

Comprehensive Analytics, Inc.

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Presentation of Analysis

For:

Julie Ann

Project:

Analysis of Life Policy #2342

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This report is based on research and discovery of historical sequence and documentation related to the financial planning strategies created or recommended. This may include the relationship of various entities, such as family limited partnerships, general partnerships, trusts, GRAT's, Irrevocable Life Insurance Trusts (ILIT), split dollar arrangements, collateral assignments and release of such, replacement of previous policies, etc. In addition, discussions with advisor and/or client took place to address certain issues of the existing and/or proposed strategies.

Analysis, conclusion and recommendations have been developed on the documentation, financial records, insurance provider statements and illustrations, and other such relevant data as supplied by the advisor, the client and the stated insurance carriers. Comprehensive Analytics, Inc, case managers, and those who perform the analysis and recommendation have no responsibility for the information supplied by all sources heretofore mentioned.

Implementing the process of LIFE-180®

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Index:

Cover	
Index	
Page 3	Preface Commentary: Disclosure Statement and Executive Summary
Pages 4 - 6	Preface Commentary continued...
Pages 7 - 8	Fiduciary Approach
Pages 9 - 10	Functionality of Policy Styles
Page 11	Recommendation Commentary
Pages 12 - 13	Intentionally left blank

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Preface Commentary

Disclosure Statement:

This Report is limited to the analysis of the referenced policy only, and does not take into consideration the process necessary to properly identify client risks, impact and probabilities of said risks, time-line integration, appropriate selection of policy style preference to best manage said risks in the most efficient manner, elements of risk management control and flexibility, cost efficiencies, capital use alternatives, gifting limitations, and tax considerations.

Information provided is represented by the most current policy anniversary statement dated March 29, 2015, and an in-force illustration dated August 11, 2015. From such information, we know that said policy was issued March 29, 2005 and have assumed that the client was age 50 at time of issue, and is currently age 60. All comparative data is based on those age assumptions, as a female rated Preferred Select Non-Tobacco. Policy owner is an Irrevocable Trust.

Executive Summary:

Life Policy #2342 provides for a death benefit of \$1 Million dollars, and illustrates an annual premium of \$20,000. The policy cash values are positioned with 51% in an investment portfolio and 48% in the Fixed Account (per anniversary statement; 1% differential is due to rounding off).

The policy structure is that of a modified Variable Universal Life (VUL). Modification is due to the inclusion of a no-lapse guarantee. The death benefit is guaranteed for life, as long as the premiums stated are paid on the due date through age 82 (32 year premium payment requirement). The in-force illustration indicates that premiums COULD stop at age 81, if the projected cash values are sufficient to allow for the one-year decrease of premium payments.

Objective of analysis is to bring full disclosure as to the economic efficiencies of this policy style in relation to the risk that it is assigned to manage.

Preface Commentary Continued . . .

Policy Analysis:

The language provided by the in-force illustration gives some guidance as to the cost and capital efficiencies of the policy.

1) "Even though it (the policy) contains a no-lapse guarantee, this policy may provide nonforfeiture benefits (such as cash surrender values) which ARE LESS than those that would be provided if the no-lapse guarantee were issued as a separate policy,..."

The question is, How much less?

If a VUL policy would have been taken back in 2005 with the same death benefit and an annual premium of \$20,000, the cash value in policy year 10 (2015) is assumed to be that of \$260,747. When compared to the \$131,786 cash value of the existing policy, the loss of capital efficiency is that of \$128,961. This is a "Cost" of lost capital.

2) ".... but with a fixed premium and face amount (where such a separate policy provide the same guarantees insurance coverage as would be provided under the no-lapse guarantee). However, the premiums for that separate policy might be higher than those for the no-lapse guarantee in this policy."

The question is, what WOULD the premium be for the same guaranteed death benefit for life, with a 30-year premium paying period?

Based on the same rating and age 50, the annual premium would have been \$7,655.

Therefore, when we look at a comparative of like-benefits (guarantees), the current policy requires excess annual premiums of \$12,345. Over the 10-year premium paying history of the current policy, the total excess premiums (not required for a comparative guarantee no-lapse policy style) is that of \$123,450. This is a "Cost" of pricing deficiency.

