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A Guide to Evaluating Life Insurance

In the last decade the life insurance industry has undergone a transformation. Lower mortality charges and cost efficiencies have created new life insurance products that may provide a greater value to the life insurance consumer. If you are considering the replacement of a permanent life insurance policy with another, you must first be aware of the possible disadvantages of such a transaction.

The substitution of one life insurance policy with another is a financial transaction that should be entered into only after serious deliberation.

- You may have to satisfy limits in your new policy that you have already satisfied in your old policy. During the first two years of a policy a life insurance company can challenge the validity of the policy and rescind a policy or deny a claim due to fraud or misrepresentation. The two-year "incontestable" and "suicide" periods begin again with the purchase of a new policy.
- If your present policy has existing loans, the transfer of the policy values may have potential tax consequences. An outstanding loan will be considered part of the policy's cash value. You should gain an understanding of this issue from your life insurance producer and also discuss this with your tax advisor.
- Even if your policy does not have a loan, there could be tax consequences. Generally, if you terminate a life insurance policy, you will be taxed on the "gain" in the policy, which is defined as the difference between the surrender value (the amount you will receive from the insurance carrier) and the cost basis (the amount of premium paid which includes any carry-over premiums from earlier contracts). These tax consequences can be mitigated with the use of a 1035 Exchange, discussed below.

Never surrender your existing life insurance policy until the new policy is in effect.

- Policies issued before June 21, 1988 may have tax benefits that are not available with the new policy being purchased since they are not subject to the rules governing Modified Endowment Contracts (MEC). If your existing contract is a MEC issued before June 21, 1988, you should gain an understanding of this issue from the life insurance producer you are working with and you should also discuss this with your tax advisor.
- New life insurance policies contain new sales and acquisition costs and a new surrender charge period. The new policy that you purchase may, at any point in time, have values that will be more or less than the values would have been in the policy being replaced.

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If you are making the decision to replace your existing policy with a new policy based on a sales illustration that relies on "current assumptions" and non-guaranteed investment returns, please be aware of the following:

Life insurance sales illustrations contain non-guaranteed elements based on current assumptions which may or may not occur.

- **Life insurance sales illustrations contain guaranteed and non-guaranteed elements.** The non-guaranteed elements are based on an interest rate or investment return assumption that may or may not be obtained, and mortality and cost assumptions that may or may not occur.
- **It should be noted that costs and mortality charges in newer policies have been trending downward as new actuarial tables and market driven cost efficiencies have come into play.**
- **If the new policy to be purchased is a Universal Life or Whole Life product, the investment returns in the policy are based on insurance company-directed accounts that invest primarily in bonds and real estate, including mortgages.** There will be an approximate 100-150 basis point difference between the actual returns obtained by the company and the amount credited to the policy. You can request information about the returns obtained by the insurance company and compare them to the amount credited.

If you are making the decision to replace your existing policy with a new policy based on a sales illustration that relies on "guaranteed assumptions," understand that the policy guarantees will be only as strong as the carrier backing them. Review the ratings of the selected carrier against this listing of top ratings from several independent rating agencies. Ratings should be monitored for changes.

AM Best	Fitch Ratings	Standard & Poors	Moodys
A++ (Superior) A+ (Superior) A (Excellent) A- (Excellent)	AAA (Exceptionally Strong) AA+ (Very Strong) AA (Very Strong)	AAA (Extremely Strong) AA+ (Very Strong) AA (Very Strong) AA- (Very Strong)	Aaa (Excep-tional) Aa1 (Excellent) Aa2 (Excellent)
B++ (Very Good) B+ (Good) B (Fair)	A+ (Strong) A (Strong) A- (Strong	A+ (Strong) A (Strong) A- (Strong)	A1 (Good) A2 (Good) A3 (Good)

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In addition to the ratings on the previous page, it is wise to select a carrier that has a Comdex rating of at least 80. The Comdex rating is the average percentile ranking for all of the ratings received by a company. As such, it is not another rating, but rather an objective scale that can be used to easily compare the ratings of different companies.

There are a number of very valid reasons why a new policy should be obtained in exchange for another policy.

- Changes in underwriting of the insured(s). Sometimes, the insureds have favorable changes to their health that might affect the cost structure of the policy.
- Underwriting opportunities. Specific underwriting programs that offer opportunities to reduce undesirable ratings from the original underwriting offers may become available. These may reduce the mortality costs within the policy.
- Carrier financial difficulties. If the financial stability of an insurer changes, it may be prudent to move to a more financially solvent company.
- Newer policies may have lower costs. Many of the newer policies available today have cost structures that are lower than policies issued just a few years ago. The carriers tend not to pass these cost savings on to people with older policies (policies issued more than five years ago) – so those who wish to take advantage of the newer costs may need to purchase new, more efficient policies.

An Internal Revenue Code Section 1035 Exchange refers to a tax-free method of exchanging an existing life insurance policy for a new policy with a different company. A 1035 Exchange allows the contract owner to exchange contracts while preserving the original policy's tax basis and deferring recognition of gain for federal income tax purposes.

- The owner, beneficiary and insured on the "new" contract must be the same as under the "old" contract. Changes in ownership may occur after the exchange is completed.
- Two or more "old" contracts can be exchanged for one "new" contract. No limit is imposed on the number of contracts that can be exchanged for one contract.
- The adjusted basis of the "new" contract is the total adjusted basis of all contracts exchanged. The death benefit for the "new" contract may be less than that of the exchanged contract, provided that all other requirements are met.
- You cannot exchange a second-to-die policy for a single-life policy or vice versa.
- Under certain circumstances you may exchange a contract with an outstanding loan for a "new" contract. This depends on the guidelines followed by the insurance company with whom the "new" contract is to be taken out.

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