## Life Insurance Resource Center

# Annuity Products in New York

An annuity is a contract between a purchaser and an insurance company in which the purchaser agrees to make a lump sum payment or series of payments in return for regular disbursements, beginning either immediately (within 12 months) or at some future date. The goal of most annuities is to provide a steady stream of income during retirement for a specified period of time or for the remainder of one or more lives. The lives on which payments depend are called annuitants. The purchaser is often the annuitant and the person to whom periodic payments are made.

There are two basic kinds of annuity contracts: immediate and deferred.

- **Immediate Annuity.** An immediate annuity is an annuity contract in which payments start within 12 months of the date of purchase. The immediate annuity is purchased with a single premium and periodic payments are generally equal and made monthly, quarterly, semi-annually or annually.
- **Deferred Annuity.** A deferred annuity is an annuity contract in which periodic income payments are not scheduled to commence for at least 12 months. Periodic payments are deferred until a maturity date stated in the contract or, if earlier, a date selected by the owner of the contract.

## Immediate Annuity Contracts

The most common Immediate Annuity Contract payment options include:

- **Straight Life Annuity.** Insurer makes periodic payments for the annuitant's lifetime. An option based upon the annuitant's survival is called a life contingent option. The owner/annuitant cannot outlive the income payments.
- **Life Contingent with Period Certain.** Periodic payments are made during the greater of the annuitant's lifetime or a specified period, such as 10 or 20 years. If the annuitant dies before the end of the specified period, a beneficiary receives the periodic payments for the remainder of the certain period.
- **Life Contingent with Refund Feature.** Periodic payments are made during the annuitant's lifetime. If the annuitant dies before the sum of the periodic payments made date equals the premium paid, the excess is paid to the beneficiary either in cash or installments.
- **Joint & Survivor Annuity.** There are two annuitants (called joint annuitants), usually a husband and wife and periodic payments continue until the death of both. The income payment amount may continue at 100% when only one annuitant is alive or be reduced (50%, 66.67%, 75%) during the life of the surviving annuitant.
- **Period Certain Annuity.** Periodic payments are made for a specified period of time (e.g., 5, 10 or 20 years). The payments are payable to a beneficiary if the annuitant dies prior to the end of the specified period. Income payments cease at the end of the period.

### Important Immediate Annuity Features

- Payments are usually payable in fixed dollar amounts, such as $100 per month, and do not provide protection against inflation.
- Some immediate annuities provide inflation protection with periodic increases based upon a fixed rate (3%) or an index such as the Consumer Price Index (CPI).
- An annuity with a CPI adjustment will start with lower payments or require a higher initial premium, but it will provide at least partial protection from the risk of inflation.
- In variable annuities, income payments fluctuate with the investment experience. Income payments remain constant if the investment performance (after all charges) equals the assumed investment return (AIR) stated in the contract. If the investment performance exceeds the AIR, payments will increase. If the investment

performance is less than the AIR, payments will decrease.

- Immediate annuities generally do not permit partial withdrawals or provide for cash surrender benefits. however, some contracts provide access to cash through a commutation provision. This provision allows you to withdraw funds in exchange for a reduction or elimination of future periodic payments.
- Immediate annuities include a "free look" period of 10 to 30 days in which you can request the refund of your premium.
- Immediate annuities provide longevity protection if you select a life contingent income option.
- Persons with shorter-than-average life expectancy may qualify for higher annuity payments than standard rates would provide. Such persons should seek insurers that use substandard underwriting and consider the annuitant's health status in determining annuity income payments.

### Factors to Consider when Purchasing an Immediate Annuity Contract

- Do you have sufficient financial resources to meet your income needs without purchasing an annuity? In other words, can you manage and take systematic withdrawals from such resources, without fear of outliving your resources?
- If you are concerned with the risk of outliving your financial resources, then you might consider purchasing an immediate annuity at least in an amount sufficient to cover your basic living expenses.

Income payments under the life contingent immediate annuity income option are based upon your age, gender, mortality table used by the insurer and premium paid to the insurer. For some options, your health and marital status may be considered.