3) If we were to take an approach of implementing each policy style in a more efficient manner (i.e. - two separate policies), and used that as a comparative, (an annual premium of \$7,655 for the guaranteed no-lapse policy; an annual premium of \$12,345 for a VUL policy) the independent VUL policy would have accumulated an assumed \$160,486, with an additional death benefit of \$404,426. This death benefit would increase each year. At age 82, the VUL is assumed to have accumulated a cash value of \$1,077,581 with a death benefit of \$1,551,716. Whereas, the existing policy's in-force illustration projections to age 82 shows a cash value of \$983,985 with an increased death benefit of only \$352,501. The differentials represent "Costs" of both lost capital, pricing deficiency, and death benefit.

Preface Commentary Continued . . .

Contract Language and Structure:

A No-Lapse Guarantee provision is usually provided by a "Rider" to the policy. We were not provided a copy of the policy contract to confirm this, but this Rider represents standard protocol. Once the Rider becomes part of the contract, there is an impact on several important components of the policy, whether it be the more commonly used Universal Life (UL) policy style, or a VUL policy style (which is the style under analysis).

Impact #1

Flexibility of premium is eliminated or severely restricted, since any variation will have an affect on the Guarantees of the contract.

Impact #2

The loss of premium flexibility also relates to the premium due date. If a premium is late (and in some contracts early), penalties may be due and required. The amount and contractual calculation of such penalties are dependent on pricing methodology and use of "Shadow" accounts. We were not provided a copy of the policy contract to review these provisions, but they may not be as severe as those within policies issued prior to 2005.

Impact #3

The ability to access policy cash values is severely restricted, since any variation will have an affect on the Guarantees of the contract.

Impact #4

Flexibility of changing the death benefit is severely restricted, since any variation will have an affect on the Guarantees of the contract.

Note:

It appears that there is a requirement as to the percentage of cash value (portfolio) required to be in the Fixed Account. This is plausible since the Guarantees could not be provided without a "Base" policy - fixed account relationship.

Preface Commentary Continued . . .

Policy Costs and Expenses:

The policy under analysis has a 5.75% premium load on each premium paid. This expense is applied to the entire premium, regardless of the allocation to the Fixed or Investment accounts. The load is close to the industry average. The VUL we developed for comparative review has a 2% premium load.

Certain policy costs and expenses are related to the composition of the cash value portfolio.

The Monthly Policy Charge is \$17.50, or \$210 per annum. The VUL we used in comparison has this charge at \$7.50, or \$90 per annum.

The monthly Policy Issue Charge is \$508, or \$6,096 per annum. Appears to increase annually.

The monthly Cost-of-Insurance (COI) is in the \$150.00 range (slight variances each month), or \$1,800 per annum. This will increase each year. Increases in COI's is common in every life insurance policy style.

The assumed portfolio management expenses are not clearly defined in the illustration due to the blending of the Fixed and Investment account portfolio. However, the listing of sub-account managers on Pages 16 though 18 of the in-force illustration provides the Investment Expense for each money manager. These expenses are slightly above average, much higher than the VUL we used as a comparative.

Notes:

A) The allocations shown on Pages 16 though 18 of the in-force illustration are not consistent with the allocations shown in the Policy Anniversary Statement dated March 29, 2015.

B) All policy Costs and Expenses are taken from the investment portfolio. This is a negative result strategy in relation to properly surviving a downward market cycle.

END

The Fiduciary Approach to Risk Management (life insurance)

The questions:

- How do we engage in the facilitation of the financial planning process from a different perspective to that which is most common in the industry?
- How do we employ unbiased objectivity and open architecture?
- How do we filter the planning strategies from product solicitation?
- How can we separate or uncouple the integration of solicitation activity and concept?
- How can we change the process so that there is a more prudent approach under fiduciary standards of full disclosure and transparency?
- How do we accomplish this with focused discernment for the client's best interest?

