Begin with the End in Mind:

Summer 2020 Permanent Life Insurance Pricing & Product Selection Review

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INTRODUCTION

Too often life insurance cases of significant size arrive as a solution looking for a problem. If we do not truly match the product solution to the problem rather than the other way around, we do the client a disservice.

In this paper, I highlight a few key pricing and feature advantages of two Universal Life and two Participating Whole Life products.

In the past few years, there have been dramatic changes in products being offered and consolidation of major carriers mixed in with times of unprecedented uncertainty. Each carrier and product carries its own advantages and weaknesses, but the key takeaway is that there is no one-size solution.

In the end, what is required even before choosing an insurance carrier and starting underwriting is to determine what outcome we are aiming for. Then we should perform a market survey to determine that the carrier and product recommended is the best fit and value. That said, I will summarize a few guidelines for best use cases.

METHODOLOGY

The review done here considers four different permanent cash value life insurance products.

I used Manulife's very well-priced InnoVision Universal Life YRT85/15 product that has a guaranteed payment period to age 85 or 15 years, whichever is greater. I used Canada Life's 10 Pay Universal Life since they have market-leading pricing there. Selecting a carrier to use to illustrate Participating Whole Life options can be trickier. I have used Canada Life here since their lower posted dividend scale interest rate (DSIR) of 5.1% is more conservative. Other carriers with higher advertised DSIRs may have higher investment return assumptions baked into their pricing. It is key to know that it is not the actual DSIR but the difference between the assumed and actual DSIR that drives actual dividends paid along with the assumptions around mortality, expenses, and policy lapses.

There are dozens of insurance products in the market. This analysis is for illustrative purposes only. It is not meant to be exhaustive for all products and carriers but part of a series of whitepapers comparing a range of possible scenarios.

For the purposes of comparison, I considered:

- Male, non-smoker in 5-year increments from 40 to 70 as of 2 July 2020
- Marginal tax rate of 49.80%
- $100,000 annual premium for ten years
- Solve for the maximum death benefit available based on these premiums

- For Whole Life
  - Maximum additional deposit options while maintaining tax-exempt status
  - Premium Offset After Year 10, where policy dividends pay the required premiums
  - Dividend Option: Term Enhancement, then Paid Up Additions
  - Assumed dividend scale interest rate -1% of current
  - Products: Canada Life Estate Select to Age 100, Maximum ADO (**ES100**) – delayed cash value
  - Canada Life Wealth Select to Age 100, Maximum ADO (**WS100**) – early cash value
- For Universal Life
  - Maximum death benefit that can be funded based on the ten premiums without using a taxable side account
  - Account value growth of 1.5% based on the minimum guaranteed return for a 10-year guaranteed investment account
  - Products:

  - Manulife InnoVision Yearly Renewable Term to Age 85/Year 15, Level Death Benefit and Valued Client Bonus (**YRT85**)
  - Canada Life 10-Pay Universal Life, Death Benefit Face Value plus Cash Value (**UL10p**)

The key metrics considered were:

- Total death benefit at age 90
- Capital Dividend Account at age 90
- Cash Value at Year 10