A straight life annuity will provide a higher monthly income payment for a given premium than life contingent annuity with a period certain or refund feature. In other words, the cost of a specified income payment (e.g., $100 per month) will be higher for a life contingent annuity with a period certain or refund feature than for a straight life annuity. However, since payments cease upon the annuitant's death with a straight life annuity, the annuitant assumes the risk that only a small percentage of the premium paid will be received in periodic payments if the annuitant dies shortly after the purchase (or earlier than his or her life expectancy).

If an immediate annuity is purchased, the income option selected should be appropriate under the circumstances. For example, a person with a dependent spouse may want to consider a joint and survivor annuity.

A person concerned with receiving a minimum return on his or her annuity premium may want to consider a life contingent option with a period certain or a refund feature.

A variable immediate annuity is often chosen to keep pace with inflation during your retirement years. However, such option exposes the annuitant to additional investment risk because income payments can decline in a falling market.

## Deferred Annuity Contracts

In deferred annuity contracts, the periodic income payments are deferred for a period of at least 12 months.

The periodic income payment amount is determined when the contract is purchased or a premium is paid in the case of a paid-up deferred annuity or at commencement of such payments (upon annuitization) based upon the amount of funds accumulated under the contract in the case of an accumulation annuity.

The amount of the income payment depends on the premium paid for the paid-up deferred annuity and on the accumulation account for an accumulation annuity and on the annuity income option chosen.

Paid-up Deferred Annuity. A paid-up deferred annuity is an annuity contract in which each premium payment purchases a fixed dollar income benefit that commences on a specified date, such as a person's retirement date. The contracts do not maintain an account value. The premium cost for this product is much less than for an immediate annuity and it allows a person to retain control over most of his or her other assets during retirement, while securing longevity protection.

In the past, employers used this contract to fund employee retirement benefits. Each premium payment purchased a stream of income. At an employee's retirement, the income streams were added together. The employer could maximize the employee's retirement benefit if the contract did not provide for a death benefit or cash surrender benefit. Today, insurers are marketing a similar product, often referred to as longevity insurance. The contracts are generally purchased at retirement (age 65) and income payments are not scheduled to commence for a specified time period, such as 20 years (at age 85).

The contracts generally do not provide cash surrender benefits and may not provide a death benefit.

#### Accumulation Annuity

An accumulation annuity is a deferred annuity contract in which premiums paid (less expenses) are accumulated in an account (during the contract's accumulation phase) and the accumulation amount is applied to purchase an annuity income option at a selected retirement age (during the payout phase). The most significant features of accumulation annuities include the following:

- **Account value.** Unlike a paid-up deferred annuity, an accumulation annuity maintains an account value which is used in determining all contract benefits. New York law establishes minimum standards for the computation of such account value by prescribing maximum charges and minimum interest.
- **Cash surrender benefit.** Most accumulation annuities are required to provide access to contract funds through partial or full withdrawals, also called surrenders, at any time prior to or at retirement. Surrender charges, subject to statutory maximums discussed below, may be applied to such withdrawals.
  - When purchasing an accumulation annuity, you should consider whether you will need funds deposited in the contract prior to the expiration of the surrender charge period.
  - Most contracts permit withdrawals below a specified level (e.g., 10% of the account value) on an annual basis without surrender charge.
  - Cash surrenders may be subject to a six- month deferral.
- **Death benefit.** Accumulation annuities generally provide for a cash payment in the event of death prior to annuitization. In New York, death benefits are not treated as surrenders and, as such, are not subject to surrender charges.
- **Annuitization benefit.** Accumulation annuities allow contract holders to apply their accumulation amount to purchase income options at the more favorable of the contract's guaranteed rates or the insurer's current single premium immediate annuity rates at the time of purchase. The contract may have a stated annuitization date (maturity date), but will usually allow annuitization at any time after the first year.

Annuity income options listed for immediate annuities are generally also available under deferred annuity contracts.

With an accumulation annuity, the contract owner is said to annuitize his or her accumulation account. In other words, the owner converts the accumulation account into an income stream.