Comprehensive Analytics employs a fiduciary process and open architecture of full disclosure and transparency in a fee-engagement venue. The client-centric focus takes us in a lateral direction of fiduciary development from Point A to Point B, in which:

Point A: Client

Point B: Recommendations for Resolve

Fiduciary lateral direction:



During this process, we must Spot areas of deficiency, compromise or contradiction, Seek the full horizon of potential resolutions, Select those that would best fit that particular client, and Solve or bring to resolution.

Foundational truths that represent guiding benchmarks to our approach are:

- There are two distinctive venues involved with the financial planning process; the legal venue and the asset venue.
- Each client has a need, and that need must be defined in a succinct manner.
- Every need has a relationship. The relationship may be financial, physical, emotional, mental, or spiritual. It may be closely tied to self, family, or it may be philanthropic.
- There may be any number of circumstances in which insurance is required for resolve.
- There will be any number of circumstances in which no insurance is necessary.
- We need to serve as guides with compassion and directional fortitude.
- Compensation should **never** be the Initiative or an Obstacle!
- It is the "Clean Room" environment of fiduciary process that establishes the true value at presentation.
- It is the "Clean Room" environment of fiduciary process *that must also be carried forward* in any form of facilitation for the implementation of recommendations.

The fiduciary process requires Full Disclosure, Transparency, Knowledge, Deep Skill Sets, Concepts & Strategies, Full Horizon of Product Venue and Integrity. This approach is unique in the industry.

The most common approach with insurance planning is to move in a lateral direction of B-to-A, nurtured by an environment of transactional initiative that is not completely unbiased.

Industry lateral direction:



Point B: Marketing, Concepts & Strategies, Products, Transactional, Commission driven distribution system/channel, Bonus Initiatives, External Influence, Knowledge.

The B-to-A process will always create doubt as to the recommendation being potentially influenced by “other” factors, which may have been instrumental in developing the proposed resolve (presentation).

Whereas, the fiduciary construct of the A-to-B process creates a filter to protect the client from external forces and removes any doubt as to the initiative behind the final analysis and proposal.

If the risk management issue requires insurance, there are occasions when a no-load policy represents the best solution. There are also those occasions when a commission policy may fit best. In either case, it has to be the process that is handled correctly. No other consulting approach offers the full horizon of risk management concept and product designing possibilities.

As previously stated, the two distinctive venues involved with the financial planning process are:

The Legal venue of the process:

Compensation is not a major area of concern, since the legal venue employs the facilitation of documentation at set rates and is based in a fee-engagement universe. If a client needs a particular trust, the creation of those documents will cost \$X. People Skills, Knowledge, Experience, and Expertise are the deciding factors.

The Asset venue of the process:

Assets come in many forms – hard assets, present assets, future assets, tangible and intangible. Insurance is also an asset, whether it is in the form of cash value equity, death benefit, tax impact, or leveraged capital.

This is where compensation **does** become an issue, challenging the integrity of the recommendation. How can we be sure that the insurance is necessary? Is it the right policy style? Does the policy structure best fit the objective? Has the premium strategy been comparatively tested? What product represents best execution? How do we employ a prudent man concept with fiduciary construct?

Comprehensive Analytics, Inc supports the full disclosure and transparency model for fiduciary compliance, and has developed unique methodology based on such principles. It is void of motivation to qualify for production targets and trips – keeping focus on the client, a belief that sound product design and strategy for the benefit of the client should be the driving force for accommodation.

Functionality of Life Insurance Policy Structure & Design

Old - Paradigm Policy Styles: Premium Dependent

- Term Life
- Traditional Whole Life
- Participating Whole Life - No Term Blends

A Premium Dependent policy is a design structure in which the policy contract requires the payment of premiums to continue the policy - keep it "in force".

If there is a default in the premium payment, the policy will terminate (Term), automatically borrow the required premium from any cash value that may exist within the policy (Traditional Whole Life) or combine automatic premium loans with use of dividends (Participating Whole Life).

The important features of these styles of policies is that premium and death benefit are fixed and guaranteed (Term), premium, death benefit, and cash values are fixed and guaranteed (Participating Whole Life), and in the case of Participating Whole Life, the policy provides non-guaranteed dividends (which represent a return of premium overcharges). In all cases, the premiums have been established and published in a Rate Book and are contractually required for the length of the policy.

