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Drivers of the UL/IUL Market: Regulatory Changes, Living Benefits and Low Interest Rates

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Universal life (UL) products continue to be an important part of the individual life insurance market, despite the slight decline recently in the total life insurance market share (based on annualized premium). Over the past several years, sales of indexed UL (IUL) generally and of UL/IUL products with living benefit riders have driven total UL/IUL sales growth. The UL/IUL market share (measured by annualized premium) of total individual life sales was 37 percent[1] as of March 31, 2016. The IUL share of UL annualized premium had grown to 56 percent of total UL/IUL sales in the first quarter of 2016.[2]

Milliman's ninth annual survey of leading UL/IUL insurers revealed industry information relative to the issues and challenges of these products. For purposes of the survey, sales were defined as the sum of recurring premiums plus 10 percent of single premiums. The scope of the Milliman survey included UL with secondary guarantees (ULSG), cash accumulation UL (AccumUL), current assumption UL (CAUL), and the IUL counterparts of these products. The definition of these product types is shown below.

UL/IUL with secondary guarantees. A UL/IUL product designed specifically for the death benefit guarantee market that features long-term no-lapse guarantees (guaranteed to last until at least age 90) either through a rider or as a part of the base policy.

Cash accumulation UL/IUL. A UL/IUL product designed specifically for the accumulation-oriented market where cash accumulation and efficient distribution are the primary concerns of the buyer. Within this category are products that allow for high-early-cash-value accumulation, typically through the election of an accelerated cash value rider.

Current assumption UL/IUL. A UL/IUL product designed to offer the lowest-cost death benefit coverage without death benefit guarantees. Within this category are products sometimes referred to as "dollar-solve" or "term alternative."

A new high of 35 carriers submitted responses to t he survey relative to their UL/IUL products. The key findings of the survey are summarized in this article.

UL SALES

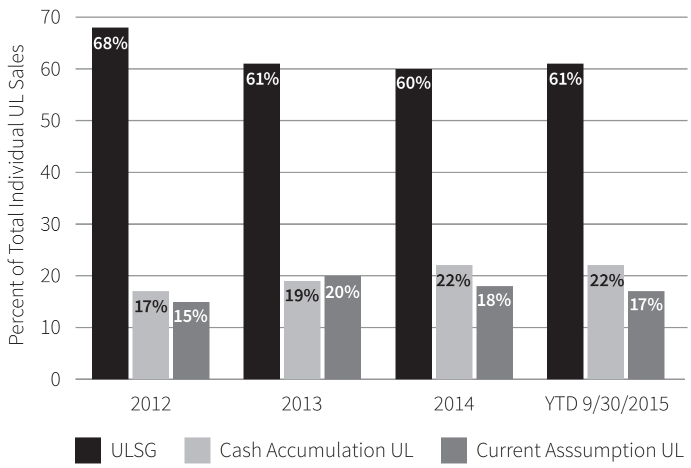
The mix of UL sales (excluding IUL sales) reported by survey participants for calendar years 2012 through 2014, and for 2015 as of Sept. 30, 2015 (YTD 9/30/15), is shown in Figure 1. Individual company UL sales results were varied, but 11 participants reported at least a 10 percent shift from or to any one UL product when looking at the YTD 9/30/15 product mix relative to that of 2012. Five of the 11 participants reported movement to CAUL products, two to AccumUL products only, another two to both AccumUL and CAUL products, and the remaining two to ULSG products. Four participants discontinued sales of ULSG products; one discontinued AccumUL products; and another discontinued CAUL products. Two participants began selling AccumUL products.

New to the survey was the reporting of sales by 7702 option and death benefit option for calendar year 2014 and YTD 9/30/15. For both periods, about 70 percent of total individual UL sales used the cash value accumulation test (CVAT) and about 30 percent used the guideline premium test (GPT). Virtually all ULSG sales were with death benefit option A for both CVAT and GPT designs. AccumUL had the highest percentage of sales for death benefit option B, for both CVAT and GPT policies. However, this allocation was higher for GPT designs versus CVAT designs, measured both by premiums and face amount.

