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UL Products with Lifetime Guarantees

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Insure your vision

Overview

- Post-AXXX Secondary Guarantee Product Development
  - Review of XXX and AXXX
  - Pricing Strategies
  - Reinsurance Availability
  - Other Financial Remedies
  - Competitive Environment

XXX Impact

- Under XXX it was expected that secondary guarantee designs would have to support traditional CRVM reserve levels similar to whole life contracts.
  - Additionally the new method for determining deficiency reserves resulted in massive surplus strain for some companies.
    - Depending on the level of X-factors.

XXX Impact

- Of course, the impact of XXX was not the same for all secondary guarantee designs
- For purposes of generating reserves under XXX the Shadow Accounts and similar designs are viewed as a series of 1-year minimum premium guarantees.
  - The series is structured to be a single segment as defined under XXX (Section 4B).

XXX Impact

- With a single segment deficiency reserves are usually not a problem due to the application of X-factors.
- The resulting XXX reserve level for YRT designs is at the ½ c_x level using the unitary method.

AXXX Impact

- Actuarial Guideline 38 addressed two issues with Universal Life contracts.
  - How to adjust XXX reserves for policies with a “catch-up” provision.
  - How to adjust XXX reserves when the secondary guarantee is being pre-funded.

AXXX Impact

Steps for adjusting for pre-funding

1. Establish minimum gross premiums at issue that satisfy the secondary guarantee requirement.
2. Determine basic and deficiency reserves by applying 7B and 7C of the XXX Model Regulation.

AXXX Impact

3. Take the value of the shadow account
4. Determine the single premium payment necessary at the valuation date to fully fund the secondary guarantee.
   – Assume no previous pre-funding.
   – Divide the result in Step 3 by the result in Step 4 = Pre-funded Ratio.

AXXX Impact

5. Compute a net single premium on the valuation date for the coverage provided by the secondary guarantee for the remainder of the secondary guarantee period.
   – Use any value table and select factors authorized in Section 5A of the XXX Model Regulation.

AXXX Impact

6. Determine the "net amount of additional premiums" by multiplying by multiplying ratio developed in Step 4 by the difference in the NSP from Step 5 and the XXX basic & deficiency reserves calculated in Step 2.

$$\text{Step } 6 = \text{Step } 4 \times (\text{Step } 5 - \text{Step } 2)$$

AXXX Impact

7. Calculate a “reduced deficiency reserve” by multiplying the deficiency reserve by 1 - the ratio from Step 4.
8. Total Reserve is the lesser of the NSP from Step 5 and the amount of Step 6 plus the total basic and deficiency reserves
   – This amount should be reduced by policy surrender charges.

AXXX Impact

9. Determination of increased basic reserve
   - The increased basic reserve is equal to the total reserve from Step 8 less the reduced deficiency reserve from Step 7.

Post-AXXX Secondary Guarantee Products

- Actuarial Guideline 38 was designed to impose additional reserves on shadow account and similar product designs.

Post-AXXX Secondary Guarantee Products

- There have been certain perceptions about how the new guideline would impact shadow account designs
  - All secondary guarantee designs would hold the same reserve levels for the same premium pattern.
    - I.e. lifetime level premium situations would have whole life reserves as the minimum reserve level.

Post-AXXX Secondary Guarantee Products

- Consistent reserve levels among competitors has not been the result of Actuarial Guideline 38

Post-AXXX Secondary Guarantee Products

- Based on the formulaic approach outlined in the guideline, higher reserve levels should be calculated as the company's liability emerges
  - The shadow fund represents the company's liability
- Since shadow account designs differ by company one should expect to see different reserve results by company

Pricing Strategies

- Companies have re-tooled base UL product designs to be more effective competitively and financially for the target market
  - Low CAWL funding levels.
  - Reduced interest rate spreads.
  - Competitive mortality (reinsurance).
  - Maximum SNFL surrender charges.

Pricing Strategies

- Companies have also focused on shadow account designs limiting the AXXX pre-funding ratio
  - Two common methods used
    - Design higher early duration charge structures
    - Premium loads on excess premiums
  - Other methods have been employed by companies to get at the same result.

Pricing Strategies

- The premium load has come under scrutiny
  - For many companies this premium load has been important to allow appropriate pricing on single premium (1035 Exchange) business.
  - Some companies have criticized the premium load as solely being a means to depress the pre-funding ratio by increasing the value of the denominator.

Pricing Strategies

- 2001 CSO product designs
  - The new table will allow a reduction in the level of reserves generated by XXX & AXXX.
  - This results is somewhat offset by the reduction in surrender charges resulting from the new table.

Reinsurance Availability

- The lack of reinsurance company choice has always been a problem
  – Most companies prefer to spread risk among several reinsurance companies.
- The lack of choice has led to a great deal of business being funneled to one reinsurer.
  – Can one reinsurer continue to support this business going forward?

Reinsurance Availability

- Other alternatives to reinsurance
  - Forming onshore or offshore captive reinsurance companies
    - Set up as traditional reinsurance structure for secondary guarantee UL.
  - Securitization
    - Has been done on a block of business to fund XXX reserves.
    - Is volume a barrier?

Competitive Environment

- Premiums have continued to decline
  - Rate of premium decline has lessened
  - Reduced premium levels generally tied to more complex product designs
- More companies looking to get in than getting out