

**Steve Leimberg's Estate Planning
Email Newsletter Archive Message #2547**

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**Subject: Barry Flagg: 6 Essential Ingredients to Life Insurance
ADVICE**

“Life insurance is an essential planning tool for many financial and estate planning professionals. Its unique tax preferences, risk management characteristics, and asset protection qualities often make it an ideal tool for asset protection and/or income tax planning, estate planning and/or estate tax financing, and funding buy-sell agreements and/or supplemental retirement plans. However, life insurance remains the last, largest, most-neglected asset in the planners’ planning and on clients’ balances sheets. As is often the case, neglect breeds poor-performance, and life insurance is no exception, having been among the worst-performing asset-types relative to clients’ expectations for decades, and now the source of growing complaints, arbitration and litigation against advisors, brokers and insurers. The good news is the life insurance industry is being transformed by the same mega-forces that transformed the investment business over the past four decades, bringing with it the promise of greater transparency, lower costs, and better performance. Understanding these transformative forces will help financial and estate planning professionals better advise clients about the prudent selection/retention and proper management of life insurance holdings.”

In his commentary, **Barry Flagg** discusses the 3 mega-forces that transformed the investment business, how these same 3 mega-forces are transforming the life insurance business, and how to use new Best Practice Standards to 1) define roles and responsibilities of the life insurance professional in a manner that ensures client’s best interests are served, 2) analyze client’s circumstances, goals and objectives in a way that more naturally leads to prudent product selection or retention, 3) strategize defining characteristics of product types most aligned with client’s interests, 4) formalize the search criteria for best-available rates and terms (BART) that considers inherent constraints and conflicts of interest, 5) implement best-available rates and terms (BART) while avoiding prevailing life

insurance industry practices now considered “misleading”, “fundamentally inappropriate”, and unreliable by financial, insurance, and banking industry authorities, and 6) monitor the factors affecting performance to reduce the risk of client disappointment and ensure client’s interests are served over time.

Barry Flagg, CFP®, CLU, ChFC, GFS® is inventor and founder of Veralytic® - a leading publisher of pricing and performance research and ratings for life insurance products. Veralytic is the invention of his unique background as both the youngest Certified Financial Planner (CFP®) in history schooled in the fiduciary investment business, as well as life insurance practitioner consistently ranked in the top 1% of the industry. He’s a recognized expert in applying Prudent Investor principles to life insurance product selection and portfolio management serving as subadvisor to thousands of life insurance trusts. Barry has written articles for numerous national publications and has delivered continuing education to attorneys, CFP®, CPAs, and CTFAs on the management of life insurance as an asset according to established and proven asset management principles.

Here is his commentary:

EXECUTIVE SUMMARY:

Life insurance is among the last asset types to be brought under the wealth management process. For this reason, it is often the most-neglected asset in the planning of the estate and financial planner and on clients’ balances sheets. As with most other things, neglect breeds poor performance. It, therefore, comes as no surprise that life insurance has been among the worst-performing asset types relative to clients' expectations for decades.

This is not to say that life insurance has performed poorly relative to performance benchmarks for the asset-classes of invested assets underlying policy cash values. To the contrary, the performance of invested assets underlying policy cash values are quite consistent with the performance of other like-asset-class investments found outside life insurance. As such, disappointment has more to do with overly-optimistic expectations than actual under-performance.

This is because the life insurance industry's operating principles were never designed to deliver on expected performance. Instead, the industry's operating system (O/S) was designed to build and sell new products, as evidenced by the primary “output option” being illustrations of hypothetical policy values, and prevailing sales practices to compare such sales proposals for a new product to illustrations for an inforce policy as supposed due diligence and decision support.

As we will see, such illustration comparisons too often involve presenting new products using overly-optimistic assumptions in comparison to an inforce illustration too often reflecting less than realistic assumptions. For instance, in the 1980s, universal life (UL) products were generally illustrated to offer rates of return assumed to be superior to whole life (WL) products, even though both products are required by regulation to invest predominantly in the same asset classes, and thus will generally perform similarly over time.

In the 1990s, variable life (VL) products were again too often illustrated using overly-optimistic rates of return in comparison to UL products that by then were being illustrated to reflect reduced rates of return that were unrealistically even lower than historical rates of return for the corresponding asset classes into which they are required to invest. In both cases, such illustration comparisons for the “flavor of the day” product failed to examine internal costs, obfuscated excessive charging with overly-optimistic performance assumptions, and consistently produced disappointing results.

As such, disappointing performance has less to do with actual performance of life insurance products relative to other like-asset-classes, and more to do with over-reliance on a product-centric operating system (O/S) designed to build and present products that appear attractive in the environment at the point of sale, but which fail to incorporate established asset management principles proven effective over time. The West Point Draft of Best Practices Standards will be discussed hereafter as a more client-centric alternative for the prudent selection/retention and proper management of life insurance as an asset.

FACTS:

Out-Dated Operating System (O/S) – A Case Study

In re: Cochran v. KeyBank shows how the product-centric life insurance industry O/S proved effective for selling new “flavor of the day” products but produced disappointing results. For more detail, see LISI Newsletters #1486 and #1499 published 29-Jun-09 and 05-Aug-09, respectively. As such, this case offers insights for estate and financial planners, life insurance fiduciaries, and life insurance advisors who wish to distinguish their practice as client-centric and advice-oriented.

For instance, when interest rates were at lifetime highs in the 1980s, the life insurance industry developed a new product called universal life (UL) specifically designed to appear attractive in periods of high interest rates. Accordingly, Stuart Cochran created an irrevocable life insurance trust (ILIT) in the mid-1980s to own \$4.75M of UL and similar products where cash values are required by regulation as a practical matter to be invested predominantly in conservative asset classes like high-grade corporate bonds and government-backed mortgages.

Some years later, as prevailing interest rates declined, and the Dot-Com boom of the 1990s drove the stock market to all-time highs, the life insurance industry developed another new product called variable universal life (VUL) designed to appear attractive when client confidence in the stock market is high. With Cochran’s UL policy under-performing original (albeit unrealistic) expectations, Cochran’s agent recommended replacing the original \$4.75M policies with an \$8M VUL policy using comparisons of hypothetical illustrations showing a \$3M+ increase in death benefits “for no additional cost” and allocated cash values predominantly to aggressive asset classes.

With the stock market crash in the early 2000s, the life insurance industry developed another new product called guaranteed universal life (GUL) designed to appear attractive in periods of financial uncertainty. Accordingly, Cochran’s VUL cash values declined by \$37,000 – a 7% unrealized loss. Even though a 7% loss is well within the expected range of returns for an aggressive asset allocation, Cochran’s life insurance agent nonetheless recommended replacing the \$8M VUL with a \$2.5M GUL policy in response to this “unexpected” loss, and again compared

illustrations of hypothetical policy performance as decision-support for this recommendation.