INDEXED UL SALES

For survey participants, IUL sales during YTD 9/30/15 accounted for 51 percent of total UL/IUL sales combined during YTD 9/30/15, increasing from 37 percent in 2012. AccumIUL sales increased from 71 percent to 81 percent of

Figure 1
UL Product Mix by Year



total cash accumulation UL/IUL sales. IULSG and CAIUL sales, as a percent of total combined sales, decreased over this period. IUL products continue to be an attractive option in the recent low interest rate environment due to policyholders' interest in the upside potential and downside protection offered by these products.

Similar to responses in the past, overall survey statistics suggest that companies plan to focus more on cash accumulation IUL and current assumption IUL products and less on ULSG. The graph in Figure 2 illustrates the IUL product mix and the significance of AccumIUL products within the IUL market.

LIVING BENEFIT RIDER SALES

In recent years, triggers for accelerated death benefits (ADBs) on individual life insurance policies have been expanded from terminal illness to chronic illness and long-term care (LTC). Under chronic illness riders, payment of the death benefit may be accelerated if the insured has a chronic illness condition. Requirements to trigger the benefit typically utilize a combination of activities of daily living (ADLs) and cognitive impairment, or permanent nursing home confinement. For LTC accelerated benefit riders, payment of the death benefit is accelerated if the insured has a chronic illness condition (i.e., ADLs or cognitive impairment) triggering LTC.

Three common approaches are used for the payment of chronic illness ADBs. Under the discounted death benefit approach, the insurer pays the owner a discounted percentage of the face amount reduction, with the face amount reduction occurring at the same time as the accelerated benefit payment. This approach avoids the need for charges up front or other premium requirements for the rider, because the insurer covers its costs of early payment of the death benefit via a discount factor. Eight of the 15 participants that reported UL/IUL sales with chronic illness riders provided a discounted death benefit as an accelerated benefit.

Another three participants reported their chronic illness riders used a lien against the death benefit to provide the accelerated benefit, and two survey participants used a dollar-for-dollar death benefit reduction approach. The final two participants used both the lien approach and dollar-for-dollar death benefit reduction approach. Under the lien approach, the payment of ADBs is considered a lien or offset against the death benefit. Access to the cash value (CV) is restricted to any excess of the CV over the sum of the lien and any other outstanding policy loans. Future premiums/charges for the coverage are unaffected, and the gross policy values continue to grow as if the lien didn't exist. In most cases there are lien interest charges that are assessed under this design.

Under the dollar-for-dollar approach, there is a dollar-for-dollar reduction in the specified amount or face amount and a pro rata reduction in the CV based on the percentage of the specified amount or face amount that was accelerated. This approach always requires an explicit charge.

During the first nine months of 2015 sales of policies with chronic illness riders as a percent of total sales were 23 percent for UL products and 41 percent for IUL products, at or near peak levels. A greater share of chronic illness riders was seen on an IUL chassis since more new IUL products have been developed recently, and many of these included a chronic illness rider. YTD 9/30/15 sales with chronic illness riders as a percent of

Figure 2
IUL Product Mix by Year

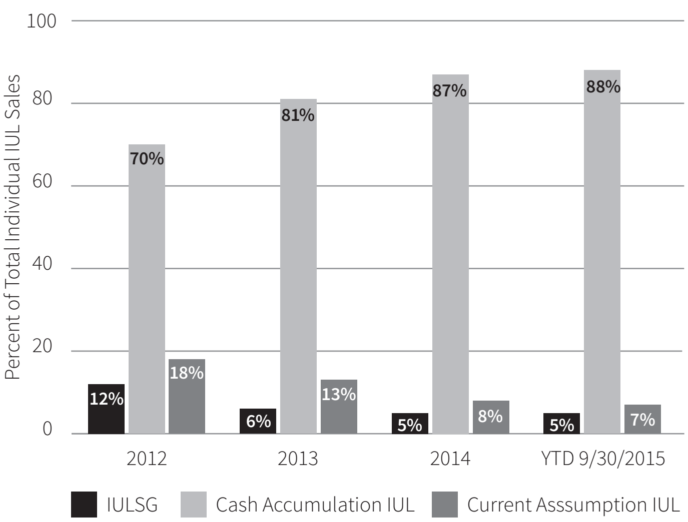


Figure 3
Chronic Illness Rider Sales as a Percentage of Total Sales

Ytd 9/30/15 UL Sales With Chronic Illness Riders As A Percent Of Total UL Sales (Weighted By Premium)			
Total Individual UL	ULSG	Cash Accumulation UL	Current Assumption UL
23%	24%	33%	9%
Ytd 9/30/15 IUL Sales With Chronic Illness Riders As A Percent Of Total IUL Sales (Weighted By Premium)			
Total Individual IUL	IULSG	Cash Accumulation IUL	Current Assumption IUL
41%	28%	41%	51%

total sales for UL and IUL products separately by product type are shown in the table in Figure 3.

