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New Insurance Policies Attract Attention

From MONEY Magazine

A new kind of life insurance is making its debut to rave notices from the critics. Thus far only a handful of companies, most of them small, are selling it. Industry titans will probably have to market it sooner or later.

Walter Miller, a senior vice president of New York Life, No. 5 in the industry, says "I can't believe there's any insurance company that isn't considering it."

If you tried to invent the ideal policy, it might closely resemble universal life. The new plan consists of a flexible, do-it-yourself combination of life insurance and a high-interest savings account.

To hear most insurance men tell it, they already sell such a policy — whole life. It provides a constant amount of coverage for as long as you want it, at a premium that never changes. Part of the premium buys insurance and part goes into cash value, which somewhat resembles a savings account and gradually replaces the insurance.

For most of this century, agents have pushed whole life with notable success. It now insures Americans for $1.2 trillion. However, it falls abysmally short of the ideal.

First of all, whole life is rather inflexible. You can reduce the coverage, but you can't increase it much unless your policy has a special provision letting you buy more later. Furthermore, buyers have no control over dividing their premiums between insurance and cash value.

Still another problem is the sales commission. Most of this cost is built into the first year's premium, and it is so large that just enough money remains to pay for insurance. Not until the second or third year do you accumulate any money in a typical whole life policy. You pay the same heavy front-end commission for each new policy you buy, even if it's from the same agent and company that sold you one before.

Worst of all, your cash in a whole life policy earns interest at a paltry rate. The insurer never tells you what the rate is, but analysts outside the industry estimate that at best it rarely exceeds 6 percent — and then only after many years.

James C.H. Anderson, president of Tillinghast Nelson & Warren, insurance consultants in Atlanta, devised universal life in 1975 to solve the problems and overcome the deficiencies of whole life.

Three years later his brainchild was marketed by Hutton Life, a subsidiary of E.F. Hutton, the brokerage firm. One element of universal life is a renewable term policy — pure insurance protection with no cash value and a premium that goes up each year. The other element is a cash-value account resembling a money-market fund. You can adjust either element almost at will.

To encourage you to invest in your life insurance policy — rather than merely paying set premiums — universal life offers significantly higher interest rates on cash values than traditional policies ever have, lately 8-½ to 15 percent.

Rather than making long-term investments, the insurer puts most of your money in medium-and-short-term government securities. Interest paid to policyholders follows money-market rates.

Every company offering universal life requires you to buy a sizable amount of insurance at first. There is also a floor under how much you must pay in. For example, a 25-year-old man who buys a $50,000 policy from Hutton Life must contribute at least $431 in the first year. The next year the minimum premium drops to $102, and after that it rises slowly. The money needn't always come from your pocket, though. You can take it at no cost from the policy's cash value.

Above the minimum levels of coverage, you can design your plan to meet your needs. As your situation changes, you can easily alter your policy.

During periods of your life when you can afford to save, universal life lets you put in additional money that will earn interest at money-market rates. At other times, you can withdraw money, again at no cost, to meet major expenses. As in a whole life policy, all earnings are tax sheltered. You pay no income tax until you withdraw more money than the total you have put into the policy.

In our opening illustration, using a Hutton policy, we assume that a young newly married couple, both working, need little insurance but can put some income into savings. Because they plan to have children, they buy coverage for the husband, spending $800 the first year. Cash value starts accumulating immediately and earns interest at Hutton's present rate, 11 percent, which is guaranteed for one year.

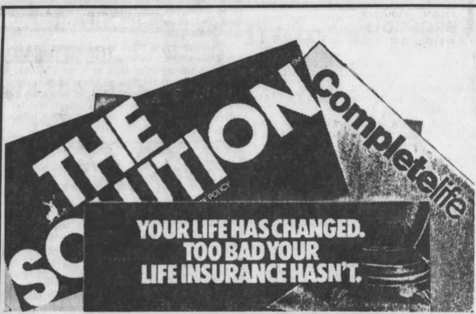
When their responsibilities grow — with the birth of children, advances in career, the purchase of a house — the couple increase their insurance protection. At its peak, in this example, the policy provides $244,452 of coverage.

By increasing the premium whenever possible, the couple accumulates $44,452 in cash value by the time their first child enters college. Then they begin withdrawing $6,000 a year.

They also stop paying premiums, letting the insurance company subtract the necessary amount each year ($912 at age 46) from the cash account. Once the two children have finished college, the couple begin putting $5,000 a year into the policy.

Assuming a constant 11 percent interest rate, the cash value would mount to $118,739 when the husband is 65. The couple could then drop the policy and invest the money. At a continuing 11 percent return, they would earn $13,000 a year without touching the principal.

Universal life policyholders get annual statements of their insurance and cash value, the interest rate on the investment portion, and how much of their money has gone for insurance, investment and company fees. That is a major innovation in life insurance.



Sampling of universal life policies

Company	Policy name	Current interest	Load*	First-year fee (per $100,000 policy)*	Minimum-coverage**
E. F. Hutton Life	Completelife	11%	7.5%	$360	$25,000
First-Penn Pacific	The Economist	10.5%	7.5%	$378	$20,000
Great Southern	Lifetime Life	10.5%	A	$300	$25,000
The Hartford	The Solution	10.25%	5.0%	$575	$50,000
Life Insurance Co. of Virginia	The Challenger	10.88%	9.0%	$708	$100,000
Transamerica	T-Plan Life	14.56%	10.0%	None	$50,000

* Load is a portion of each premium payment used to cover commissions and premium taxes. Fees generally cover issue and underwriting costs plus an element of commissions. Costs do not reflect charge for insurance itself, which generally runs about the same for all companies.

** May depend on age.

A—15% of the first $1,000 of premiums. 7.5% thereafter.

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