Ironically, the VUL-to-GUL exchange was “recommended” to protect trust assets from further stock market declines, but actually incurred a 20% realized loss due to a \$107,000 surrender charge. Had the VUL policy been maintained, the 7% unrealized loss would have rebounded since the stock market recovered as it always does. Alternatively, if an aggressive asset allocation was no longer consistent with the appropriate risk profile (if it ever actually was), then market risk could have been eliminated by simply reallocating cash values to the policy’s fixed account. Neither option was considered due to life insurance industry O/S over-reliance on illustration comparisons.

Seven months after this 3rd exchange in just 16 years, Mr. Cochran died and beneficiaries received \$5.5M less than expected, and \$3M+ less than originally intended. While each of these products offer features and benefits useful in certain client circumstances and planning situations, the Cochran case exemplifies the problems that can arise when financial and estate planning professionals look for advice on the prudent selection/retention and proper management of life insurance from an industry whose operating principles are not designed to advise, and instead are designed to build and sell “flavor of the day” products.

Indeed, Cochran v. KeyBank shows both how illustration comparisons can be an effective sales tool but also how such illustration comparisons fail to disclose costs and/or reflect reasonable investment performance relative to acceptable risk (e.g., as shown by the UL-to-VUL exchange). For these reasons, comparisons of illustrations of hypothetical policy values are now considered “misleading”, “fundamentally inappropriate”, and unreliable by financial, insurance and banking industry authorities. In other words, the information essential to advice — such as cost disclosures and historical performance — is not even an “output option” from the life-insurance-industry O/S.

Imagine trying to advise anyone about anything with out knowing what is actually being charged and what is reasonable to expect in performance, and where decision-support is based on “misleading”, “fundamentally inappropriate”, and unreliable information. It’s, therefore, no surprise that life insurance has been among the worst-performing asset types relative to

clients' expectations, and that financial and estate planners have struggled to understand how life insurance fits into their financial and estate plans and/or resisted considering life insurance as a planning tool altogether.

Prudent Investor Operating System (O/S) for Life Insurance

On the other hand, the advice industry has its own “operating system”, which I call the Prudent Investor operating system. Advice differs from product sales in that advice follows an established decision-making framework that’s been tested in the courts and proven reliable over almost 200 years. Examples of a Prudent Investor O/S include ERISA for retirement plans, the Uniform Prudent Investor Act (UPIA) for private trusts (to include life insurance trusts), and fiduciary standards for investment advisors, trustees and investment committee members.

The Prudent Investor O/S was also recently “expanded” to address life insurance in the West Point Draft of Best Practice Standards for Life Insurance Stewardship using the same universal decision-making framework already widely-accepted in the investment business. As such, financial and estate planners and life insurance fiduciaries now have a familiar decision-making framework to also understand how life insurance fits into their planning and what to reasonably expect.

The evolution from the outmoded life insurance industry O/S to the Prudent Investor O/S is being fueled by the same mega-forces that transformed the investment business decades ago, namely the advent of new standards of care, the invention of new tools and services to support new duties, and enforcement by regulators and litigators. The result was greater transparency, lower costs, and better performance.

Some readers will remember when the investment business used to look a lot like the life insurance business of today, when investments were sold by “financial advisors” based on hypothetical projections (e.g., tax shelters) instead of empirical research for costs and performance, when “advice” was generally bundled with and incidental to a sale of some product and often non-existent after the sale, and when “Investment Contracts” paid up-front commissions on the placement of some product (as much as 50% and more in some cases) rather than fees for advice, management, and results over time.

The evolution of the investment business we know today began with ERISA providing a set of rules (i.e., the new operating system) for a substantial portion of the industry (i.e., Qualified Retirement Plans). While ERISA didn't apply to the entire investment industry, these new rules made enough sense and applied to enough of the industry that this new O/S spread to much of the rest of the investment business. These new rules included 1) the duty to monitor, 2) the duty to investigate suitability, and 3) the duty to manage as a "Prudent Man" would to minimize costs and maximize benefits relative to acceptable levels of risk.

In the years following ERISA, third-party administrations (TPAs) developed record-keeping systems to support this duty to monitor, and research providers began publishing pricing and performance data to support the duty to investigate. Such ready access to information about current holdings and their prudence relative to peer-group products also lead regulators and litigators to enforce this standard-of-care.

For instance, whereas there was comparatively little litigation in the investment business before ERISA, Qualified Plan Trustees were the popular target of litigation involving breach of the duties prescribed by ERISA in the late 1980s and early 1990s. As such, ERISA set into motion three mega-forces:

- 1) Third-Party Administrators (TPAs) providing information about current holdings,
- 2) Research services publishing suitability information relative to peer-group products, and
- 3) Regulators and litigators using #1 and #2 to enforce the rules prescribed by ERISA.

The combined effect of these mega-forces transformed the investment industry from a product-centered, "manufacturers'-rep" business into a client-centered, advice-oriented business in which more and different types of advisors entered the investment advisory business. At this same time, the Baby Boom Generation was moving into its peak earnings and savings years, substantially increasing the demand for investment products, management and advice.

Just as ERISA provided an O/S for a substantial portion of the investment industry, the Uniform Prudent Investor Act (UPIA) similarly provides a set of rules (i.e., operating system) for a substantial portion of the life insurance business, namely Irrevocable Life Insurance Trusts (ILITs). These rules under UPIA have been adopted by 40+ States/Territories and similarly include 1) the duty to monitor, 2) the duty to investigate suitability, and 3) the duty to manage as a “Prudent Man” would to minimize costs and maximize benefits relative to acceptable levels of risk.

In a repeat of events following ERISA, third-party administrations (TPAs) arrived on the scene roughly coincident with the adoption of UPIA beginning in 1994 (e.g., TrustBuilder in 1992, Resource Insurance Consultants in 2000, and ITM-21st originally founded as Advicon in 2003). Then, again in parallel fashion, life insurance product research became available some years after the arrival of TPAs (e.g., Veralytic originally founded as THEInsuranceAdvsnr.COM was granted the first of its patents in 2002 and made pricing and performance research and product ratings available online in 2003).