Recently attention has been drawn to LTC needs due to the high cost of medical care and the aging population. An alternative solution to stand-alone LTC policies for LTC needs is the use of LTC riders attached to life policies, particularly UL/IUL policies (linked benefits). In the last three to four years there has been a shift away from single premium business to limited pay business. Thus, sales results by first-year premium are somewhat misleading. Despite this shift, during YTD 9/30/15, sales of policies with LTC riders as a percent of total sales were 19 percent for UL products and 9 percent for IUL products, both at peak levels. Figure 4 shows sales of LTC riders as a percent of total sales reported by survey participants for UL and IUL products separately by product type.

Few companies in the UL/IUL market offered both chronic illness riders and LTC riders; only three of the survey participants offered both chronic illness and LTC accelerated benefit riders. Nearly 83 percent of survey respondents expect to market either an LTC or a chronic illness rider within the next 24 months.

PROFIT MEASURES

Consistent with past survey responses, an after-tax, after-capital statutory return on investment/internal rate of return (ROI/IRR) was the predominant profit measure reported by survey participants. The median ROI/IRR was 10 percent for all UL products and IULSG, and was 12 percent for AccumIUL and CAIUL.

Actual results relative to profit goals were reported by survey respondents for 2014 and YTD 9/30/15. In 2014, 68 percent of ULSG participants reported they fell short of profit goals. For the remaining UL/IUL products, 69 percent of participants were at least meeting their profit goals. For YTD 9/30/15, 61 percent were short of their profit goals for ULSG, and 73 percent of participants were at least meeting their profit goals for all other UL/IUL products. The chart in Figure 5 shows the percentage of survey participants reporting they fell short of, met, or exceeded their profit goals by UL product type. Low interest earnings and expenses continued to be the top two reasons given for failure to meet profit goals.

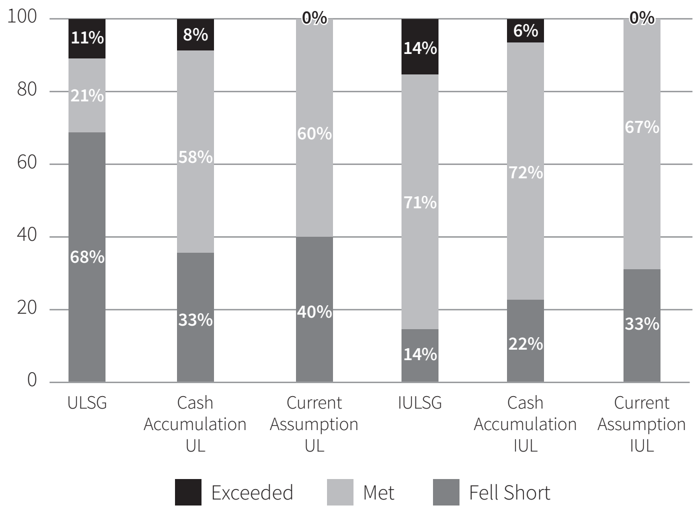
Figure 4
LTC Rider Sales as a Percentage of Total Sales

Ytd 9/30/15 UL Sales With LTC Riders As A Percent Of Total UL Sales (Weighted By Premium)			
Total Individual UL	ULSG	Cash Accumulation UL	Current Assumption UL
19%	30%	6%	< 1%
Ytd 9/30/15 IUL Sales With LTC Riders As A Percent Of Total IUL Sales (Weighted By Premium)			
Total Individual IUL	IULSG	Cash Accumulation IUL	Current Assumption IUL
9%	14%	9%	15%