Compare the income payments available under the contract to comparable payment options under single premium immediate annuities available in the market offered by other insurers.

You can make periodic withdrawals from the account value in lieu of annuitizing. Many contracts permit withdrawals of up to 10% of the account value per year without applying surrender charges.

One advantage of taking periodic or systematic withdrawals instead of annuitizing, is that you still have access to your account value. You can make a partial withdrawal if you need additional funds. In addition, your account value continues to be maintained and credited with current interest or investment earnings.

Of course, by taking periodic or systematic withdrawals you run the risk of depleting your account value and outliving the contract's accumulated funds.

### Types of Accumulation Annuities

There are four basic types of accumulation annuities offered by life insurers in New York. The four types differ in how investment income is credited under the contracts. The first three listed below are considered fixed deferred annuities (or non-variable deferred annuities) because the account values do not vary directly with the investment experience of the supporting assets during the accumulation period.

**Excess Interest Annuity.** The excess interest annuity is the most common type of accumulation annuity. The contract guarantees a minimum interest rate for the life of the contract, but permits the insurer to declare discretionary excess interest. Such discretionary excess interest is generally determined and guaranteed annually in advance and is based upon present and anticipated earnings on current investments of the insurer. The periodic changes in excess interest permit insurers to offer rates that adjust in response to prevailing market rates.

- The minimum interest rate (from 1% to 3%) is based upon the five-year constant maturity treasury index. In most contracts, the minimum interest rate is set at issue, but some contracts permit the minimum rate to be adjusted periodically.
- Excess interest contracts provide flexibility with respect to premium payments (single or flexible).
- For excess interest annuities, the surrender charge is capped at 10% and generally reduces to 0% after a number of years (e.g., 7 to 10 years).

**Modified Guaranteed Annuity (MGA).** A modified guaranteed annuity (MGA) is an accumulation annuity that guarantees principal and a high rate of interest on amounts deposited for a specified time period up to ten years with an unqualified right to withdraw an unadjusted cash surrender benefit upon the expiration of the specified time period. Generally, the contract holder can select from a number of guarantee periods offered by the insurer (e.g., 3, 5, 7, 10 years). Withdrawals made prior to the expiration of the specified period may be subject to a market value adjustment and a withdrawal charge.

- Unlike the excess interest rate which can change each year, the interest rate in a MGA is guaranteed for the specified guarantee period (up to 10 years). No excess interest is expected to be credited.
- A market value adjustment adjusts a contract's account value on surrender or withdrawal to reflect changes in interest rates since the receipt of contract funds and the remaining duration of the interest rate guarantee. The adjustment can be positive or negative.

- For MGAs, the withdrawal charge (surrender charge) is limited to 7% and must reduce by 1% each year. Like a certificate of deposit, at the expiration of the guarantee, the accumulation amount can be renewed at the company's new MGA rate.
- MGAs may, but usually do not, provide for a market value adjustment on the disability or retirement of the owner.
- The death benefit in an MGA cannot be reduced by a market value adjustment. However, a positive market value adjustment can increase the death benefit.

**Equity Indexed Annuity (EIA).** An equity indexed annuity is an accumulation annuity that credits excess interest in accordance with an external market index, such as the Standard & Poor's 500 Composite Stock Price Index. EIAs provide their owners with the potential for larger interest credits based on growth in the equities market and provide a guaranteed minimum floor to avoid the downside risk that accompanies direct investment in equities.

Unlike excess interest annuities, the amount of excess interest to be credited is not known until the end of the year and there are usually no partial credits during the year. However, the method for determining the excess interest under an EIA is determined in advance.

For an EIA, it is important that you know the indexing features used to determine such excess interest. You should know whether:

- the index interest crediting method compares index values on an annual or more frequent basis;
- includes a monthly or annual interest rate cap on the amount that can be credited;
- participates fully or partially (e.g., 70%) in the index return,
- deducts a spread or margin (e.g., 2%) from the index gain, and
- permits the insurer to alter such method in future years.