Lastly, reminiscent again of the evolution in the investment business, regulations now consider prevailing practices under the life insurance industry O/S to be “misleading”, “fundamentally inappropriate”, and unreliable, and litigation against both irrevocable life insurance trust (ILIT) trustees (e.g., Cochran v. KeyBank and French v. Wachovia) and life insurance advisors (e.g., Vagelos v. Merrill Lynch and Nacchio v. AYCO/Goldman Sachs) are beginning to enforce the rules under UPIA.

In other words, UPIA similarly set into motion the same transformational mega-forces on the life insurance business where:

- 1) Third-Party Administrators (TPAs) provide information about current holdings,
- 2) Research services publish suitability information relative to peer-group products, and
- 3) Regulators and litigators use #1 and #2 to enforce the rules prescribed by UPIA.

The combined effect of these mega-forces is driving an evolution of the life insurance business from a product-centered “manufacturers’-rep” business once the exclusive domain of agents and brokers, into a more

client-focused advisory-business where fee-based advisors and consultants are playing an increasing larger role. In response, the Financial Planning Association (FPA), recognizing the need for a universal decision-making framework for the prudent selection/retention and proper management of life insurance like that already widely-accepted in the investment business, lead in the formation of a task force that convened at West Point in 2013.

The task force was comprised of leaders from nearly every profession who have clients who own life insurance, to include representatives from one of the largest trusts and estates law practices, the largest administrator of trust-owned life insurance for institutional trustees, the largest association of financial planners, a leading university in financial planning education, several of the largest independent life insurance distributors, and several fee-based advisory firms. The result is the West Point Draft of Best Practice Standards for Life Insurance Stewardship.

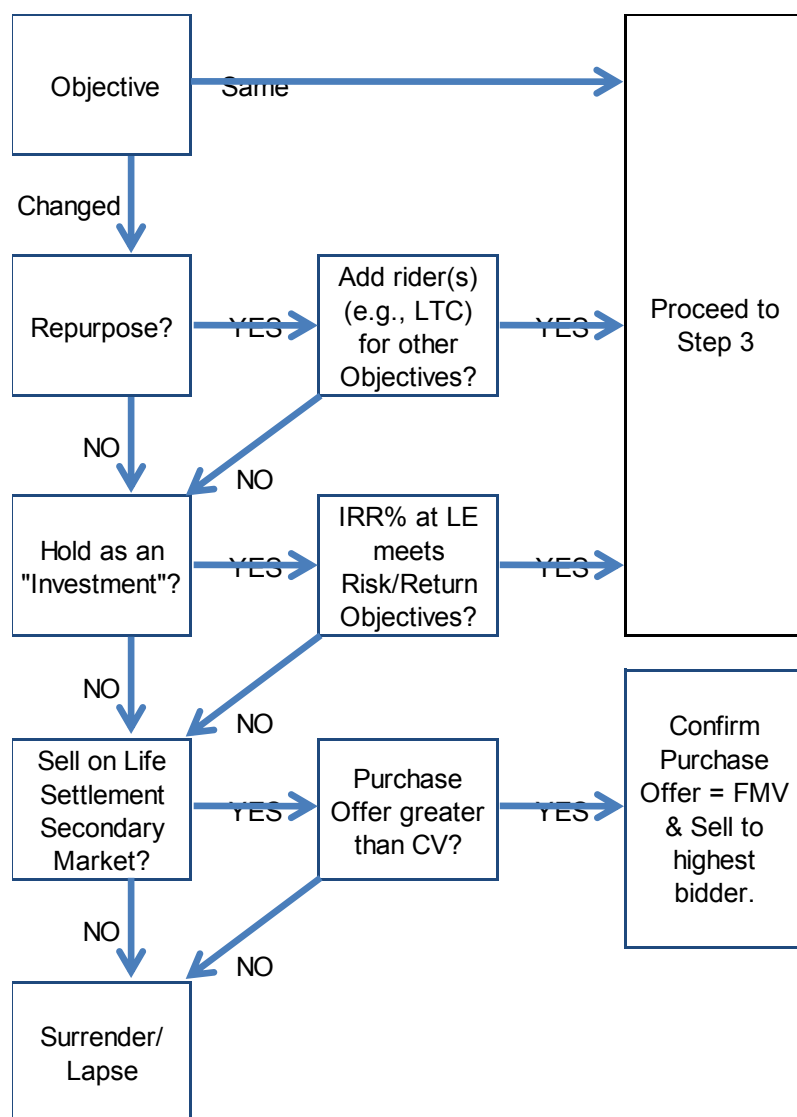
The elements of such a Prudent Investor O/S generally include 1) defining roles and responsibilities for members of the planning team, 2) analyzing goals and objectives, 3) strategizing the most prudent solutions sets (i.e. product types), 4) formalizing the search criteria for the product within the optimal solution set, 5) searching for and implementing the vehicle(s) offering best-available rates and terms (BART), and 6) monitoring performance relative to both original expectations and peer-group alternatives. The West Point Draft of Best Practice Standards is comprised of the same 6 steps, as follows.

Step 1 - Define: Just as the investment advisor is a member of the planning team, life insurance advisors distinguish themselves as advisors by first discussing their role and responsibilities on the planning team. Too often, conversations about life insurance start with hypothetical illustrations for some product or products. Instead, starting the conversation by defining roles and responsibilities in the planning process distinguishes the life insurance advisor from life insurance sales people, leads to better working relationships between the banker, CPA, attorney, trust officer, etc. members of the planning team, and ensures client's best interests are served.

Step 2 - Analyze: In the same way that investments for clients seeking income will be different from the investments for clients seeking growth,

different life insurance products are also designed for different risk profiles, asset allocations, time horizons, and expected outcomes. In addition, some life insurance products are designed for defined contributions and maximum accumulation, whereas others are designed to minimize premiums for a defined death benefit, and some are designed for both. As such, advising clients about the prudent selection/retention and proper management of life insurance requires an analysis and understanding of their circumstances, goals and objectives.

See below flowchart of an example decision tree for analyzing existing life insurance holdings in response to changing planning objectives.



Step 3 - Strategize: The rate of return reasonable to expect from any financial strategy is most influenced by its underlying asset allocation. Different life insurance product types are thus most significantly differentiated by their investments underlying policy cash values. For instance, most universal life (UL) and whole life (WL) products are required by regulation as a practical matter to invest assets underlying policy cash values predominantly in high-grade bonds and government-backed mortgages whereas variable products (VL) allow for allocation across various asset classes.

