EQUITABLE

Adding value to financial planning with insurance portfolio reviews

Advanced Markets

Policy review guide

The purpose of this guide is to help in the policy review process. Your client's insurance portfolio may include whole life, universal life, indexed universal life, variable universal life or term policies. If your client wants to update their insurance based on a change in need or goals, it is important to understand these products to maximize their benefit to the client.

The guide includes:

- Checklists for each type of product and business-owned policies to help gather the information needed for a review.
- Product-by-product changes that might be made to help a policy meet the client's needs and goals:
  - Increase or decrease in insurance.
  - Reduce the cost of the policy.
  - Maximize livings benefits.
- Questions to ask if a new policy is being considered.
- Worksheets to use with 1035s when the policy has a loan.
  - How to calculate the tax on the 1035 when the loan is not carried over.
  - How much additional premium is needed, or loan repaid to carry over the balance of the loan.

Whole life policy review checklist

Policy #: ______________________ Issued by: ______________________

Policy details

Policyowner: ______________ Beneficiary: ______________ Register Date: _______

Insured: ______________ DOB: ______________ Rating Class: _______

If survivorship policy:

Insured: ______________ DOB: ______________ Rating Class: _______

Is second insured living? ◯ Yes ◯ No

Policy values

Face Amount: $ ______________ Death Benefit: $ ______________

Net Policy Cash Value: $ ______________ Annual Dividend: $ ______________

Dividend Option ◯ Paid-Up Additions (PUAs) ◯ Cash ◯ Reduce Premiums ◯ Accumulate

◯ Other ______________________________

Cash Value of PUAs: $ ______________ Death Benefit of PUAs: $ ______________

Basis in Policy: $ ______________ Surrender Charge: ◯ Yes ◯ No

Premium: $ __________ Premium Mode: ◯ Annual ◯ Semiannual ◯ Quarterly ◯ Monthly

Annual Out-of-Pocket Outlay:

Premium: $ ________ Loan Interest: $ ________ Loan Repayment: $ ______________

Policy is a Modified Endowment Contract: ◯ Yes ◯ No

Outstanding Loan: $ ________ Dividends Recognize Loan: ◯ Yes ◯ No

Annual Interest Rate ________ %

Policy features

Riders: ◯ Waiver ◯ Spouse Term ◯ Child Term ◯ Term on Insured ◯ ADB ◯ LTC

◯ Other ______________________________

Is any part of the death benefit term insurance? ◯ Yes ◯ No Term Death Benefit: $ ________

Is the term portion: ◯ Specified amount ◯ Combination of term and Paid-Up Additions/1-Year Term

Suggested ledgers to request from carrier

◯ Current Values Ledger

◯ Change dividend option to Reduce Premium/Balance to Paid-Up Additions

◯ Proposal showing minimum annual outlay/Proposal showing reduced paid-up policy

Term policy review checklist

Policy #: ______________________________ Issued by: ______________________________

Policy details

Insured: ____________________ DOB: __________________ Register Date: _________________

Type of Term Policy: ○ ART ○ YRT ○ Return of Premium ○ Level Premium Term ______Yrs

Conversion Option Ends Age: ____ or Policy Year: ___________

Policyowner: _________________ Beneficiary: _____________ Rating Class: _________________

Policy values

Face Amount: $ _________________________

Premium: $ _____________ Premium Mode: ○ Annual ○ Semiannual ○ Quarterly ○ Monthly

Waiver of Premium: ○ Yes ○ No

Child Term Rider: ○ Yes ○ No Amount of Term Rider: ____________________________

Suggested ledgers to request from carrier

○ ART, YRT or ROP Term: Ledger

○ Level Term: Ledger or schedule showing term premiums at end of level term period

Variable/indexed/current assumption universal policy review checklist

○ Variable ○ Indexed Universal Life ○ Universal Life

Policy #: ______________________ Issued by: ______________________

Policy details

Policyowner: ______________ Beneficiary: ______________ Rating Class: ______________