You should also know that the minimum floor for an EIA differs from the minimum floor for an excess interest annuity. In an EIA, the floor is based upon an account value that may credit a lower minimum interest rate and may not credit excess interest annually. In addition, the withdrawal charge for equity indexed annuities starts at 10% and declines by 1% each year.

**Variable Annuity.** A variable annuity contract can be defined as a contract in which amounts paid to the insurer are allocated to one or more separate accounts and in which the account value or annuity benefits payable under the contract vary with the investment performance of the assets allocated to the separate account.

Separate accounts typically are organized into separate portfolios called sub-accounts, each with its own investment objective (e.g., money market sub- account, bond or income-related sub-account or stock type sub-account). The allocation of the amounts paid into the contract is generally elected by the owner and may be changed by the owner, subject to any contractual transfer restrictions.

The following are important features of and considerations in purchasing variable annuities:

- The contract holder bears the investment risk associated with assets held in a separate account (or sub account). Consumers should understand the risks inherent in the investment options selected.
- Withdrawals from a variable annuity may be subject to a surrender charge. You should be aware of the size of the charge and the length of the surrender charge period.

Request a copy of the prospectus. Variable annuities can provide benefits that exceed the contract's account value. Most variable annuities include a death benefit equal to the greater of the account value, the premium paid or the highest anniversary account value. Many variable annuity contracts now offer guaranteed living benefits that provide a guaranteed minimum account, income or withdrawal benefit.

For variable annuities with such guaranteed benefits, consumers should be aware of the charges for such benefit guarantees as well as any limitation or restriction on investments options and transfer rights.

## Other Annuity Features and Factors to Consider

**Bonus Annuities.** Many accumulation annuities (both fixed and variable deferred annuities) provide for the crediting of a bonus rate (typically, 1%, 2%, 3%) on amounts deposited under the contracts for the first year. For fixed deferred annuities, the bonus rate is added to the interest rate declared for the first contract year.

Know how long the bonus rate will be credited, the interest rate to be credited after such bonus rate period and any additional charges attributable to such bonus, such as any higher surrender or mortality and expense charges, a longer surrender charge period or a bonus recapture charge on death.

**Replacement.** Be wary of replacing an existing contract solely to receive a bonus on another product. Before replacing an existing insurance or annuity product, you should compare the two policies, be aware of the consequences of replacement (new surrender charge and contestability period) and be sure that the new product suits your current needs.

Agents are required to provide you with prescribed comparison forms to help you decide whether the replacement is

in your best interest.

**Taxes.** Annuity contracts provide certain tax advantages. Income taxes on interest and investment earnings in deferred annuities are deferred. However, in general, a partial withdrawal or surrender from an annuity before the owner reaches age 59 ½ is subject to a 10% tax penalty. Special care should be taken in roll-over situations to avoid a taxable event.

Annuity products have become increasingly complex. It is imperative that you understand the products available and the tax ramifications of these products. Consult a competent tax advisor for assistance.

**Guaranty Fund.** Generally, immediate and deferred annuity contracts issued to a New York resident by a licensed life insurance company that provide fixed benefit guarantees are covered by the **Life Insurance Company Guaranty Corporation** of New York for up to $500,000.

Such fixed benefit guarantees include the guaranteed minimum death benefit and guaranteed living benefits in variable annuity contracts.

Separate account investment options that limit guarantees to the contract holder's interests in assets allocated to the separate account are not covered by the guaranty fund. Generally, claims under a variable annuity contract would be satisfied out of such separate account assets.

**Suitability.** Make sure that the contract you select is appropriate for your circumstances. For example, if you purchase a tax qualified annuity, minimum distributions from the contract are required when you reach age 70 ½. You should know the impact of minimum distribution withdrawals on the guarantees and benefits under the contract. Guaranteed living benefits in variable annuities often restrict withdrawals or limit or reduce benefits because of withdrawal activity.

Only purchase annuity products that suit your needs and goals and that are appropriate for your financial and family circumstances.

**Buy New York.** Agents and brokers licensed by the New York State Department of Financial Services are required to be competent and trustworthy. Make sure that the agent or broker is licensed in good standing with the Department.