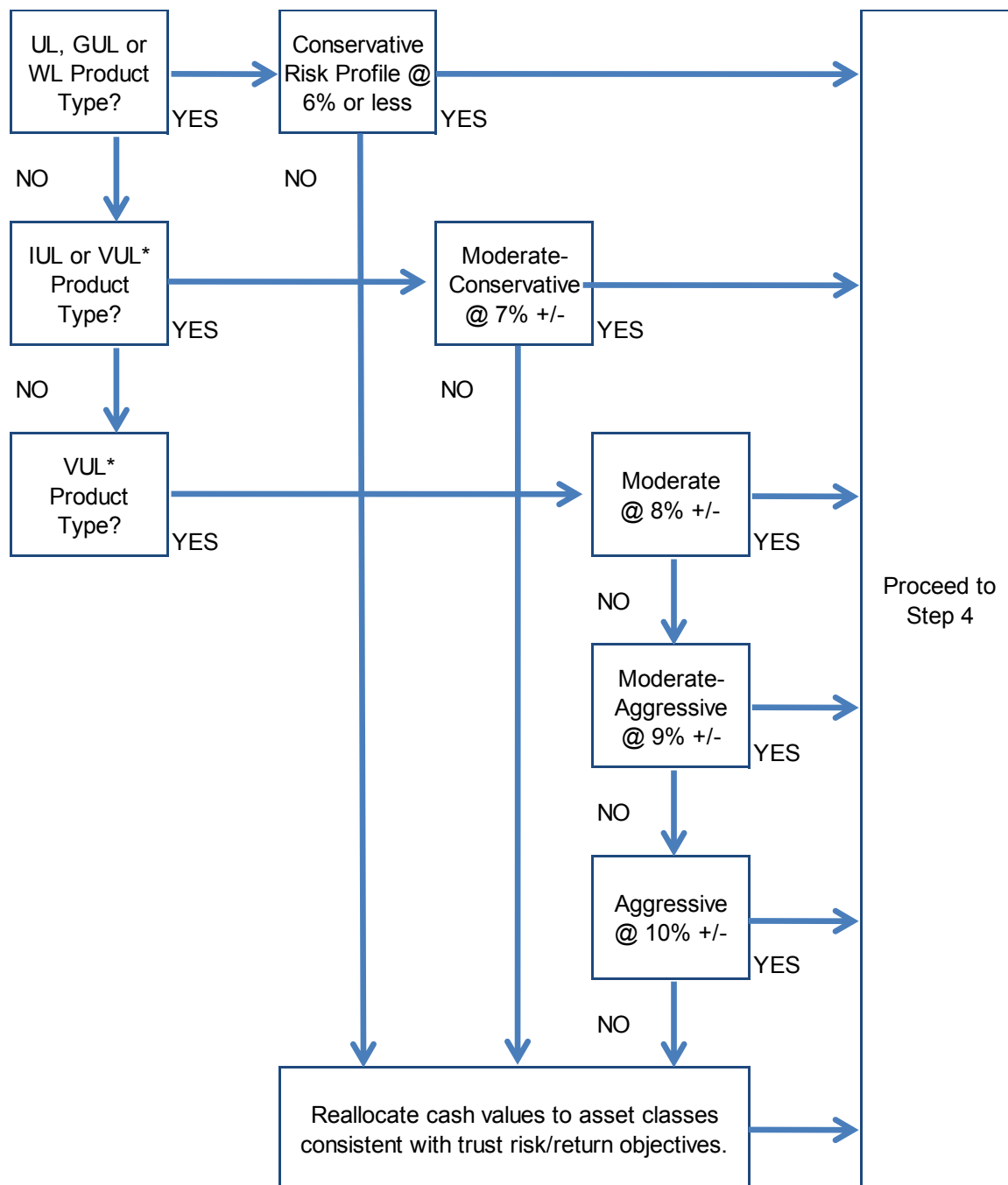
As such, the most prudent product type for a given client situation is a function of the **R**isk tolerances of the client, the corresponding **A**sset class preferences, the **T**ime horizon and the **E**xpected outcomes (remember R.A.T.E.), as follows:

Risk Profile	Asset Allocation (Equities/Fixed-Income)	Product Type	Rates of Return Reasonable to Expect
Conservative	20% / 80%	UL/GUL/WL	5% - 6%
Moderate-Conservative	40% / 60%	IUL/VUL	6% - 7%
Moderate	60% / 40%	VUL	7% - 8%
Moderate-Aggressive	80% / 20%	VUL	8% - 9%
Aggressive	100% / 0%	VUL	9% - 10%

Volatility is another consideration in determining the prudence of a given product type and the rate of return reasonable to expect. For instance, an Aggressive allocation historically produces higher rates of return over the long-term, but also a wider range of expected returns and possibly even negative returns over the short-term. As such, more Aggressive allocations also involve risk that cash values will be “sold at a loss” to cover monthly deductions for cost of insurance charges and policy expenses, thereby adversely impacting the rate of return that is reasonable to expect.

Monte Carlo simulations are useful in quantifying such adverse impact of volatility, and the corresponding risk of a “premium call” due to volatility, where the probability a policy will lapse without value and without paying a claim unless addition premiums are paid is calculated in thousand(s) of separate trial runs using different and randomly-selected rate of return assumptions. Understanding the probability of a “premium call” is essential to determining the product type that is prudent for the given client risk profile.

See below flowchart of an example decision-tree for identifying the product types appropriate to the various risk profiles.



* VUL cash value allocations that historically produce the approximate target rates of return corresponding to each risk profile are as follows:

- Moderate-Conservative: 40% equity/60% fixed
- Moderate: 60% equity/40% fixed
- Moderate-Aggressive: 80% equity/20% fixed
- Aggressive: 100% equity/0% fixed