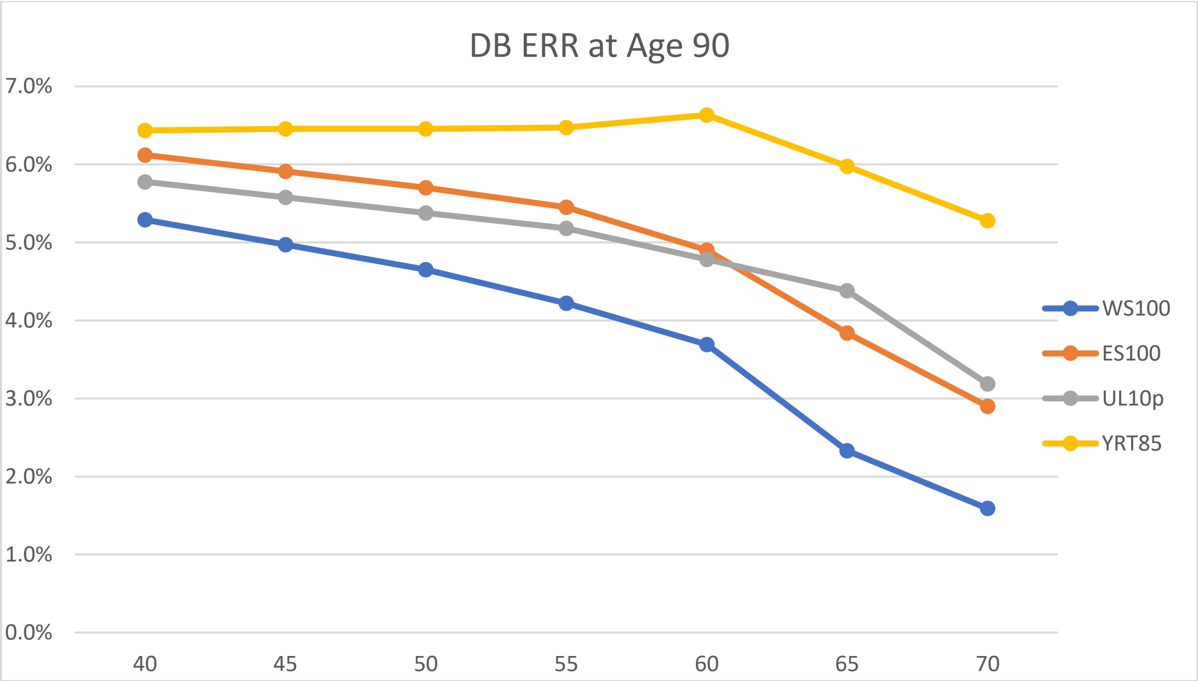
To evaluate these metrics, I consider the effective rate of return that would be required on an alternate investment (ERR) at the specified marginal tax rate. To reach this figure, I first calculate the internal rate of return (IRR), namely the discount rate or interest rate that will bring to zero the net present value (NPV) of the premiums paid for the corresponding death benefit or cash value. Then the IRR is grossed up by the marginal tax rate [ERR = IRR / (1-MTR)].

KEY FINDINGS

Best return for Death Benefit?

Surprise, surprise: YRT is back

When running the analysis based on the death benefit ERR at age 90, I was genuinely surprised by the strength of the InnoVision YRT85/15 product from Manulife. Perhaps this is an assumption held over from the days of YRT policies with funding problems caused by failing to meet the aggressive account growth assumptions made at policy issue. We avoid any sensitivity to the growth assumption by using the 1.5% guaranteed interest rate offered as well as a YRT policy with a limited payment horizon. While part of the strength of this product is clearly the very strong pricing by Manulife, it also performs well with other carriers. This is of course influenced by recent pricing increases in level cost and limited pay universal life.



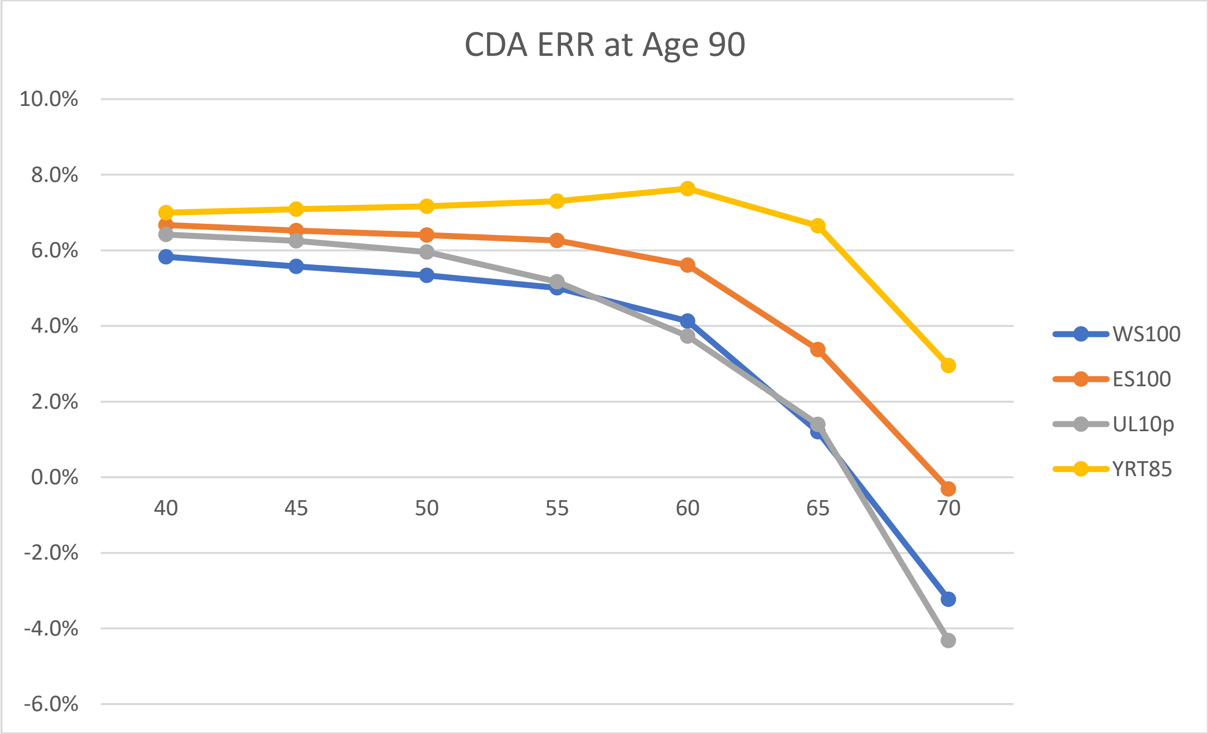
There is a key crossover date between age 60 & 65 where the runner-up position switches from the Estate Select product to the UL 10 pay, but at these ages the gap between the YRT85 product is even wider than for younger insureds. Clearly, if the only metric of consideration is achieving the most death benefit for the premiums paid, YRT85 should be considered.