Annuity products approved for sale in New York generally provide greater consumer protections than products sold elsewhere. The minimum account values are higher, charges are lower and annuitization and death benefits are more favorable.

Make sure that you are buying a New York approved annuity product. Be wary of an agent who suggests that you sign an application outside New York to purchase a non-New York product.

Next Topic: **Policyholder Protection and the LICGC**

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Updated 08/27/2014

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## Life Insurance Resource Center

## Basic Types Of Policies

For the most part, there are two types of life insurance plans - either term or permanent plans or some combination of the two. Life insurers offer various forms of term plans and traditional life policies as well as "interest sensitive" products which have become more prevalent since the mid-1980's . In New York State, the Department of Financial Services must approve any life insurance policy before a company can issue it to consumers. The New York Insurance Law provides for standard provisions that must be included in every policy.

**TERM INSURANCE** Term insurance provides protection for a specified period of time. This period could be as short as one year or provide coverage for a specific number of years such as 5, 10, 20 years or to a specified age such as 80 or in some cases up to the oldest age in the life insurance mortality tables. Policies are sold with various premium guarantees. The longer the guarantee, the higher the initial premium. If you die during the term period, the company will pay the face amount of the policy to your beneficiary. If you live beyond the term period you had selected, no benefit is payable. As a rule, term policies offer a death benefit with no savings element or cash value.

Premiums are locked in for the specified period of time under the policy terms. The premiums you pay for term insurance are lower at the earlier ages as compared with the premiums you pay for permanent insurance, but term rates rise as you grow older. Term plans may be "convertible" to a permanent plan of insurance. The coverage can be "level" providing the same benefit until the policy expires or you can have "decreasing" coverage during the term period with the premiums remaining the same. If you do not pay the premium for your term insurance policy, it will generally lapse without cash value, as compared to a permanent type of policy that has a cash value component. Currently term insurance rates are very competitive and among the lowest historically experienced.

It should be noted that it is a widely held belief that term insurance is the least expensive pure life insurance coverage available. One needs to review the policy terms carefully to decide which term life options are suitable to meet your particular circumstances.

**Types of Term Insurance:**

- **Renewable Term.** Renewable term plans give you the right to renew for another period when a term ends, regardless of the state of your health. With each new term the premium is increased. The right to renew the policy without evidence of insurability is an important advantage to you. Otherwise, the risk you take is that your health may deteriorate and you may be unable to obtain a policy at the same rates or even at all, leaving you and your beneficiaries without coverage.
- **Convertible Term.** Convertible term policies often permit you to exchange the policy for a permanent plan. You must exercise this option during the conversion period. The length of the conversion period will vary depending on the type of term policy purchased. If you convert within the prescribed period, you are not required to give any information about your health. The premium rate you pay on conversion is usually based on your "current attained age", which is your age on the conversion date. This type of policy often provides the maximum protection with the smallest amount of cash outlay.
- **Level or Decreasing Term.** Under a level term policy the face amount of the policy remains the same for the entire period. With decreasing term the face amount reduces over the period. The premium stays the same each year. Often such policies are sold as mortgage protection with the amount of insurance decreasing as the balance of the mortgage decreases. If the insured dies the proceeds of the policy can be used to pay off the mortgage.
- **Adjustable Premium.** Traditionally, insurers have not had the right to change premiums after the policy is sold. Since such policies may continue for many years, insurers must use conservative mortality, interest and expense rate estimates in the premium calculation. Adjustable premium insurance, however, allows insurers to offer insurance at lower "current" premiums based upon less conservative assumptions with the right to change these premiums in the future. The premium, however, can never be more than the maximum guaranteed premiums stated in the policy.