Insured: ______________ DOB: ______________ Register Date: ______________

If survivorship policy:

Insured: ______________ DOB: ______________ Rating Class: ______________

Is second insured living? ○ Yes ○ No

Policy values

Face Amount: $ ______________ Current Death Benefit: $______________

Policy Cash Value: $ ______________ Basis in Policy: $ ______________

Premium: $ __________ Premium Mode: ○ Annual ○ Semiannual ○ Quarterly ○ Monthly

(UL or IUL) Current Crediting Rate: ________% (VUL or IUL) Percentage of Funds in GIA: _____%

Guaranteed Interest or GIA Rate: _______% Policy is a Modified Endowment Contract: ○ Yes ○ No

Surrender Charge Period: $ ______________

Oustanding Loan: $ ________ Annual Interest Rate: _____ % Rate Credited to Loaned Account: ____%

Policy features

Death Benefit Options: ○ Option A ○ Option B ○ Child Term ○ Option C

Definition of Life Insurance Test: ○ CVAT ○ GPT

Riders: ○ Waiver ○ Spouse Term ○ Child Term ○ Term on Insured ○ ADB ○ LTC

○ Other ______________________________ ○ Return of Premium

Are there any secondary guarantees? ○ No-lapse guarantee ○ Lapse protection rider ○ Other

Loan Extension Provisions: ○ Yes ○ No Paid-Up Death Benefit Guarantee Option: ○ Yes ○ No

Is any part of the death benefit term insurance? What percentage or amount is term? ______________

Suggested ledgers to request from carrier

- ○ Current proposal
- ○ Proposal showing minimum annual outlay to carry the policy for life
- ○ Request proposals at guaranteed rate and at a rate the client agrees is appropriate

Business-owned policy review checklist

(Complete in addition to policy checklist)

Policy #: ______________________ Issued by: ______________________

Policy details

Premium Payor: ○ Business ○ Insured ○ Insured's Business Co-Owner

If premiums are being paid by the business, is the policyowner being taxed on the premiums: ○ Yes ○ No

Is the policy subject to a collateral assignment? ______________________

Policy issue date: ______________

If the policy was issued after August 6, 2007, or if it was issued prior to and materially modified after that date:

Did the employer obtain an EOLI Consent and Acknowledgement form from the insured? ○ Yes ○ No

Has the employer filed IRS Form 8925 each year? ○ Yes ○ No

Is the insured: ○ Owner of the business ○ Key Person ○ Retired or former employee

Original purpose of insurance: ○ Key Person ○ Buy-sell funding ○ Security for loan ○ Executive benefit

Does the original purpose still apply: ○ Yes ○ No

Is there a written, signed: ○ Split-dollar agreement ○ Deferred compensation agreement ○ Buy-sell agreement

Business details

Is the business a: ○ C Corporation ○ S Corporation ○ Partnership ○ LLC ○ Sole Proprietorship

Business owners:

Name: ______________________ Age: ______ Percent Ownership: ______________%

Name: ______________________ Age: ______ Percent Ownership: ______________%

Name: ______________________ Age: ______ Percent Ownership: ______________%

Whole life policy

Goal: Increase or decrease insurance protection

Dividend options:
Consider changing the dividend option. If dividends are being used to reduce the premium or are paid in cash, the total death benefit of the policy may be increased gradually by using the dividends to buy Paid-Up Additions. The amount of additional paid-up insurance purchased by the dividend depends on the insured's age. For example, a $2,000 dividend on a policy insuring a 45-year-old male will purchase more additional paid-up insurance than a $2,000 dividend on a policy insuring a 55-year-old male.

Increase in face amount:
Most whole life policies do not allow for an increase in the face amount of the policy unless a paid-up additional insurance rider is included in the policy.