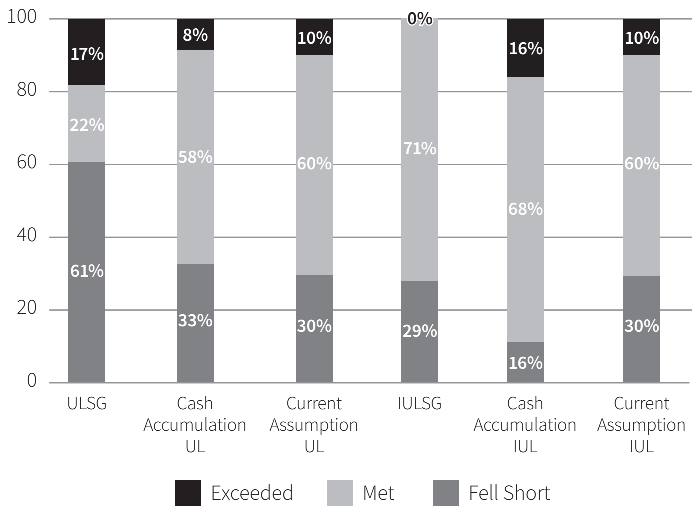
PRINCIPLE-BASED RESERVES

Principle-based reserves (PBR) will be effective Jan. 1, 2017, and nine survey participants reported they anticipate implementing PBR immediately. Nineteen expect phasing in the implementation of PBR over the three-year phase-in period allowed. Factors impacting the rationale for participants' implementation plans include resource issues, the impact on reserves and capital,

Figure 5
Actual Results Relative to Profit Goals



Actual YTD 9/30/15 Results Relative to Profit Goals



the need for preparation and research, and competitive reasons. Fifteen participants do not know what approach they will use for pricing new UL/IUL products in a PBR environment for products that require one of the VM-20 reserve components (VM-20 includes valuation manual minimum requirements for PBR for life insurance products). For the remaining participants, various responses were received including no changes to the reserve approach they currently use in pricing, reflecting VM-20 reserves in pricing, using a reduced subset of stochastic scenarios in pricing, and using approaches that estimate additional reserves.

ILLUSTRATIONS

The percentage of participants reporting that they are no longer illustrating non-guaranteed elements on ULSG products was 43 percent, down from 48 percent reported last year.

Eighteen of the 22 IUL participants reported the rate that was calculated for the Benchmark Index Account per Section 4A of Actuarial Guideline 49 (AG 49). The average rate was 6.72 percent and the median was 6.87 percent. Eight participants reported the rate for the hypothetical Benchmark Index Account, with an average of 6.99 percent and median of 7.05 percent.

Twenty of 22 survey participants reported that the illustrated rate used in IUL illustrations decreased relative to the illustrated rate of one year ago. The median illustrated rate was 6.70 percent and the average was 6.59 percent. This compares with the median illustrated rate one year ago of 7.50 percent, and an average of 7.10 percent. The majority of IUL participants (19) reported they had made adjustments to illustrations based on AG 49, but few participants had made changes to their product designs because of AG 49.

Survey participants reported whether they were currently testing in-force business or using Actuarial Standard of Practice (ASOP) 24 Section 3.7 to not test when certifying for illustration actuary testing on in-force business. ASOP 24 Section 3.7 applies to illustrations on policies in force one year or more. Thirteen of 34 participants reported they were currently using ASOP 24 Section 3.7 to not test when certifying for illustration actuary testing. Eleven participants were testing in-force business, and six were using both approaches.

The majority (27 of 35) of participants were doing sensitivity testing to see where the disciplined current scale (DCS) breakpoints are (i.e., when the DCS might fail).

Three participants reported they were illustrating utilization scenarios/examples for ADB riders with a discounted death benefit approach. One of the three, plus four additional participants were illustrating utilization scenarios/examples for other ADB riders. The majority of participants that were illustrating ADB utilization reported that the illustrations were in a supplemental illustration, rather than in the basic illustration.

CONCLUSION

Many trends in the UL/IUL market arise as a response to challenges presented by regulatory actions, economic issues and even health/aging issues. In recent years, this has included secondary guarantee issues, IUL popularity, and the development of living benefit riders. Who knows what the next bump in the road will be and what direction the UL/IUL market will take? It's important to follow industry trends, address challenges, and also take advantage of opportunities in order to stay competitive in the UL/IUL market.

A complimentary copy of the executive summary of the June 2016 Universal Life and Indexed Universal Life Issues report may be found at: *http://www.milliman.com/insight/2016/Universal-life-and-indexed-universal-life-issues--2015-survey/*. ■

ENDNOTES

1 LIMRA International, Inc.

2 Ibid.

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