WARNING: THE NATIONAL ASSOCIATION OF LIFE UNDERWRITERS HAS DETERMINED THAT THE FTC IS DANGEROUS TO YOUR LIFE INSURANCE

The Staff of the Federal Trade Commission — **not the Commission itself** — has completed a report on cost disclosure in life insurance. The report contains many statements about cash value life insurance which are either misleading, or based on false and controversial assumptions, or both. To provide balanced information, the following replies to the FTC's report and provides much needed additional explanation.

A RESPONSE TO THE FTC

• THE REPORT STATES that the rate of return consumers receive on the savings component of cash value insurance is often very low compared with what could be earned by placing the savings component of cash value life insurance in other types of savings or investments.

— THE FACTS ARE that this assumes a whole life policy can be separated into a combination of pure insurance protection and a separate savings fund. This is a misleading and erroneous concept; it presumes that the cash value in a whole life policy is the same as a bank savings account.

Unlike a savings account, the cash value of a whole life policy may be used in additional ways, such as to purchase extended term or paid-up life insurance benefits, or for a relatively low cost policy loan. Moreover, income taxes are not currently payable on interest that is paid on the cash value.

Further, at death, life insurance proceeds can be obtained quickly without passing through the estate of the insured. Other investment media do not provide any of these features; they do not provide the very long term investment guarantees which are inherent in whole life policies, nor can they guarantee an insured's ability to continue his program of family protection, by providing such benefits as waiver of premium in the event of disability. These advantages of cash value life insurance are essentially ignored by the FTC Staff in their statements concerning the low rate of return on the savings component of cash value insurance.

• THE REPORT STATES that consumers earn 1 to 2 percent on their whole life cash value policies.

— THE FACTS ARE that it is simply incorrect to say that the earnings estimate for whole life or cash value policies is 1 to 2 percent. The FTC Staff economist who headed their life insurance study later stated that the 1.3 percent figure quoted in the report ". . . represents the return that all policyholders received in 1977. So, it's not just whole life insurance policyholders. It was people who had endowment policies, that are much more savings-intensive, so-called limited pay-life, and a lot of exotic things, called deposit term . . . When we talk about a return on a particular whole life policy that's a different calculation." This same economist went on to admit that some whole life policies have rates of return as high as 7 or 8 or even 9 percent. The FTC Staff has therefore conceded that such an aggregate industry figure has no real relevance for the individual purchaser of life insurance.

In calculating 1.3 percent as an "industrywide rate of return", the FTC Staff has used such a mixture of different products issued at different times that the figure is totally meaningless for any particular buyer. Also, the figure assumes that all premiums paid for ordinary life insurance go either for the cost of protection or "savings"; the figure contemplates an allowance for insurer expenses that is barely adequate to pay the industry's taxes, much less the substantial expenses of operating financially stable insurance companies.

• THE FTC STAFF REPORT SAYS that the cost of similar life insurance policies varies widely.

— BUT THE FACTS ARE that the costs of similar life insurance policies do not vary widely. They do, however, vary as much as the costs of similar automobiles, bicycles, and lawnmowers vary.

One of the main reasons for the variance in cost of whole life policies is that the companies in the life insurance marketplace do not produce identical products. A portion of the disparity in prices can be explained by this differentiation in product line. Other factors affecting variation in the cost of life insurance from company to company are different policy provisions, policy loan interest rates, anticipated dividends, cash value growth, method of premium payment, yields from company investments, mortality experience, type of business sold, size of company, average size of policy sold, quality of field representatives, administrative and sales expenses, underwriting criteria, financial standing and reputability, investment philosophy, and gains or losses incurred.

Further, specific life insurance markets are not similar. As with other markets, some parts — such as the industrial insurance market — are harder to reach than others, or at least call for different and sometimes more expensive marketing techniques. This dissimilar marketplace increases cost and often necessitates somewhat different products, which are in turn priced differently.

• THE FTC STAFF SAYS that consumers often receive a small amount of protection against premature death relative to the premiums paid for ordinary insurance.

— THE FACT IS that if any person could know that he is going to die within a year, or even five years, there is no doubt that his best buy would be some form of low-cost term insurance. Fortunately, we are not given this kind of foresight, and therefore we must plan — and hope — for longevity. The FTC Staff would prefer to have people buy term insurance and invest separately the difference between the premium for the term insurance and the premium for the same amount of cash value insurance, on the theory that if the insured should die during the term period the beneficiary will not only have the insurance proceeds but also whatever amount has been accumulated in the separate investment fund.

This advice may prove excellent in some cases; however, it can prove disastrous for the person who either a) lives beyond the period of their term insurance (most term insurance expires at a certain age) and has no insurance at all when he dies, or b) lives so long that the premiums for the term insurance (they increase with age) grow so high that he can no longer afford them and is thus forced to lapse his insurance. Curiously enough, while one government agency — the FTC — seems to be urging people to buy term insurance because it is cheaper, another government agency — the Veterans Administration — has recognized the danger inherent in over-reliance on term insurance, and advises veterans in VA Pamphlet 29-76-1 (May 1976) that "The effect on our term policyholders of the steep insurance premium increases required at the older ages has been of great concern to both the Veterans Administration and the Congress."

The VA says, "Since 1940, the majority of our term policyholders have gone through six terms of renewal which have increased their premiums substantially. At each renewal period, we have suggested that consideration be given to converting their insurance to one of the permanent plans of insurance such as the Ordinary Life, 20-payment Life or 30-Payment Life plans."

The VA goes on to say that, "In addition to alerting our policyholders of the increased cost of continuing the insurance on the term plan at each renewal period, we have also made several mass mailings of literature about the advantages of converting to a permanent plan of insurance." The VA's admonitions are directed only at government-provided term insurance, but would apply to the forms of term insurance advocated by the FTC Staff as well.

• THE FTC STAFF REPORT ALSO SAYS that:

1. Consumers are uninformed about life insurance;
2. Consumers are unable to evaluate cost;
3. Most consumers do not compare policies for cost.

— BUT THE FACT IS that the FTC has conducted two separate surveys of its own, with much fanfare and at great expense to the taxpayers, on these very questions. One of these was conducted at Purdue University to determine what information consumers use in making life insurance purchase decisions and how various cost disclosure materials help them. The FTC also retained a professor at the University of Wisconsin to survey life insurance buyers in New Jersey regarding their recent purchases of life insurance.

The first study, which cost the taxpayer $155,000, concluded that "consumers exposed to any one of the six different disclosure systems used in this investigation were by and large able to make good purchase decisions." Reference to the results of this research was confined to a footnote in the FTC Staff report and a small summary buried in Appendix IX.

The other survey interviewed 194 buyers in New Jersey and only 3.1 percent had any dissatisfaction with the life insuranse policy they purchased. On the other hand, 83.3 percent were satisfied, of which number 15.6 percent said they were extremely satisfied and 41.7 percent said they were very satisfied.

Furthermore, 80.8 percent maintained that the sales presentation made by the agent was not confusing; 84.5 percent said the sales person was not aggressive, 78.9 percent claimed that the sales person did not urge them to make a decision in a short period of time, and 84.5 percent asserted that they would contact the same person if they required more life insurance.

Overall, the FTC-sponsored research indicates quite clearly that people make good purchase decisions and are satisfied with their purchases and the agents with whom they deal.

In the face of these contradictions by their own studies, one might wonder why the FTC Staff insists on assuming a Big Brother role for the consumer, especially in an area traditionally regulated by the states and not by the federal government; one might also wonder why the FTC seems to be working at cross-purposes with highly respected government agencies such as the Veterans Administration.

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