



# DUE CARE BULLETIN

January 2010

## An Overview of Whole Life Versus Universal Life

The debate regarding the benefits of Whole Life (WL) vs. Universal Life (UL) began when UL was introduced in the early 1980s. This debate—waged by loyal advocates for each respective product—has continued ever since. This M Due Care Bulletin will compare these two different life insurance products, including illustrated performance comparisons.

*Life insurance due care requires an understanding of the factors that impact policy performance and drive product selection.*

*M Financial Group continues to lead the industry in life insurance due care and client advocacy, providing valuable insight and analysis that delivers significant value to clients.*

### Key Comparison points:

#### **Insurance Building Blocks (Mortality, Interest, Expense, and Persistency)**

- ❑ The building blocks for each product are identical.
- ❑ Therefore resulting policy performance will be similar if the experience fundamentals are identical (i.e., the different product mechanics don't necessarily drive better product performance).

#### **Policy Contract and Mechanics**

- ❑ WL and UL have different policy contracts and mechanics.
- ❑ WL uses non-guaranteed dividends to pass on current experience to policyholders, while UL uses current assumption credits and charges to reflect current experience.
- ❑ UL product mechanics are transparent, while WL product mechanics are “black box”. Transparency allows for a better understanding of policy performance and an ability to review/audit performance.

#### **Premium Flexibility**

- ❑ WL has limited premium flexibility which requires conservative funding levels that always endow the policy.
- ❑ UL provides premium flexibility, including the ability to fund more conservatively like WL, but also the ability to fund at lower levels, such as targeting \$1 of cash value at age 120.

#### **Coverage Flexibility**

- ❑ WL requires lifetime coverage, and will not allow the contract to lapse if dividends are reduced or premiums are not paid. Either additional premiums are required or the death benefit is reduced in order to maintain coverage for life.
- ❑ The coverage period for UL is flexible. Funding for less than lifetime coverage is possible. If charges or interest credited worsen, additional premiums or a reduced face amount are not required to maintain coverage for life. The UL contract simply allows the policy to lapse (i.e., coverage terminates) when the account value goes to zero.

In summary, the drivers of policy performance for WL and UL, and the actual performance results, are similar; however, UL provides greater flexibility in premium funding and coverage.

## Overview of Whole Life vs. Universal Life (continued)

Refer to the M Due Care Bulletin—“An Assessment of Whole Life Versus Universal Life”—for a more detailed comparison of WL and UL. The analysis includes a review of product mechanics and illustrated performance comparisons, as well as a summary of relative strengths and challenges.

### Illustrated Performance Comparisons

#### Premium Comparison:

Per the example below, the required premium solve (\$49,513) for the WL product may be considered conservative as it ends up endowing the policy at age 110. WL does not provide the flexibility to fund at a lower level (such as \$1 of cash value at age 120). When assuming the same target as WL for endowment at age 110, the M proprietary UL product premium is \$44,393, a 10% reduction from the WL premium. But UL can fund lower; for example, when solving for \$1 of cash value at age 120, the resulting premium (\$40,454) is 18% less than the WL premium.

#### Scenario Specifications:

- Male, Age 55, Best Nonsmoker Class
- \$2 million Level Death Benefit
- Decreasing term for WL, which achieves a level death benefit in all year
- Current non-guaranteed assumptions, including current dividend scale for the WL product
- Products: Whole Life from a non-M carrier and an M proprietary UL product

#### Annual 10-Pay Premium

Carrier	Product	Target	Premium \$	% Diff*
Carrier A	Whole Life	Required - Endow Age 110	49,513	
M Carrier	Proprietary UL	Endow Age 110	44,393	-10.3%
M Carrier	Proprietary UL	\$1 Age 120	40,454	-18.3%

\*Percentage change in premium from WL premium

### Evaluation of Downside Risk with Lower UL Funding Levels - Reduced Interest Credited and Resulting Additional Premiums:

The example below quantifies the additional number of premiums needed when the interest rate assumption is reduced by 50 basis points (bps), 100 bps, or lowered to the guaranteed minimum interest rate. The additional premiums are solved in order to achieve the original target, such as endowing at age 110 or \$1 at age 120.

#### Additional Premiums with Lower Credited Interest

Product Funding Target	Whole Life Endow Age 110	Universal Life Match WL Prem	Universal Life Endow Age 110	Universal Life \$1 Age 120
10 Annual Premiums*	49,513	49,513	44,393	40,454
<u># of Premium Payments</u>				
Current Interest	10	10	10	10
50 bps Interest Drop	12	11	12	12
100 bps Interest Drop	13	12	14	13
Guaranteed Interest	26	18	22	20

\*Number of premium payments to obtain the original solve target

The two additional premium payments required when interest credited is lowered by 50 bps are virtually identical; however, M proprietary UL with funding at the higher WL level only requires one additional premium. For a 100

## Overview of Whole Life vs. Universal Life (continued)

bps interest crediting drop, the number of additional premiums needed increases to three, but again the higher WL funding level in the M proprietary UL product is slightly better at two additional premiums. When lowering credited interest to the guaranteed level, the proprietary UL product (when funding at the WL level) only requires eight additional premiums versus 16 for the WL product. Even the lower funding levels for M proprietary UL, both endow and \$1, require less additional premiums than WL (12 and 10 additional premiums, respectively).

As a result of this analysis, there does not appear to be better downside risk protection for WL, as compared to UL, due to higher funding levels. In fact, in this example, WL with term blending has more downside risk than UL.

### Cash Value Comparison:

To this point we have focused on premiums. Clearly UL has an advantage with premium flexibility, including the ability to fund at lower levels. But what about cash accumulation?

As seen in the example below, when funding at identical levels, cash accumulation is similar between the two products. The M proprietary UL product has slightly better early and late policy year surrender values through age 100, while WL has slightly better surrender values after policy year 10 and through policy year 30. The M proprietary UL product does have significantly higher surrender values from attained age 100 and beyond.

Policy Year	Age	Whole Life	Universal Life
10 Annual Premiums		49,513	49,513
<b>Surrender Values</b>			
1	55	17,543	32,355
5	59	194,573	230,652
10	64	523,567	557,506
20	74	855,484	795,786
30	84	1,252,307	1,116,922
40	94	1,603,611	1,654,130
50	104	1,810,134	2,735,520
60	114	2,295,137	4,582,472

### Illustrated Performance Comparison Conclusion

WL and UL illustrated policy performance is similar when funding at identical levels. But UL provides premium flexibility to fund at lower levels. The lower funding levels offered by UL do not appear to provide worse downside risk protection than WL.

Refer to M's Due Care Bulletin "An Assessment of Whole Life versus Universal Life," for a more detailed look at product mechanics and additional performance comparisons.

Refer to the M Due Care Bulletin—"Comparing WL and UL: Common Questions and Answers,"—for additional information about product similarities/differences, myths, and relative strengths/challenges.

## For More Information

To learn more, please contact:

Jeffrey D. Dattolo  
CFP, CLU, ChFC  
Partner  
908.603.1256  
jdattolo@  
AtlasAdvisoryGroup.com

Atlas Advisory Group, LLC  
21 Commerce Drive, Suite 301  
Cranford, NJ 07016  
908.276.0096  
908.276.0038 Fax