Goal: Reduce the cost of the policy

Dividend options:
Dividends may be buying Paid-Up Additions (PUAs). The dividend option may be changed to reduce premiums or reduce premiums with the balance buying PUAs.

Use of dividends:
Many whole life policies offer a plan where the cash value of Paid-Up Additions is surrendered to pay current premiums.

Nonforfeiture options:
If the client doesn't want to pay any additional premiums, the two nonforfeiture options available on most whole life policies are:

Reduced Paid-Up — the policy cash value is used to purchase a paid-up policy. The amount of insurance purchased will be most likely be less than the current face amount, but no further premiums are due.

Extended Term — The policy cash value is used to purchase term insurance in the same amount as the current policy. The length of the term insurance depends on the policy cash value.

Goal: Maximize living benefits of the policy

Dividend options:

The policyowner can elect to have policy dividends paid in cash. If the dividend exceeds the policy premium, the dividends may pay the premium first with any excess dividend paid in cash.

If dividends are paid in cash, the dividend will be taxable once dividends paid exceed basis in the policy.

Policy withdrawals:

The policy cash value in a whole life policy is made up of guaranteed cash value, cash value of Paid-Up Additions (PUAs) and cash value of dividends left to accumulate.

The cash value of PUAs comes from dividends buying PUAs each year or premiums paid into a PUA rider. The ledger will show the amount of the base premium and the amount of the PUA rider premium.

The only cash value that may be withdrawn from the policy is the cash value of PUAs. The guaranteed cash value is not available to withdraw.

When the cash value of PUAs is withdrawn (surrendered), the face amount of the PUAs will decrease. Each dollar of cash value withdrawn will reduce the face amount of PUAs by more than one dollar. The younger the insured, the higher the PUA face reduction.

Dividends are paid on the PUA face amount. As the face amount decreases, the dividends on PUAs decrease.

Nonforfeiture options:

Once all the PUAs in a policy have been withdrawn, policy loans must be taken to access the guaranteed cash value.

Whole life policies may have either a fixed or variable loan rate. The interest may be due either at the beginning or end of the policy year.

Policy loans may be a good source of funds if the plan is to pay back the loan. Loans may be repaid. Policy withdrawals may not be returned to the policy.

Dividends may be affected, positively or negatively, by the existence of a policy loan. Please see the discussion of policy dividends below.

The policy loan will not be treated as taxable income if the policy stays inforce. If the loan interest is not paid and there isn't enough policy cash value to borrow to pay the loan interest and policy premium, the policy may lapse.

Understanding dividends on whole life policies

An insurance company calculates the premium for a participating whole life policy by assuming their mortality experience will coincide with the CSO mortality table, the interest they earn will equal the minimum rate guaranteed in the policy and operating expenses will be at a predetermined amount. To declare dividends, their actual mortality, earnings and or expense experience must be better.

The inforce whole life ledger assumes the current dividend scale continues for the life of the policy. Dividends are not guaranteed.

Policy loans may affect dividends. Dividends may be higher or lower than the same policy without a loan. This effect is referred to as direct recognition. The amount of the downward or upward adjustment of dividends depends on whether the assumed interest rate used in the calculation of the dividend scale is higher or lower than the loan interest rate. For example, if the loan rate is 8% and the interest rate assumption in the dividend calculation is 4%, the policy with a loan will get a higher dividend than the same policy without a loan. On the other hand, if the loan rate is 6% and the interest rate assumption in the dividend calculation is 7%, the policy with a loan will get a lower dividend than the same policy without a loan.

Policy loan interest rate	**8%**	**6%**
Interest rate assumed in dividend scale calculation	**4%**	**7%**
Policy with a loan gets:	**Higher dividend**	**Lower dividend**

Universal life, variable universal life or IUL policy

Goal: Increase or decrease insurance protection

Dividend options:

A change in death benefit option from A to B may allow the policy death benefit to grow as the policy account value grows. Consider this strategy if the plan is to pay additional premiums.