Source: Morningstar

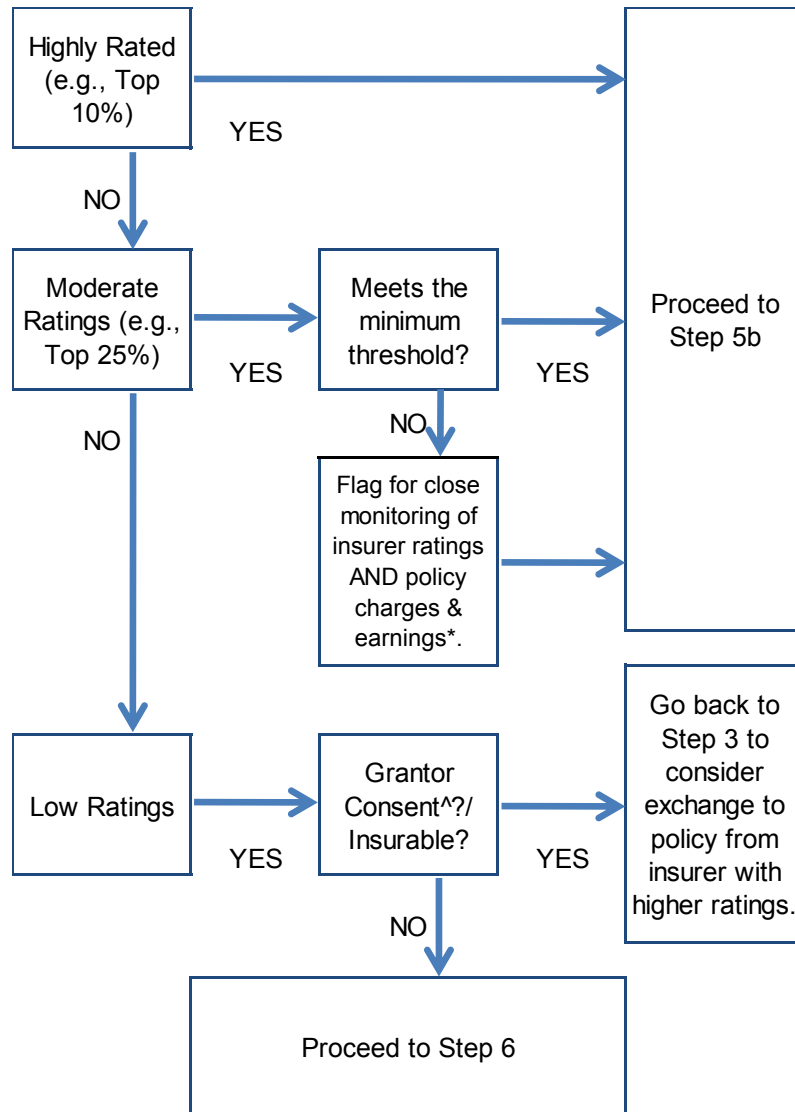
Step 4 - Formalize: The life insurance industry is full of constraints and conflicts (i.e., not unlike the investment business of decades ago). With 10,000+ pricing combinations and permutations for every product, cost of insurance charges (COIs) being the largest expense (not commissions), and as much as an 80% variance between best-available rates and terms (BART) and worst-available rates and terms (WART), no insurer, product, compensation model, distribution system, nor proprietary product is inherently “better” for all clients or all situations.

Understand the universe of products for the product-type peer-group identified in Step 3, ask the life insurance advisor about constraints (e.g., agents/brokers not properly licensed to discuss and place whichever product type is identified in Step 3, distribution systems that limit product availability to only or mostly proprietary products, fee-only advisors limited to a handful of products offering no/low sales-loads but potentially higher COIs, etc.), and conflicts (e.g., higher commissions for placement of some product than other products, special payments for placement of proprietary products, fees charged for some products but not for other products, reward trips, etc.) and discuss reconciling and resolving such constraints and conflicts.

Step 5 - Implement: A search for best-available rates and terms (BART) considers at least the financial strength and claims-paying ability of the insurer, the competitiveness of internal policy charges, the stability of the insurer’s pricing representations, restrictions on access to policy account values, and the historical performance of invested assets underlying policy cash values. Investigating such discrete product attributes also avoids hypothetical illustration comparisons now considered “misleading”, “fundamentally inappropriate”, and unreliable by financial, insurance, and banking industry authorities. Additional considerations for prudent implementation can be underwriting capabilities and ongoing service and reporting.

See below flowchart showing an example decision-tree of a search for best-available rates and terms.

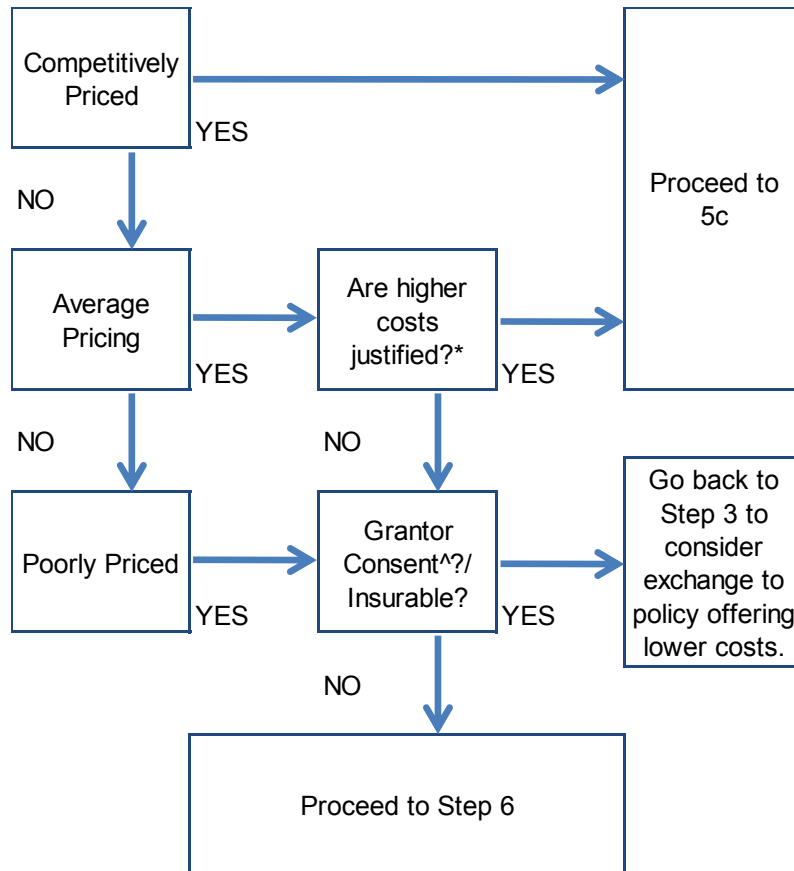
5a – Financial Strength and Claims-Paying Ability



*When an insurer's rating is downgraded, the change often means either the insurer's profitability has declined, or the insurer's reserves have deteriorated, or both. The insurer's most immediate response to a downgrade in its ratings, and its most effective means for restoring profitability and recovering reserves, can be to increase policy costs for cost of insurance (COI) charges and expenses and/or decrease interest/earnings credited to policy cash values. In other words, when ratings go down, policy charges are more likely to be increased and/or policy interest/earnings are more likely to be decreased, and thus premiums are likely to (need to) go up. As such, it can be important to measure what is actually being charged and what is actually being earned from invested assets underlying policy cash values for insurers with lower financial strength and claims-paying ability ratings.

^Grantor Consent refers to the grantor's consent to participate in the underwriting process.

