One of the most successful products in the current market is the death-benefit-focused UL. This type of product offers guaranteed lifetime protection (using a secondary guarantee and a maturity extension) at a very affordable price. Many companies have utilized a shadow account approach to make the guaranteed coverage even more affordable.

The shadow account is a value that is calculated similar to a UL cash value. However, the shadow account has its own set of charges. As long as the net shadow account value is positive, the policy will stay in force regardless of whether the cash value is sufficient to cover the insurance charges.

Pricing a product with a shadow account can be very difficult because of the need to reflect the reserves required under Guideline AX AXX. However, once the product is successfully priced, there is still the difficult task of getting the product to market. This task can be especially difficult for companies with legacy administrative systems.

Two Account Values
The biggest challenge to using a shadow account is calculating two separate account values: one for the shadow account and one for the actual cash value. When premiums are paid, they must be applied to both the shadow account and the cash value.

One approach is to use a single plan (policy record) that contains the charges for both the shadow account and the actual cash value. When premiums are paid, the plan calculates both the shadow account value and the actual cash value (See Figure 1).

This approach can be difficult because of the need to store two sets of charges. This can be especially difficult if the charges are vastly different. For example, actual COI charges may be on an attained age basis, but shadow charges could be select and ultimate.

Another option for keeping track of two account values is to use two plans. One plan contains the charges for the shadow account and one contains the actual charges used in calculating the cash value. In this case, the paid premiums are sent to both plans. The first plan calculates the shadow value and the second one the cash value (See Figure 2).

The biggest challenge under this approach is making sure both plans contain the same information. The same premium must be sent to both plans. Moreover, when a change is made to the policy, it must be made to both plans. Also, there must be a link between the two plans to indicate when the shadow account is no longer positive and the guarantee is no longer in effect.

Overall, there are difficulties with both approaches to calculating two separate account values.

Communication
Communicating the concept of a shadow account is another challenging endeavor. Several terms are used in the actuarial community that may not be appropriate when marketing to potential policyholders. For instance, the term “shadow” may suggest something secretive or deceptive, which is probably not the image that is desired. Moreover, referring to an “account value” may give the impression that the shadow account has a surrender value, which is not the case. Terms such as “balance” or “threshold” may be more appropriate.

Once the terminology is in place, the shadow account can be described to policyholders and agents. The shadow account calculations can be explained in great detail or the discussion can be limited to the guarantee provided by the shadow account. In either case, it is important for agents to be familiar with the unique features of a shadow account guarantee.

Policy Form
Since the shadow account provides a guaranteed death benefit, the policy form for the
shadow account must contain enough information so that the policyholder can reproduce the shadow account calculations. At least two approaches can be used to accomplish this goal:

1) Use the description of the cash value found in the base contract and describe any differences. This approach produces a shorter form, but can be confusing if there are a lot of differences between the shadow account calculations and the cash value calculations.

2) Describe all of the calculations from scratch, but apply them to the shadow account values. This approach takes up more space but is effective in separating the shadow account from the cash value.

When describing the charges that will be used in calculating the shadow account, it's again important to consider the terminology that will be used. Also, since these charges are guaranteed, they will need to be printed somewhere in the policy form. A separate schedule of charges can be included that applies only to the shadow account. This can help to distinguish between the guaranteed charges that apply to the actual Cash Values and the charges that are guaranteed for the shadow account calculations.

**Conclusion**

All in all, the process of administering and filing a shadow account product can be even more difficult than pricing the product. However, with hard work and creativity, it is possible to effectively market and administer a very competitive, complex product.

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