A change from option A to option B does not typically require evidence of insurability. In the year of the change, the specified amount is reduced by the existing policy account value meaning the net amount at risk doesn't change. The net amount at risk is the difference between the policy death benefit and the policy account value.

Increase in face amount:

The policy may allow an increase in the face amount of the policy with evidence of insurability. In some cases, the policy won't allow in increase. Some of the reasons why an increase in face may not be allowed include:

- A rider on the policy prohibits an increase.
- The policy is based on something other than the current Commissioners Standard Ordinary (CSO) mortality tables and the increase in face is not contractual.
- The terms of the policy do not allow an increase in face.
- Underwriting determines the insured's rating is different from the rating on the original policy, so the face amount may not be increased.
- Considerations when increasing the policy face amount:
- An increase in face may lead to a recalculation of the MEC premium. The MEC premium calculation uses the policy account value at the time of the change to determine the new MEC premium. A high policy account value may result in a MEC premium lower than the planned premiums.
- A face amount increase that happens on a date other than the policy anniversary will result in a mismatch between the policy anniversary and the new MEC date. This can make it challenging to illustrate future premiums.
- The face increase may lead to a new layer of surrender charges, policy charges and/or premium charges.

Decrease in face amount:

Most policies allow a decrease in the face amount of the policy. A decrease may not be allowed if the decrease would result in a face amount below the policy minimum.

Considerations when decreasing the policy face amount:

- A decrease in face may lead to a recalculation of the MEC premium. The MEC premium calculation uses the policy account value at the time of the change to determine the new MEC premium. A high policy account value may result in a MEC premium lower than the planned premiums.
- A face amount decrease that happens on a date other than the policy anniversary will result in a mismatch between the policy anniversary and the new MEC date. This can make it challenging to illustrate future premiums.
- The face decrease may lead to a surrender charges.
- A decrease in face will cause a recalculation of the Guideline Level Annual Premium (GLAP). If the GLAP is negative, the total amount that may be paid into the policy under the Guideline Premium Test will decrease each year, possible causing premium force-outs. In some cases, the policy will lapse due to the force-outs and the inability to add more premiums to the policy. If you see that on the illustration, it may make sense to either keep the current death benefit or reduce it by a lesser amount.
- Some policies are banded, meaning there are lower cost of insurance (COI) rates for higher face amounts. It can happen that a decrease in face that takes a policy into a lower band results in higher COIs than the higher face. For example, if a policy is banded at $250,000, the premium for a $250,000 face may be lower than the premium for a $200,000 face.

Goal: Reduce the cost of the policy

Dividend options:

It may be possible to reduce the premiums paid into the policy based on the current policy value or no-lapse guarantee feature. An inforce illustration will show how long a policy can last with reduced premiums. If you're requesting illustrations from another carrier, request an illustration based on a range of crediting rates.

Consider using a varying premium payment schedule. For example, if a policyowner is paying college tuition and knows cash flow will increase in the future, try paying a minimum premium for a short number of years and then increasing the premium.

Change in death benefit options:

The policyowner may be able to pay less in premium by changing from Option B to Option A. The net amount at risk, and therefore the cost of insurance, will be less with a level death benefit (Option A).

Note: A change from Option B to Option A will cause a recalculation of the Guideline Level Annual Premium (GLAP). If the GLAP is negative, the total amount that may be paid into the policy under the Guideline Premium Test will decrease each year, possible causing premium force-outs. In some cases, the policy will lapse due to the force-outs and the inability to add more premiums to the policy. If you see that on the illustration, it may make sense to keep the policy at Option B.

Goal: Maximize the living benefits of the policy

Policy withdrawals:

Policy cash value may be withdrawn up to the limits specified in the policy.

In general, policy withdrawals are not taxable until they exceed the basis in the policy, assuming the policy is not a Modified Endowment Contract (MEC). The exception to that is when the policy is in the first 15 policy years. Withdrawals may be limited by the definition of life insurance test.