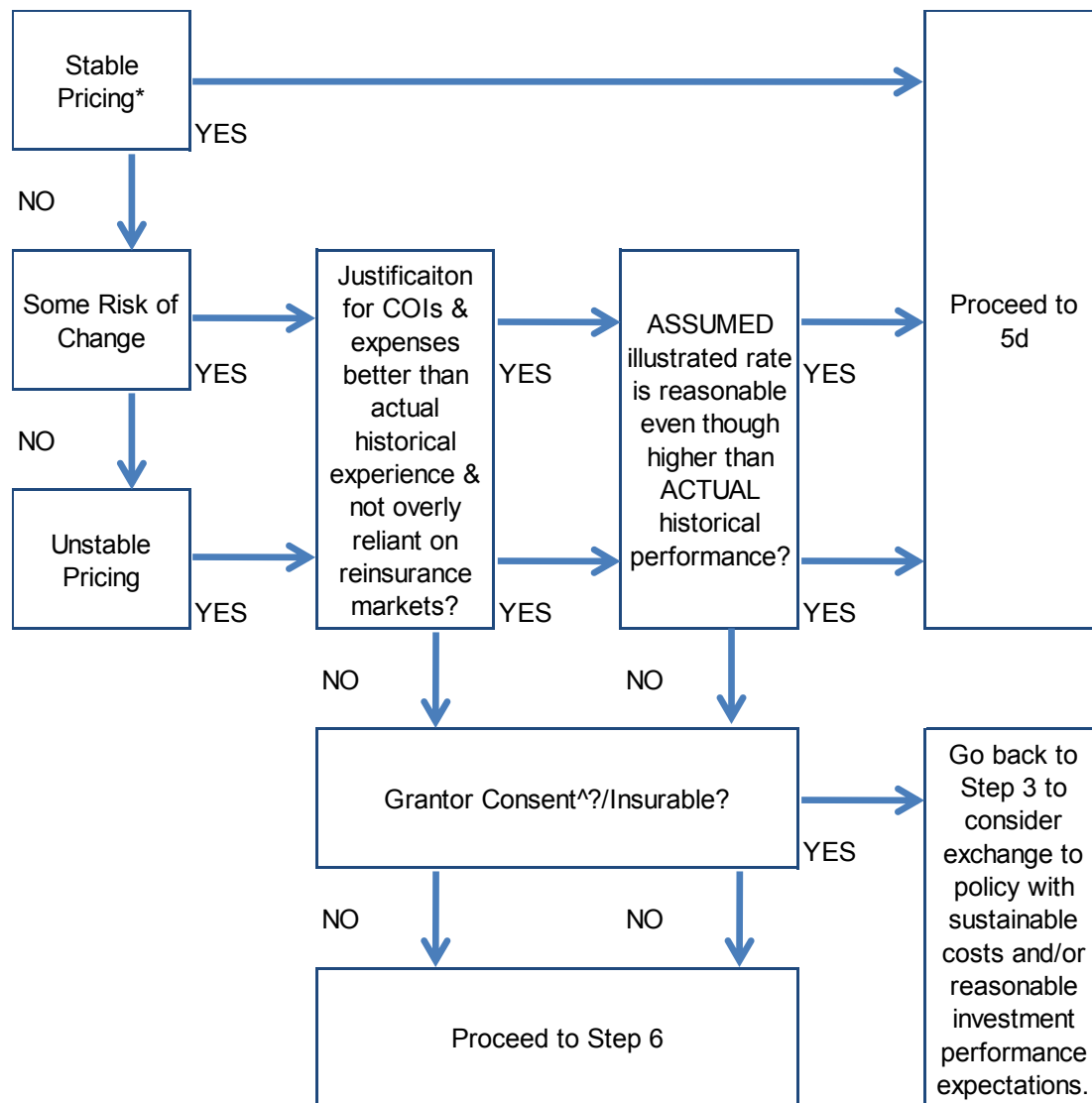
5b – Cost Competitiveness



* UPIA Section 7 prescribes fiduciaries "may only incur costs that are appropriate and reasonable in relation to the assets, the purposes of the trust, and the skills of the trustee." As such, if cost of insurance charges (COIs), fixed administration expenses (FAEs), cash-value-based "wrap fees" (e.g., VUL M&Es) and/or premium loads are higher than that generally-available in the marketplace, then trustees should either: 1) document the reasons for paying higher costs (e.g., very high ratings for financial strength and claims-paying ability, very stable pricing, very high cash value liquidity, superior performance of invested assets underlying policy cash values, etc.) or 2) consider activities to reduce costs.

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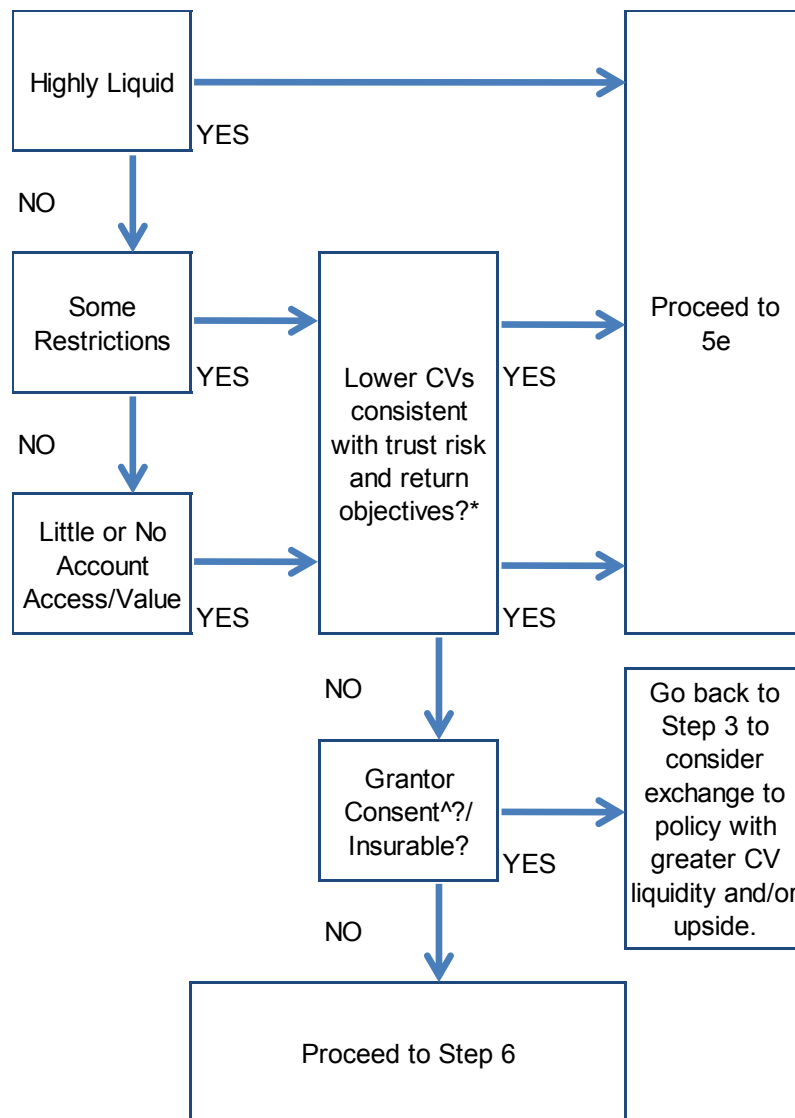
5c – Pricing Stability



* e.g., pricing that is consistent with the insurer's actual historical mortality experience, operating experience, and investment experience.

