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Universal Life and Indexed UL Current Trends and Reactions

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Results of Milliman's 10th annual survey of leading universal life (UL) and indexed UL (IUL) products have been compiled, revealing reactions to the various dynamics of this market. Thirty-two carriers submitted responses to the survey related to product and actuarial issues such as sales, profit measures, target surplus, reserves, risk management, underwriting, product design, compensation, pricing and illustrations.

The scope of the Milliman survey included UL with secondary guarantees (ULSG), cash accumulation UL (AccumUL), current assumption UL (CAUL), and the indexed UL (IUL) counterparts of these products. The definition of these product types is shown as follows:

- 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 efficient accumulation of cash values to be available for distribution is the primary concern 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."

Highlights of the key findings of the survey are summarized in this article.

UL SALES

The graph in Figure 1 illustrates the UL product mix (excluding IUL sales) as reported by survey participants from calendar years 2013 through 2015, and for 2016 as of Sept. 30, 2016 (YTD 9/30/16). For purposes of the survey, sales were defined as the sum of recurring premiums plus 10 percent of single premiums. Relative to prior survey results, fewer participants reported significant shifts in their UL product mix when comparing the mix at the end of the survey period to that of the beginning of the survey period.

INDEXED UL SALES

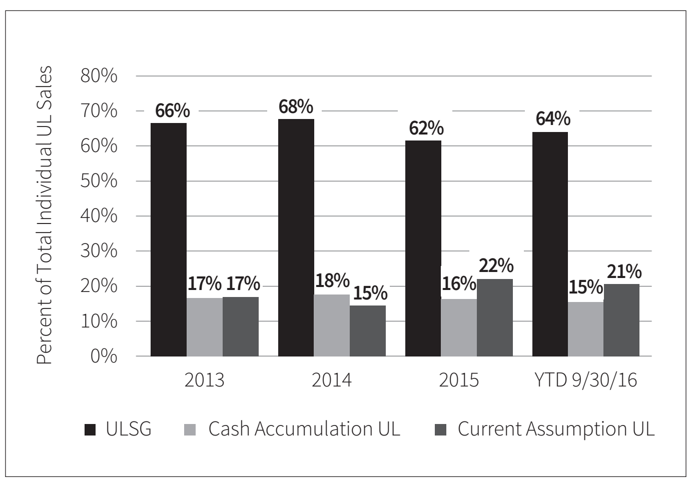
For survey participants, IUL sales during YTD 9/30/16 accounted for 49 percent of total UL/IUL sales combined during YTD 9/30/16, increasing from 34 percent in 2013. Also, the IUL sales percent increased for AccumIUL sales from 2013 to YTD 9/30/16 from 71 percent to 79 percent of total cash accumulation UL/IUL sales. IULSG also increased from 5 percent to 8 percent of total combined ULSG/IULSG sales over the survey period. CAIUL sales, as a percent of total combined CAUL/CAIUL sales, decreased from 32 percent to 30 percent over this period. Similar to responses in the past, overall survey statistics suggest that in the future participants plan to focus more on IUL products, especially AccumIUL, and on CAUL products.

The graph in Figure 2 illustrates the IUL product mix and the significance of AccumIUL products within the IUL market.

LIVING BENEFIT RIDER SALES

Seven of the 12 participants that reported UL/IUL sales with chronic illness riders provide a discounted death benefit as an accelerated benefit. 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

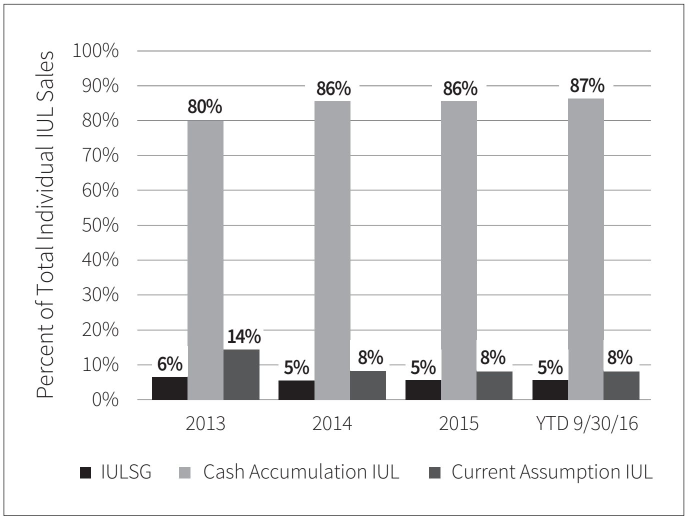
Figure 1
Ul Product Mix by Year



premium requirements for the rider, because the insurer covers its costs of early payment of the death benefit via a discount factor.

Another two participants reported their chronic illness rider uses a lien against the death benefit to provide the accelerated benefit, and one participant uses a dollar-for-dollar death benefit reduction approach. The final two participants use both the lien approach and dollar-for-dollar death benefit reduction approach. Under the lien approach, the payment of accelerated death benefits 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.