Withdrawals may not be allowed if they would reduce the policy face amount below the specified minimum face. Withdrawals within the first 7 years, or in the 7 years following a material change, may cause the policy to become a MEC.

In general, only the surrender value net of any surrender charges may be withdrawn. If the policy has a cash value enhancement rider that increases the policy value in the early years by returning policy charges or reducing surrender charges, the increased amount is not typically available for withdrawal.

A withdrawal generally reduces the policy account value, the cash surrender value, and the death benefit on a dollar-for-dollar basis.

Policy loans:

Policy cash value may be borrowed up to the limits specified in the policy.

Policy loans may be a good source of funds if the plan is to repay the money. Policy loans may be repaid at any time.

In general, only the surrender value net of any surrender charges may be withdrawn. If the policy has a cash value enhancement rider that increases the policy value in the early years by returning policy charges or reducing surrender charges, the increased amount is not typically available for withdrawal.

A withdrawal generally reduces the policy account value, the cash surrender value, and the death benefit on a dollar-for-dollar basis.

Questions to ask if a new policy is being considered

In all cases:

- Will the insured qualify for the same or better rating as in the existing policy?
- Has the insured's smoking status changed from when the existing policy was issued?
- Does the new policy offer a guaranteed rate and how does it compare to the existing rate?
- Are there features on the existing policy such as lapse protection rider, waiver of premium, spouse or children rider, charitable rider, customer loyalty credits or bonuses (in place or about to be received) that add value to the policy? Or, are there features on the proposed policy not available on the existing that meet current needs?
- Has the risk tolerance of the policyowner changed since he or she bought the policy?
- What is the surrender charge on the new policy and does the client understand the charges?
- Is the policy owned by a business? If so, and if the face amount will be higher on the new policy, the policy must comply with the employer-owned life insurance rules under IRC 101(j) in order the keep the death benefit income tax-free to the business.

When the goal is to increase or decrease insurance protection

- Does the existing policy allow for an increase or decrease in face amount?
- Has it been determined, that prior to a reduction, that the client has sufficient protection inforce that meets their needs?
- If the face amount is decreased, will that lead to guideline premium force-outs? If so, it may make it difficult to fund the policy and keep it inforce.
- Will a decrease in face amount be considered a TAMRA reduction in benefits? If so, this may cause the policy to become a MEC.

When the goal is to reduce the cost of the policy

- Can dividends be used to reduce or pay the entire policy premium?
- Can cash value of PUAs be used to pay the policy premium?
- How long will the policy last if premiums are no longer paid?
- How long will the policy last with reduced premium?
- Is there a secondary guarantee such as lapse protection rider or no-lapse guarantee that may be affected by paying a lower premium?
- Can the face amount be reduced to reduce or eliminate premiums?

When the goal is to maximize living benefits of a policy

- How much inforce of the cash value is available for surrender and/or loan?
- What is the loan interest rate?
- What is the crediting rate for loaned funds?
- Is this a short term need for cash value?
- If withdrawals or loans are taken, will it affect any of the policy features?
- Are the riders available on the current policy (that would be lost) or on a new policy (that may be gained) which offer the insured or policyowner added benefits and features?
- Is the policy a MEC? Is there a secondary guarantee such as lapse protection rider or no-lapse guarantee that may be affected by taking loans or withdrawals?

1035 Worksheets

Worksheet to calculate taxable amount if loan is not carried to new policy

1	Total Policy Cash Value	______________________
2	Basis in Policy	______________________
3	Taxable Gain (Line 1 - Line 2)	______________________
4	Outstanding Policy Loan	______________________
5	Taxable Amount on 1035 (Enter the lesser of Line 3 and Line 4)	______________________

Example 1 - Taxable gain is more than loan

1	Total Policy Cash Value	$72,000
2	Basis in Policy	$51,000
3	Taxable Gain (Line 1 - Line 2)	$21,000
4	Outstanding Policy Loan	$17,000
5	Taxable Amount on 1035 (Enter the lesser of Line 3 and Line 4)	$17,000