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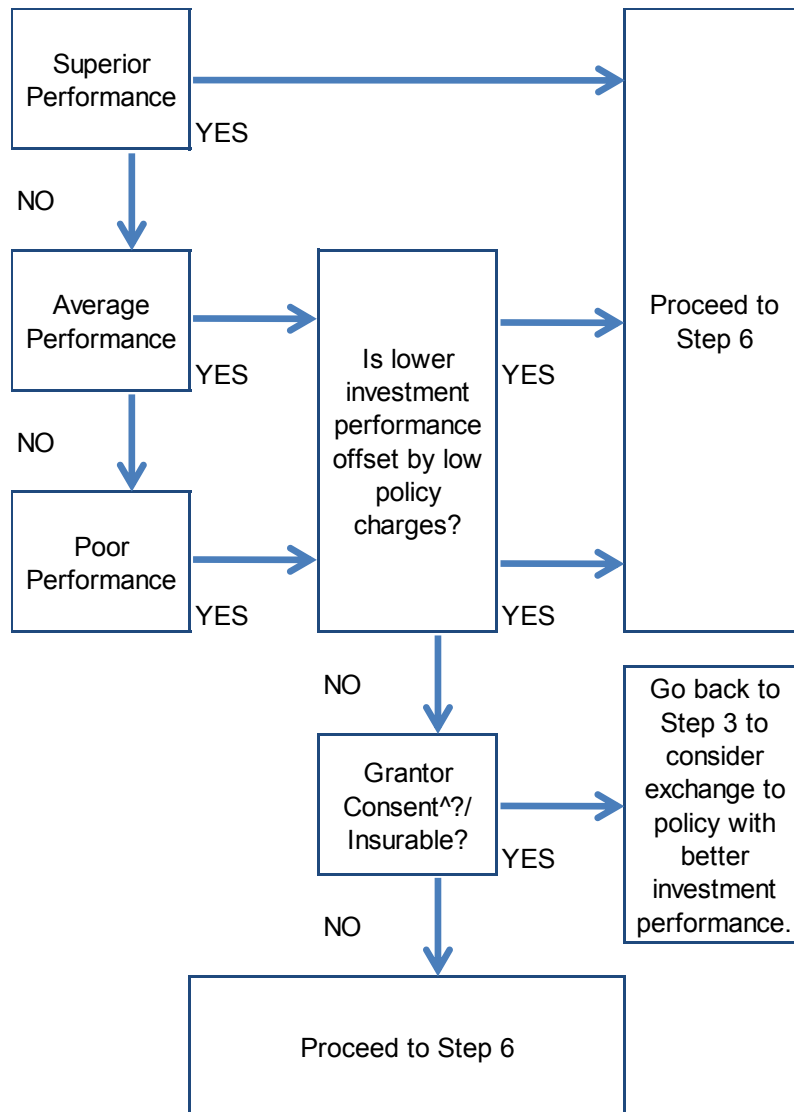
5d – Relative Account Liquidity



* Cash Values can be relevant to trust objectives when an objective of the trust is to 1) accumulate wealth for a specific reason like retirement, 2) pay future cost of insurance charges (COLs) and policy expenses, and/or 3) seek higher interest/earnings rates on invested assets underlying policy cash values to the extent consistent with trust risk/return parameters. In the absence of the above or other reasons that cash values would be relevant to trust objectives, policies with lower or even no cash values can be suitable. While a policy with cash values is considered more suitable than a policy without cash values WHEN ALL OTHER POLICY ATTRIBUTES ARE EQUAL, a policy without cash values can be more suitable than a policy with cash values if/when the policy without cash values offers some other advantage over the policy with cash values. For instance, term life insurance (e.g., LT10) products have no cash value, but offer a much lower premium than policies with cash values. Similarly, guaranteed universal life (i.e., GUL) products often have little to no cash values, and to the extent premium requirements are lower than the premium requirements for a product with cash values, then a GUL product can be more suitable than a product with cash values.