**PERMANENT INSURANCE** (Whole Life or Ordinary Life). While term insurance is designed to provide protection for a specified time period, permanent insurance is designed to provide coverage for your entire lifetime. To keep the premium rate level, the premium at the younger ages exceeds the actual cost of protection. This extra premium builds a reserve (cash value) which helps pay for the policy in later years as the cost of protection rises above the premium. Whole life policies stretch the cost of insurance over a longer period of time in order to level out the otherwise increasing cost of insurance. Under some policies, premiums are required to be paid for a set number of years. Under other policies, premiums are paid throughout the policyholder's lifetime. The insurance company invests the excess premium dollars

This type of policy, which is sometimes called cash value life insurance, generates a savings element. Cash values are critical to a permanent life insurance policy. The size of the cash value build-up differs from company to company. Sometimes, there is no correlation between the size of the cash value and the premiums paid. It is the cash value of the policy that can be accessed while the policyholder is alive.

The Commissioners 1980 Standard Ordinary Mortality Table (CSO) is the current table used in calculating minimum nonforfeiture values and policy reserves for ordinary life insurance policies. This table provides the minimum cash values that must be guaranteed in your policy.

The policy's essential elements consist of the premium payable each year, the death benefits payable to the beneficiary and the cash surrender value the policyholder would receive if the policy is surrendered prior to death. You may make a loan against the cash value of the policy at a specified rate of interest or a variable rate of interest but such outstanding loans, if not repaid, will reduce the death benefit.

In 1984 a new federal tax law required that for permanent insurance to enjoy preferred tax treatment it must provide coverage up to at least age 95, limit the amount of premium that may be paid in relation to the face amount of coverage and establish a minimum ratio between cash value and face amount of insurance. Many permanent policies will contain provisions, which specify these tax requirements.

There are two basic categories of permanent insurance, traditional and interest-sensitive, each with a number of variations. In addition, each category is generally available in either fixed-dollar or variable form.

**Traditional Whole Life.** Traditional whole life policies are based upon long-term estimates of expense, interest and mortality. The premiums, death benefits and cash values are stated in the policy. There are six basic variations of traditional permanent insurance:

- Non-Participating Whole Life A non-participating whole life policy will give you a level premium and face amount during your entire life. The advantages of such a policy are its fixed costs and generally low out-of-pocket premium payments. The disadvantage is that it pays no dividends.
- Participating Whole Life A participating whole life policy pays dividends. The dividends represent the favorable experience of the company and result from excess investment earnings, favorable mortality and expense savings. Dividends can be paid in cash, used to reduce premiums, left to accumulate at interest or used to purchase paid-up additional insurance. Dividends are not guaranteed.
- Indeterminate Premium Whole Life An indeterminate premium whole life policy is like a non-participating whole life plan of insurance except that it provides for adjustable premiums. The company will charge a "current" premium based on its current estimate of investment earnings, mortality, and expense costs. If these estimates change in later years, the company will adjust the premium accordingly but never above the maximum guaranteed premium stated in the policy.
- Economatic Whole Life An economatic whole life policy provides for a basic amount of participating whole life insurance with an additional supplemental coverage provided through the use of dividends. This additional insurance usually is a combination of decreasing term insurance and paid-up dividend additions. Eventually, the dividend additions should equal the original amount of supplemental coverage. However, because dividends may not be sufficient to purchase enough paid up additions at a future date, it is possible that at some future time there could be a substantial decrease in the amount of supplemental insurance coverage.
- Limited Payment Whole Life If you want to pay premiums for a limited time the limited payment whole life policy gives you lifetime protection but requires only a limited number of premium payments. Because the premiums are paid over a shorter span of time, the premium payments will be higher than under the whole life plan.
- Single Premium Whole Life Single premium whole life is limited payment life where one large premium payment is made. The policy is fully paid up and no further premiums are required. Many such policies have substantial surrender charges if you want to cash in the policy during the first few years. Since a substantial payment is involved, it should be viewed as an investment-oriented product.
    - Interest in single premium life insurance is primarily due to the tax-deferred treatment of the build-up of its cash values. Taxes will be incurred on the gain, however, when you surrender the policy. You may borrow on the cash value of the policy, but remember that you may incur a substantial tax bill when you surrender, even if you have borrowed out all the cash value.

**Interest Sensitive Whole Life.** While insurers guarantee stated benefits on traditional contracts far into the future based on long-term and overall company experience, they allocate investment earnings differently on interest sensitive whole life in order to better reflect current fluctuations in interest rates. The advantage is that improvements in interest rates will be reflected more quickly in interest sensitive insurance than in traditional; the

disadvantage, of course, is that decreases in interest rates will also be felt more quickly in interest sensitive whole life.