Best return for Capital Dividend Account?

YRT again

When considering an insurance product that will be owned and paid for by a corporation with a corporate beneficiary, it is important to consider the Capital Dividend Account. As a refresher, the Capital Dividend Account of a corporation is increased by the amount the Death Benefit exceeds a policy's Adjusted Cost Base. The capital dividend account can be paid out as a tax-free capital dividend to shareholders of the corporation so can be an extremely powerful tool for estate planning when a corporation is involved. Since the calculations that change the adjusted cost base vary depending on the product, the ERR considering the CDA does not perfectly match the ERR for the Death Benefit.

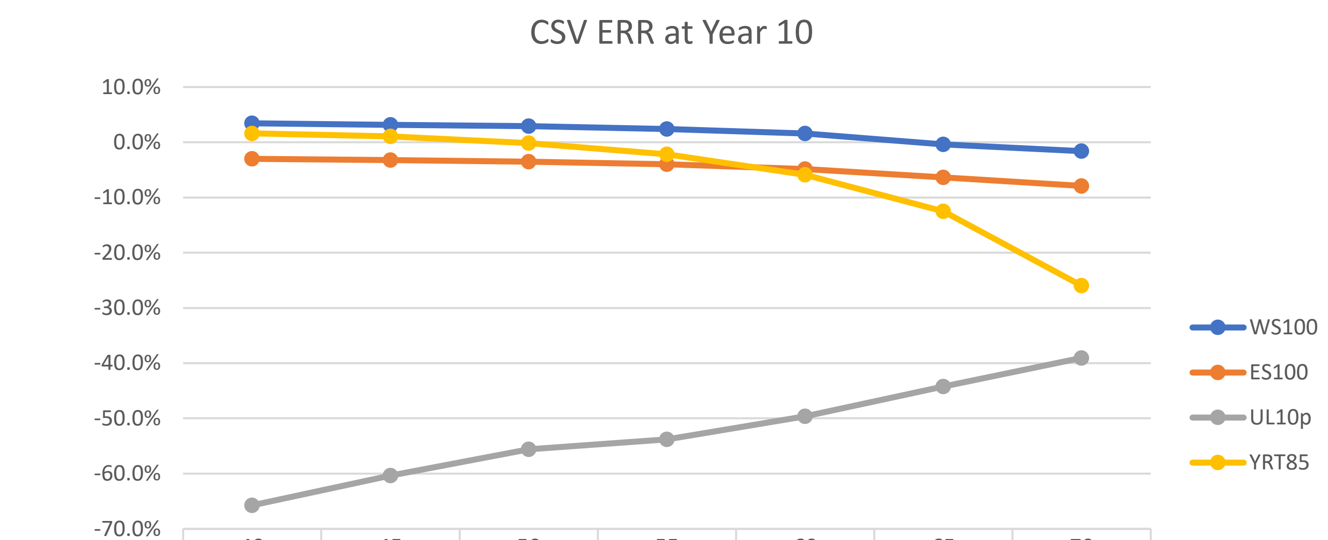
Once again, the YRT product performs the strongest in all ages considered while this time the Estate Select delayed cash value whole life product is the runner-up.



Best return on Early Cash Surrender Value?

Unsurprisingly, Wealth Select is best

This is the result I expected. This product was recently relaunched with even stronger early cash values. After just the first policy year, the cash values are between 87% and 70% of the premiums paid. This can make sense in scenarios where client want to maintain access to the premiums paid or maintain the strength of their balance sheet. While ERRs in the low single digits are not necessarily compelling, they can outperform a client's fixed-income investments with current low interest rates, especially when the other reasons to hold an insurance policy are considered.