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5e – Historical Performance



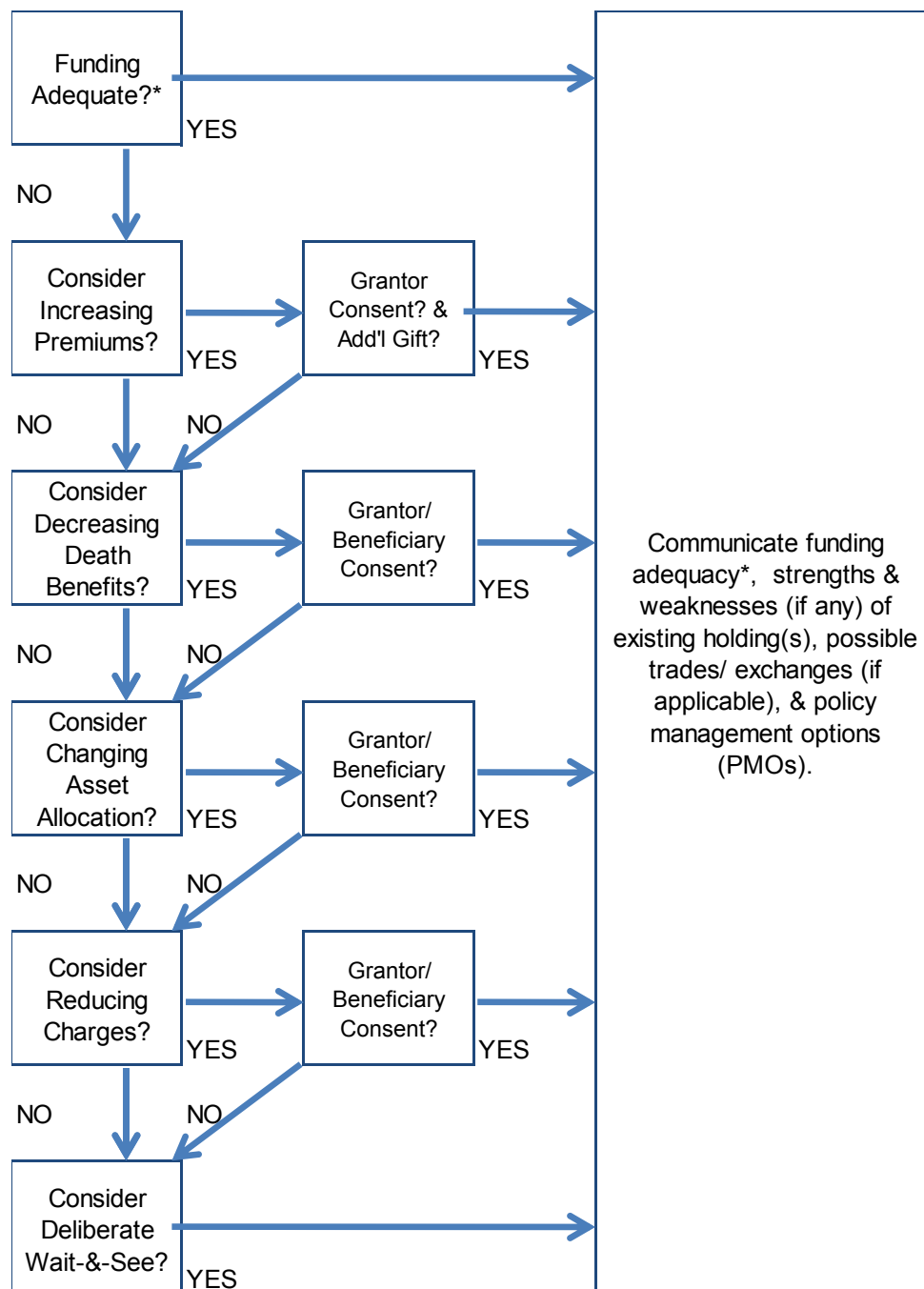
* UPIA Section 2(b)(5) prescribes that fiduciaries “shall consider ... the expected total return [from the] overall investment strategy having risk and return objectives reasonably suited to the trust.” While past performance is no guarantee of future results, using actual historical performance is generally-accepted as a useful measure of expected future performance. Because illustrations of HYPOTHETICAL policy values are NOT required to illustrate an assumed rate of return that is correlated with actual historical performance of invested assets underlying policy cash values, it is particularly important for fiduciaries to separately consider the expected return on invested assets underlying policy cash values.

^Grantor Consent refers to the grantor's consent to participate in the underwriting process.

Step 6 - Monitor: Life insurance has been among the most disappointing asset types relative to client expectations for decades due in part to lack of monitoring, reporting, and management. Advising clients about the prudent selection/retention and proper management of life insurance, therefore, involves periodically checking on changes in the health, risk tolerance, time horizon, performance expectations and/or planning objectives of the client, changes in the financial stability and claim-paying ability of the insurer, and/or changes in internal costs, investment performance, and/or the funding adequacy of policy holdings. Only with such information can policies be prudently managed as follows:

Portfolio Management Option	Under-funded Policies	Over-funded Policies
PMO #1: Change Premiums	Increase premiums to increase cash values in amounts necessary to cover policy costs over the intended coverage duration.	Reduce premiums or refund cash values no longer necessary to cover policy costs over the intended coverage duration.
PMO #2: Change Benefits	Reduce benefits to reduce costs such that existing cash values and planned premiums can cover reduced costs over the intended coverage duration.	Increase benefits using excess cash values to cover costs of increased benefits over the intended coverage duration.
PMO #3: Change Cash Value Allocation / Expected Rate of Return	Re-allocate to more aggressive asset classes with a historically higher expected rate of return in an effort to increase cash values needed to cover policy costs over the intended coverage duration, albeit with greater volatility/risk of loss.	Re-allocate to more conservative asset classes to reduce volatility and minimize the risk of a "premium call" otherwise needed to cover policy costs over the intended coverage duration.
PMO #4: Change Policy Costs	Reduce excessive costs such that existing cash values and planned premiums are better able to cover the cost of intended benefits over the intended coverage duration.	Reduce excessive costs such premiums can be reduced, cash values can be refunded, benefits can be increased, and/or cash values can be reallocated to more conservative asset classes.
PMO #5: Coverage Duration	Consider "wait & see" where cash values are sufficient to support policy costs for a reasonable period, where policy costs are competitive, where interest/earnings are within the expected range of returns even if below the target rate of return, and there is no looming risk of a lapse.	N/A

See below flowchart showing an example decision-tree for the above portfolio management options (PMOs).



*Funding Adequacy refers to the degree to which existing policy cash values and planned premiums are sufficient to pay future cost of insurance charges (COIs), fixed administration expenses (FAEs), cash-value-based "wrap fees" (e.g., VUL M&Es) and/or premium loads over the intended duration of the policy contract. If a policy is intended to provide a permanent death benefit, then funding adequacy means cash values and planned premiums are sufficient to pay cost of insurance charges (COIs) and policy expenses to contract maturity (i.e., typically either age 100 or age 120). However, if the intended coverage duration is less than permanent (e.g., in the case of an insured in declining health where life expectancy is believed to be shorter than that for a health insured), then funding adequacy means cash values and planned premiums are sufficient to pay cost of insurance charges (COIs) and policy expenses over this shorter period of time.

COMMENT:

Life insurance is an essential planning tool for many financial and estate planning professionals, but remains the last, largest, most-neglected, and most-disappointing asset on clients' balance sheets and in planners' planning. At the same time, the population over age 65 is projected to double between now and 2030, and the Baby Boom Generation is expected to transfer more wealth than ever before, substantially increasing the demand for life insurance products. Given such an increase in demand, and the neglect and poor-performance of this asset to date, it's time for a new operating system for life insurance advice.

Financial and estate planners who reject the outmoded life insurance industry O/S of the past which doesn't even include a "management module", and instead adopt a Prudent Investor O/S will bring clients greater transparency, be better prepared to meet the coming demand for advice, and be more likely to lower costs, improve performance, and meet client expectations. The West Point Draft of Best Practice Standards for life insurance is just such a Prudent Investor O/S based on the same established, proven, and universal decision-making framework widely-accepted in the investment business.

HOPE THIS HELPS YOU HELP OTHERS MAKE A *POSITIVE* DIFFERENCE!

Barry Flagg

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