Example 2 - Taxable gain is less than loan

1	Total Policy Cash Value	$72,000
2	Basis in Policy	$61,000
3	Taxable Gain (Line 1 - Line 2)	$11,000
4	Outstanding Policy Loan	$17,000
5	Taxable Amount on 1035 (Enter the lesser of Line 3 and Line 4)	$11,000

Final numbers are determined at the time of the assignment or 1035 exchange so the maximum loan, taxable amount, loan repayment or additional premium needed at issue may be changed.

Notes

Total Policy Cash Value – This is the account value or cash value before the loan has been deducted from it. Net cash value usually means that the number is less the loan whereas cash surrender value, gross cash surrender value or total cash surrender value usually means that it includes the loan. (Terminology can vary by company and product.) For example, if the cash surrender value is $25,000 and the outstanding loan is $30,000, the total policy cash value is $55,000.

Basis in Policy – This is the total premiums paid less policy withdrawals. Request this value from the life insurance carrier.

Taxable Gain – This is the amount the policyowner would report as taxable income if the policy was surrendered.

Outstanding Policy Loan – This is the total of the loan and any accrued interest due as of the date of the exchange.

1035 Worksheets cont.

Worksheet to determine 75% maximum loan limit

1	Total Policy Cash Value	______________
2	Additional Premium Paid at Policy Issue	______________
3	Total Policy Cash Value + Add'l Premium Paid at Issue (Line 1 + Line 2)	______________
4	Outstanding Loan	______________
5	Maximum Loan Allowed (Multiply Line 3 by .75)	______________

Example

1	Total Policy Cash Value	$83,000
2	Additional Premium Paid at Policy Issue	$0
3	Total Policy Cash Value + Add'l Premium Paid at Issue (Line 1 + Line 2)	$83,000
4	Outstanding Loan	$68,000
5	Maximum Loan Allowed (Multiply Line 3 by .75)	$62,250

Final numbers are determined at the time of the assignment or 1035 exchange so the maximum loan, taxable amount, loan repayment or additional premium needed at issue may be changed.

Worksheet to meet 75% test by paying down the existing loan in cash

1	Total Policy Cash Value	______________
2	Additional Premium Paid at Policy Issue	______________
3	Total Policy Cash Value + Add'l Premium Paid at Issue (Line 1 + Line 2)	______________
4	Outstanding Loan	______________
5	Maximum Loan Allowed (Multiply Line 3 by .75)	______________
6	Loan Repayment in Cash to Existing Policy (Line 4 – Line 5)	______________

Example

1	Total Policy Cash Value	$83,000
2	Additional Premium Paid at Policy Issue	$0
3	Total Policy Cash Value + Add'l Premium Paid at Issue (Line 1 + Line 2)	$83,000
4	Outstanding Loan	$68,000
5	Maximum Loan Allowed (Multiply Line 3 by .75)	$62,250
6	Loan Repayment in Cash to Existing Policy (Line 4 – Line 5)	$5,750

Worksheet: Meet 75% by paying additional premium at policy issue

1	Total Policy Cash Value	______________
2	Outstanding Loan	______________
3	Additional Premium Paid at Policy Issue [(Line 2/.75) – Line 1)]	______________

Example

1	Total Policy Cash Value	$83,000
2	Outstanding Loan	$68,000
3	Additional Premium Paid at Policy Issue [(Line 2/.75) – Line 1)]	$7,667

Final numbers are determined at the time of the assignment or 1035 exchange so the maximum loan, taxable amount, loan repayment or additional premium needed at issue may be changed.

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When a client considers a 1035 exchange, they need to review all aspects of the exchange that include, but are not limited to, new surrender change schedule, different features and benefits, insurance charges, loads, mortality and expense charges for variable contract, administrative charges, charges for additional riders.

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