Universal Life

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What is this product, this product concept, called "universal life"? It is a pestilence which has come upon our land; it will consume in-force business and destroy our industry ... or so some might say. It is the instrument for the survival of our industry; it will shield us against the attacks by consumerists and other financial institutions ... or some might say. It is most likely neither of these extremes. It is simply permanent life insurance brought into the 1980's. Its fundamental "mechanics" are indistinguishable from those underlying traditional life insurance products.

Universal life really does only three key things differently than traditional forms of life insurance. **First, it alters the structural rigidity of traditional forms.** It transforms the traditional fixed-premium, fixed-benefit product into a dynamic product by making premium payments flexible and death benefits adjustable. **Second, it alters the "optics" of traditional forms.** It "opens up" permanent life insurance so that all its pieces are highly visible ... pieces like expense charges, mortality costs and interest credited. **And third, it alters the costs-to-benefit ratio on the savings component** inherent in any traditional life insurance product (other than, say, annually renewable term). It makes permanent life insurance a "better deal" as to its savings component by reducing expense charges on dollars saved (i.e., cash value build-up), and crediting a current rate of interest on accumulated cash value which is reflective of prevailing yields.

Mechanically, here's how a typical universal life product works. Premiums paid, less specified expense charges, are credited to an individual cash value account. Interest is credited at a current rate to, and pure mortality costs are deducted from, the cash value account on a monthly basis. And in the first year only, certain other specified expense charges are deducted from the cash value account. It's worth repeating. This process is precisely that underlying any permanent life insurance policy, except that the pieces are not visible to the buyer under traditional forms like they are under a universal form. In addition, universal products provide for an annual report to the buyer typically showing all of the pieces just described, as well as the cash value balance on a monthly basis.

The proponents of universal life would typically highlight its consumer- oriented features ... featues like adjustable death benefits, flexible premium payments, structural simplicity, unprecedented disclosure, current interest rate and mortality costs, and significant improvement in its savings features.

The opponents of universal life have typically said things like ... (1) the lower-than-normal commission levels produced may threaten the agency system, (2) the product may increase an already troublesome replacement problem, (3) total flexibility in premium payments eliminates the "forced savings" under fixed premium permanent insurance and may lead to no savings, and (4) the tax treatment of universal is uncertain. The uncertainty which exists with regard to the taxation of universal life is, in my opinion, neither less nor greater than that which exisits for many of the new products introduced over the last decade -- for example, excess-interest annuities and indeterminate premium whole life.

Arguments expressed by the opponents of universal life appear to focus on unknowns and uncertainties. In this context, they are natural and understandable. Change is, after all, often accompanied by skepticism, doubt, fear, ... uncertainty. It is frequently disturbing and unsettling. So it has been and will always be, but change nevertheless remains as an inevitable force