	40	45	50	55	60	65	70
WS100	3.4%	3.1%	2.9%	2.4%	1.6%	-0.4%	-1.6%
ES100	-3.0%	-3.2%	-3.5%	-4.0%	-4.9%	-6.3%	-7.9%
UL10p	-65.7%	-60.4%	-55.6%	-53.8%	-49.6%	-44.2%	-39.0%
YRT85	1.6%	1.0%	-0.2%	-2.2%	-5.9%	-12.5%	-26.0%

This type of policy can also be very useful when the cash value might be relied upon for future uses, through a policy loan or by using the it as collateral for a third-party loan such as an Immediate Financing Arrangement. If proceeds from a third-party loan are invested in a business or to earn investment income, this may make both the loan interest and a portion of the insurance costs deductible. While outside the scope of this analysis, higher cash value policies can increase the value of the corporate shares owned by the deceased shareholder on the terminal tax return. This can be mitigated through other estate planning strategies such as separate corporate shares entitled to the insurance benefit.

COUNTERFACTUALS

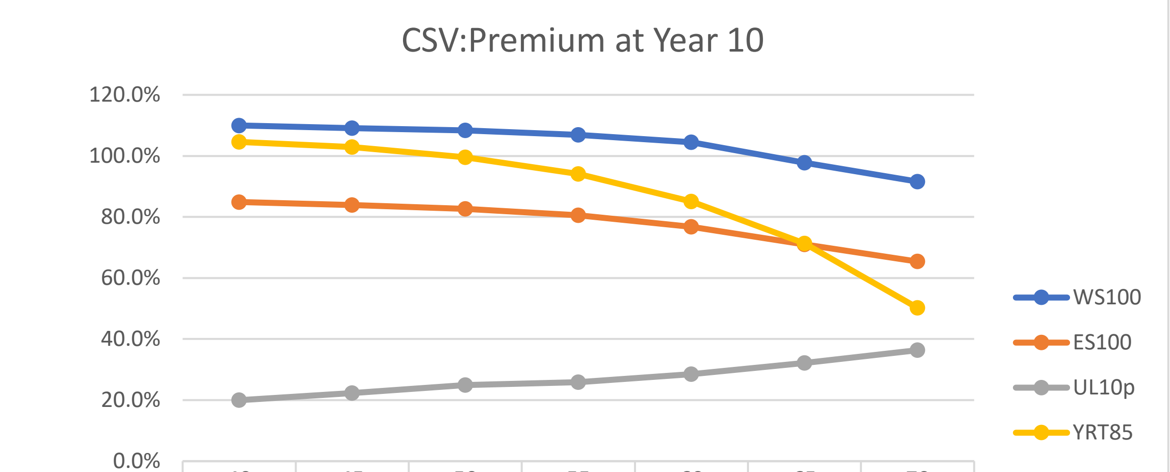
So YRT85 in most cases?

Contrary to the overall strengths of the YRT on the above metrics, it's worth noting that while the YRT85 shows as reasonably competitive with the Wealth Select option in the younger policy years in terms of the cash value, it can be more difficult to access the cash value in these policies. Since the face amount is level, any withdrawals of the policy's cash value result in a proportional reduction in the policy's death benefit. There may be some ability to borrow against the cash value inside the policy in early years, but since the policy's cost of insurance increases annually and depletes by the end of the plan, this could be problematic as well.

In addition, since the death benefit of the YRT85 plan is level, additional premiums paid do not go toward increasing the death benefit. The death benefit also does not increase through time, which lacks some of the inflation-protection offered by other policy options. Additionally, should the client have unforeseen additional insurance needs down the road, additional underwriting would be required. With the whole life policies, the client could opt to return to making policy premium payments instead of relying on the dividends to pay policy premiums. With the 10-Pay UL policy, the client could make additional premium deposits up to the tax limits on the policy, which would increase the death benefit. While there is not the same "bang for the buck" here, it still has strong estate planning uses.

I also may have understated how many clients who are considering insurance policies of significant size greatly value keeping access to the cash value inside a policy. It can also help their investment advisor take more risk elsewhere in their portfolio knowing that there is a solid vested cash value that experiences returns akin to fixed-income ones. Some clients compare the lower ERR on the Death Benefit with the ready access to a significant portion of the premiums paid as a reasonable price to pay for this flexibility.