Figure 2
IUL Product Mix by Year



During YTD 9/30/16, sales of policies with chronic illness riders as a percent of total sales were 15.8 percent for UL products and 35.5 percent for IUL products. Because more new IUL products have been developed recently, and many included a chronic illness rider, we see a greater share of chronic illness riders on an IUL chassis. The table in Figure 3 shows YTD 9/30/16 sales with chronic illness riders as a percent of total sales for UL and IUL products separately by product type.

The use of long-term care (LTC) riders attached to life insurance policies, particularly UL/IUL policies, has become an alternative solution to stand-alone LTC policies. This is an important trend to address LTC needs due to the high cost of long-term care, the aging population and the exiting of some life insurers from the stand-alone LTC market. During YTD

Figure 3
Chronic Illness Rider Sales As A Percent Of Total Sales

Calendar Year	Total Individual UL	ULSG	Cash Accumulation UL	Current Assumption UL
UL Sales With Chronic Illness Riders As A Percent Of Total UL Sales				
2013	15.8%	19.1%	9.3%	9.1%
2014	15.5%	18.3%	11.6%	7.2%
2015	14.6%	18.4%	14.9%	3.9%
YTD 9/30/16	15.8%	18.5%	18.8%	5.0%
Calendar Year	Total Individual IUL	IULSG	Cash Accumulation IUL	Current Assumption IUL
IUL Sales With Chronic Illness Riders As A Percent Of Total IUL Sales				
2013	30.3%	10.2%	34.4%	15.9%
2014	31.7%	26.0%	32.7%	25.1%
2015	33.1%	29.6%	34.3%	22.1%
YTD 9/30/16	35.5%	39.1%	36.7%	19.5%

Figure 4
LTC Rider Sales as a Percent of Total Sales by Premium

Calendar Year	Total Individual UL	ULSG	Cash Accumulation UL	Current Assumption UL
UL Sales With LTC Riders As A Percent Of Total UL Sales				
2013	16.4%	24.0%	1.6%	0.8%
2014	19.9%	28.9%	1.4%	0.3%
2015	22.3%	31.9%	2.1%	10.3%
YTD 9/30/16	24.0%	33.5%	1.0%	11.8%
Calendar Year	**Total Individual IUL**	**IULSG**	**Cash Accumulation IUL**	**Current Assumption IUL**
IUL Sales With LTC Riders As A Percent Of Total IUL Sales				
2013	9.5%	23.1%	8.6%	8.3%
2014	9.9%	20.5%	9.2%	10.0%
2015	10.6%	13.5%	10.5%	9.7%
YTD 9/30/16	9.8%	8.5%	9.6%	12.6%

9/30/16, sales of policies with LTC riders as a percent of total sales by premium were 24.0 percent for UL products and 9.8 percent for IUL products. Figure 4 shows sales of LTC riders as a percent of total sales (measured by premiums, and weighting single-premium sales at 10 percent) for UL and IUL products separately by product type.

PROFIT MEASURES

The predominant profit measure reported by survey participants is an after-tax, after-capital statutory return on investment/internal rate of return (ROI/IRR). This is consistent with what has been reported in past surveys. The average ROI/IRR target reported by survey participants was 9.9 percent for ULSG, 11.1 percent for AccumUL, 10.5 percent for CAUL, 10.1 percent for IULSG, 12.3 percent for AccumIUL and 12.8 percent for CAIUL.

The charts in Figures 5 and 6 shows the percentage of survey participants reporting that they fell short of, met or exceeded their profit goals by UL product type for calendar year 2015 and YTD 9/30/16, respectively. Of note is the percentage of participants that fell short of their profit goals for ULSG products: 50 percent in 2015 and 63 percent during YTD 9/30/16. As in the past, the primary reasons reported for not meeting profit goals were low interest earnings and expenses.

PRINCIPLE-BASED RESERVES AND THE 2017 CSO

Results from the survey indicate a staggered approach in implementing recent regulatory changes. Principle-based reserves (PBR) may be implemented as early as Jan. 1, 2017, and 27 survey participants reported they expect to implement PBR for all of their UL/IUL products gradually over the three-year phase-in period allowed. Resource issues, time needed, financial impact/cost/benefits, clarification/finalization of PBR/IRS regulations and PBR implementation of other product first were cited as factors impacting the rationale for implementation plans.

Similarly, the earliest effective date for the use of the 2017 Commissioner's Standard Ordinary (CSO) mortality table was