There are four basic interest sensitive whole life policies:

Universal Life The universal life policy is actually more than interest sensitive as it is designed to reflect the insurer's current mortality and expense as well as interest earnings rather than historic rates. Universal life works by treating separately the three basic elements of the policy: premium, death benefit and cash value. The company credits your premiums to the cash value account. Periodically the company deducts from the cash value account its expenses and the cost of insurance protection, usually described as the mortality deduction charge. The balance of the cash value account accumulates at the interest credited. The company guarantees a minimum interest rate and a maximum mortality charge. Some universal life policies also specify a maximum basis for the expense charge. These guarantees are usually very conservative. Current assumptions are critical to interest sensitive products such as Universal Life. When interest rates are high, benefit projections (such as cash value) are also high. When interest rates are low, these projections are not as attractive.

Universal life is also the most flexible of all the various kinds of policies. Because it treats the elements of the policy separately, universal life allows you to change or skip premium payments or change the death benefit more easily than with any other policy.

The policy usually gives you an option to select one or two types of death benefits. Under one option your beneficiaries received only the face amount of the policy, under the other they receive both the face amount and the cash value account. If you want the maximum amount of death benefit now, the second option should be selected.

You generally pay a planned premium designed to keep the policy in force for life, and accumulate cash value, based upon the interest and expense and mortality charges you assume. It is important that these assumptions be realistic because if they are not, you may have to pay more to keep the policy from decreasing or lapsing. On the other hand, if your experience is better then the assumptions, than you may be able in the future to skip a premium, to pay less, or to have the plan paid up at an early date.

You do not have to pay the planned premium, but if you pay less, the benefit may be more like term insurance, which is only in force for a limited time and builds no cash value. On the other hand, if you pay more, and your assumptions are realistic, it is possible to pay up the policy at an early date.

If you surrender a universal life policy you may receive less than the cash value account because of surrender charges which can be of two types. A front-end type policy will deduct a percentage of the premium paid, while a back-end type policy will deduct a more substantial charge but only if the policy is surrendered before a specified period, generally 10 years but which could be as long as 20 years. A back-end type policy would be preferable if you intend to maintain coverage, and the charge decreases with each year you continue the policy. Remember that the interest rate and expense and mortality charges payables initially are not guaranteed for the life of the policy.

Although this type of policy gives you maximum flexibility, you will need to actively manage the policy to maintain sufficient funding, especially because the insurance company can increase mortality and expense charges. You should remember that the mortality charges increase, as you become older.

Excess Interest Whole Life If you are not interested in all of the flexible features of Universal Life, some insurers offer fixed premium versions called excess interest whole life. The key feature is that premium payments are required when due just like traditional whole life. If premiums are paid when due, the policy will not lapse.

With the premium level fixed, any additional or excess interest credited, or better life insurance experience, will improve the cash value of the policy. The premium level will probably be comparable to traditional whole life policies. Cash value may be applied to pay future premium payments. This type of product maximizes the deferred tax growth of your cash value.

Current Assumption Whole Life Current assumption whole life is similar to a universal life policy but your company determines the amount of premium to be paid. The company sets the initial premium based upon its current estimate of future investment earnings and mortality experience and retains the contractual right to reevaluate its original estimates to increase or decrease your premium payments later. If premiums are increased, some policies let you decrease the face amount of coverage so that you can continue to pay the original premium. Current mortality and experience and investment earnings can be credited to the insurance policy either through the cash value account and/or the premium or dividend structure (depending on whether it is a stock or mutual company). Regardless, this type of policy has the following characteristics:

The premiums are subject to change based on the experience (mortality, expenses, investment) of the company. The policyowner does not exercise control over the changes.

The policyowner can use the cash value to make loans just as he/she would with any traditional ordinary life insurance policy.

A minimum amount of cash value is guaranteed, just as with traditional ordinary life insurance.

The death benefit does not fluctuate.