best way to start building a bridge across The Great Divide is to compare the probability of policy failure to the probability of when the insured will die. Basic logic says if the policy lives

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beyond the insured, a death benefit will be paid and some of the money invested in the policy will have been put to good use. Which is better than what happen when the insured outlives the policy: in these all too frequent cases, all of the money invested is wasted.

While one of these outcomes is merely satisfactory, and the other intolerable, the good news is that most existing policies, if they are put under the management of knowledgeable professionals early enough (the sooner the better), are able to become stellar performing assets when compared to other safe types of investments.

The bad news is that most life insurance owners and their advisors put off taking action until too much harm has been done. The deterioration of a life insurance policy does not occur in a steady, incremental fashion. The longer you wait, the worse it gets as the penalties grow in a geometric fashion.

But, there is more good news: doing a little today saves a lot tomorrow. The sooner you act, the better your life insurance will perform.

The LIPM™ Snapshot

If you want to do a little today to save a lot tomorrow – not to mention avoid complete failure – consider the LIPM™ Snapshot. This is the starting point for the solutions I offer to all the issues presented in this article. There are other solutions from other advisors available. Regardless of which you choose, the challenges are the same.

Start any conversation about life insurance by assessing which side of The Great Divide you are on. The chances are, the life insurance you own is something other than pure and simple, no rider, whole life that has not been borrowed against. What you likely own is a buy and manage asset. **If this is the case, you need to cross over to the management side of The Great Divide and start practicing some form of life insurance performance management.**

About T. Mark Pace, CLU, ChFC, RHU

Creator of ObjectiView: The Life Insurance Performance Management System™, Level 5 Underwriting™ and The LifeSpan Advantage™, Mark has over 35 years of experience in the life insurance industry and intimate knowledge of the design, manufacture, and distribution of its products. Over the course of his career, Mark has assisted in the rehabilitation, acquisition and on-going optimization of billions of dollars of life insurance.

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