Figure 5
Actual Results Relative to Profit Goals for 2015

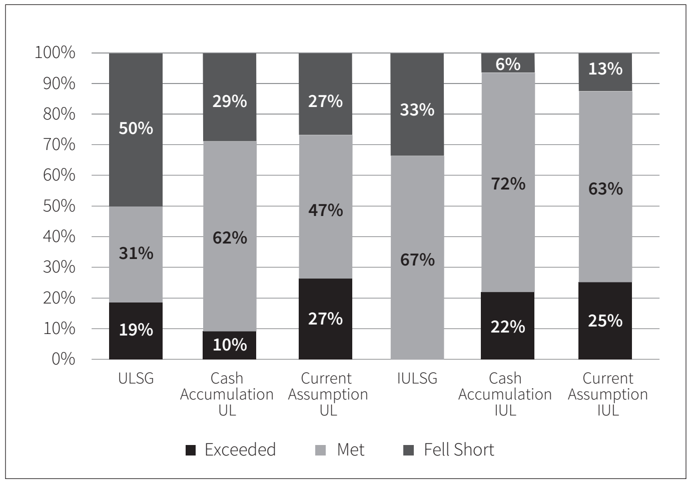
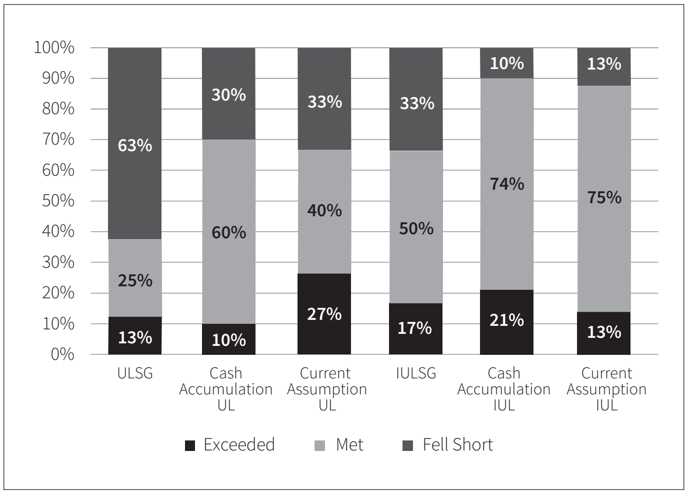


Figure 6
Actual Results Relative to Profit Goals for YTD 9/30/16



Jan. 1, 2017. The 2017 CSO is the new valuation mortality table to be used in the determination of CRVM (Commissioners Reserve Valuation Method), net premium reserves, tax reserves, minimum nonforfeiture requirements and so on. Twenty-two survey participants reported that they would implement this table for all of their UL/IUL products gradually over the three-year phase-in period allowed. Ten participants reported implementation of the 2017 CSO would be product dependent; implementation will be immediate for some products and over the three-year phase-in period for others.

It is not surprising that these regulatory changes are not being implemented immediately, given the complexity of the regulations, the potential impact on pricing and the bottom line, and the strain on resources, especially for smaller carriers.

In addition, 21 participants provided a rating of how effective they believe PBR will be in making reserve financing arrangements (e.g., captives) obsolete. Ratings are shown in the table in Figure 7. More participants believe PBR will be effective rather than ineffective in making reserve financing arrangements obsolete.

Figure 7
Effectiveness Ratings of PBR Making Reserve Financing Arrangements Obsolete

Rating	# Of Responses
Very Ineffective	0
Ineffective	4
Average	9
Effective	6
Very Effective	2

UNDERWRITING

The use of predictive modeling in the life insurance industry has recently gained attention. Predictive modeling utilizes statistical models that relate outcomes/events to various risk factors/predictors. Scoring models in life underwriting are an example of predictive modeling used in the life insurance space. Eleven survey participants use scoring models to underwrite their UL/IUL policies. Eight of the 11 use scoring models for fully underwritten policies, one uses them for simplified issue business, and the final two use them for both fully underwritten and simplified issue business. Eight participants reported using scoring models with automated rules.

The types of scoring models were reported by 10 of the 11 survey participants that use scoring models. In total, seven use lab scoring models, four use credit scoring models and five use scoring models relative to motor vehicle records (MVR).

ILLUSTRATIONS

The credited rate used in IUL illustrations for participants' most popular strategies decreased relative to the illustrated rate of one year prior for 10 of 21 survey participants. One participant reported no change in the illustrated rate, and eight reported increases in the illustrated rate. The median illustrated rate reported was 6.69 percent and the average was 6.58 percent.

The survey has included a number of questions relative to IUL illustrated rates and rates calculated under Actuarial Guideline 49 (AG 49) Section 4A and Section 4C. A new question

In future years, the implementation of PBR, the 2017 CSO table, and new underwriting approaches will likely have a more significant impact on the UL/IUL market than seen in recent years.

that was included in the survey this year asked participants to report the maximum illustrated rate that was allowed for the most popular strategy/investment choice within their IUL portfolio, both immediately pre-AG 49 and immediately post-AG 49. The pre-AG 49 rates ranged from 5.60 percent to 8.50 percent, with an average of 7.38 percent and a median of 7.65 percent. The post-AG 49 rates ranged from 5.02 percent to 7.75 percent, with an average of 6.69 percent and a median of 6.86 percent.

CONCLUSION

Trends in the UL/IUL market in recent years generally have been due to the popularity of indexed UL and continuing low interest rates, with some reaction to regulatory actions. In future years, the implementation of PBR, the 2017 CSO table, and new underwriting approaches will likely have a more significant impact on the UL/IUL market than seen in recent years. To remain competitive, and even to survive, in this market, it is critical for carriers to address the issues and opportunities that arise.

A complimentary copy of the executive summary of the May 2017 Universal Life and Indexed Universal Life Issues report may be found at: *http://us.milliman.com/insight/2017/Universal-life-and-indexed-universal-life-issues--2016-survey/*. ■

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