Consider the table here that shows the percentage of the policy cash surrender value compared to the total premium paid after ten years. This balance sheet performance can sometimes trump other considerations



	40	45	50	55	60	65	70
WS100	110.0%	109.1%	108.4%	106.9%	104.4%	97.8%	91.6%
ES100	84.9%	83.9%	82.6%	80.6%	76.8%	71.0%	65.4%
UL10p	20.0%	22.3%	24.9%	25.9%	28.5%	32.1%	36.4%
YRT85	104.6%	102.9%	99.5%	94.1%	85.0%	71.3%	50.2%

CONCLUSION

In review, it is essential to dig down to what estate planning need is being addressed through an insurance policy. Policy preferences and rules of thumb can become outdated over time. So too, can preferred insurers as premium costs change through time.

With that in mind, YRT85 pricing should once again be given serious consideration, especially if the amount of death benefit need is fixed and the client does not expect to have need of accessing the policy's cash value. Unsurprisingly, choosing a product with a very high early cash value can have negative impacts on the other features of the policy but can still be compelling when balance sheet and insurance lending implications are considered.

Key Takeaways

- Best return for Death Benefit? Manulife InnoVision YRT85/15
- Best return for Capital Dividend Account? Manulife InnoVision YRT85/15
- Best return on Early Cash Surrender Value? Canada Life Wealth Select 100 with Max ADO

ABOUT EVOLUTION STRATEGIES

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Evolution Strategies is founded on a deep commitment to redefine the delivery of estate and legacy planning. We believe our industry should be focused on delivering impartial, holistic advice that ensures all your plans – from your taxes to your investments and your estate – are working together. Backed by 35+ years of experience, we dedicate our energy to looking at our clients' wealth transfer goals with an independent lens, and ultimately making your wealth matter.

We create fully transparent, family-focused strategies that safeguard your wealth, communicate your values, and create your legacy.

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Jesse Martyn's philosophy on estate and legacy planning is firmly rooted in the view that legacies fail when the values, life experiences, social connections, and beliefs that helped older generations succeed aren't passed along with a financial inheritance.

Jesse found his way into financial services somewhat indirectly — after a decade as a professional actor. He uses his inherent creativity balanced with his practical and analytical mindset to take a rare holistic approach to his clients' estate matters.

As the lead technical expert on the Evolution Strategies team, he works with clients and their trusted advisors to empower business owners and families to preserve, transfer, and grow their wealth, values, and knowledge for generations to come.

Jesse is a Certified Financial Planner® and Chartered Life Underwriter. He's driven by his values of Security, Happiness, Integrity, Health, and Environment.

APPENDIX

Death Benefit at Age 90 ERRs

Age 90 DB ERR	Product			
Age	WS100	ES100	UL10p	YRT85
40	5.3%	6.1%	5.8%	6.4%
45	5.0%	5.9%	5.6%	6.5%
50	4.7%	5.7%	5.4%	6.5%
55	4.2%	5.5%	5.2%	6.5%
60	3.7%	4.9%	4.8%	6.6%
65	2.3%	3.8%	4.4%	6.0%
70	1.6%	2.9%	3.2%	5.3%

Capital Dividend Account at Age 90 ERRs

Age 90 CDA ERR	Product			
Age	WS100	ES100	UL10p	YRT85
40	5.8%	6.7%	6.4%	7.0%
45	5.6%	6.5%	6.2%	7.1%
50	5.3%	6.4%	6.0%	7.2%
55	5.0%	6.3%	5.2%	7.3%
60	4.1%	5.6%	3.7%	7.6%
65	1.2%	3.4%	1.4%	6.7%
70	-3.2%	-0.3%	-4.3%	3.0%

CSV at Year 10 ERRs

Yr 10 CSV ERR	Product			
Age	WS100	ES100	UL10p	YRT85
40	3.4%	-3.0%	-65.7%	1.6%
45	3.1%	-3.2%	-60.4%	1.0%
50	2.9%	-3.5%	-55.6%	-0.2%
55	2.4%	-4.0%	-53.8%	-2.2%
60	1.6%	-4.9%	-49.6%	-5.9%
65	-0.4%	-6.3%	-44.2%	-12.5%
70	-1.6%	-7.9%	-39.0%	-26.0%

CSV as % of Premiums Paid at Year 10

Yr 10 CSV ERR	Product			
Age	WS100	ES100	UL10p	YRT85
40	3.4%	-3.0%	-65.7%	1.6%
45	3.1%	-3.2%	-60.4%	1.0%
50	2.9%	-3.5%	-55.6%	-0.2%
55	2.4%	-4.0%	-53.8%	-2.2%
60	1.6%	-4.9%	-49.6%	-5.9%
65	-0.4%	-6.3%	-44.2%	-12.5%
70	-1.6%	-7.9%	-39.0%	-26.0%

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