Access to any cash value equity is restricted with regard to options, there is limited flexibility, and the cash value will usually accrue over a long period of time.

Transitional Policy Style: Dividend Dependent

- Participating Whole Life - With Term Blends

This policy style will consist of a small "base" policy with a large addition of a term rider - referred to as a "term blend". The contract guarantees are limited to the base policy, and the term portion has no guarantees. Assumed, non-guaranteed dividends are responsible to maintain the policy. There is very little disclosure in these policy styles and can be very frail.

New Paradigm Policy Styles: Cash Value Dependent

- Universal Life (Single Life or Survivorship)
- Variable Life (Single Life or Survivorship)

These new policy styles shifted away from the Premium Dependent design to that of a Cash Value Dependent design. The contracts were to pass through to the client the advantages of current mortality experience (Cost-of-Insurance), current interest rate markets (Universal Life), or current investment market (Variable Life) potential.

This policy style has no contractual premium requirements.

Policy costs are taken internally from the cash value within the policy. The policy cannot lapse or terminate due to non-payment of premiums, but will lapse or terminate if there is not sufficient cash value to cover the policy's cost. Therefore, premiums for this style of policy become a "deposit strategy", so that there is always sufficient cash value to maintain the continuation of the policy (or for the accumulation of a tax-advantaged asset).

Premiums for a cash value dependent policy are developed in cooperation between the insuring company and the advisor, the construction of which is predicated on certain cost and market return assumptions. As there are no Rate Book premiums to guide in this calculation, illustration software has been developed to assist in developing the premium deposit strategy so that there is sufficient cash value equity to continue the policy.

The important features of these styles of policies are that minimum interest rates (Universal Life) and maximum policy costs (Universal Life and Variable Life) for the death benefits purchased are fixed and guaranteed. Access to any cash value equity has various options and there is increased flexibility and control over the policy. Cash value will usually accrue earlier and more rapidly than it would in a premium dependent policy.

New-Paradigm *Hybrid* Policy Styles: Premium Dependent

- **No-Lapse Guarantee Universal**

The functionality of this policy style is that of a hybrid between Term, Traditional Whole Life, and Universal Life, but it is NOT any of those policy styles. The pricing is similar to a term-until-death, with some accrual of cash value.

The important features of this style of policy is that it has more flexibility than Traditional Whole Life and can produce an equal amount of death benefit coverage at a lower premium requirement (Policy is not required to endow, as is the case of Traditional Whole Life). The policy will provide coverage for life, which term cannot provide.

This policy does not provide the cash value accumulation potential or the maximum flexibility and control that is prevalent in the Universal Life and Variable Life policy styles.

The guarantees of the policy will become void if the contractual premium is not paid.

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Recommendation Commentary

1) The strategy of paying excess premiums to accumulate equity in a policy that is held within an ILIT (Revocable Trust) is generally not the recommended approach, unless the objective is other than that of securing the guarantee of premiums and death benefit (so that a claim is paid regardless of the age of demise); We are not aware of another objective.

2) Assuming the insured is in good health, a comparative Guaranteed No-Lapse policy can be obtained, with the same coverage of \$1 Million for life, the same limited premium paying period to age 81, by initiating a 1035 tax free exchange of existing cash value into a new policy. Annual premiums to age 81 would be in the \$5,300 range. This would reduce the contractually required premium by \$14,700. The result would be the institution of a much more cost efficient policy.

3) If there is a desire to accumulate invested equity within a tax-advantaged VUL policy, we would recommend a review of a no-load product.

Conclusion:

The existing policy does not appear to provide the "Best" of both worlds (guarantee and accumulation), but the "Least" efficient use of capital (premium outlay) due to the blended policy style.

Caveat:

In order to determine the best course of action so that the appropriate policy style is selected for each defined risk, the client should consider a Risk Management Mapping Analysis Program to determine appropriate amount of coverage and policy style selection for each risk identified. This would also open up a review of creative strategies and concepts, provide transparency and full disclosure, and an unbiased analysis that may also suggest non-insurance alternatives for resolve.

END

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