Managing Your Life Insurance Policies

A friend of mine just called me to tell me that his mom had been paying for a $1,000,000 life insurance policy for the last twenty years. However, her life insurance company just sent her a letter letting her know that her policy was scheduled to expire unless she was willing to more than double her annual premiums.

I explained to my friend that when his mother originally purchased her current policy, interest rates were much higher.  It was not uncommon for life insurance companies to project continued 8-9% growth on the cash value of the policies.  Based on those assumptions, the policies would continue to remain in force for the rest of the insured’s life.

However, many insurance agents fail to explain to customers that the policies are not fully guaranteed but rather they are based on projections.  When interest rates fall for a long time like they have, most life insurance policies will underperform their original projections. Therefore, it is imperative that you review the performance and the updated projections of your policies each year to avoid unpleasant surprises.

Whole life insurance policies typically last for your whole life but they also have a cash value component.  That cash value grows each year based on the performance of the life insurance company’s general portfolio which usually consists of very conservative investments like treasuries and bonds.  Since those portfolios had been accumulating new bonds during a low interest rate environment, those portfolios which used to make 8-9% per year now perhaps make only 4% per year.

If you don’t want your cash value to grow at such a low rate for the rest of your life you could consider exchanging your policy to a variable life policy that offers a wide variety of investment choices that will allow you to potentially earn much more on your money than a conservative bond portfolio, while maintaining the ability to grow your money tax free, withdraw nontaxable income and leave a large income tax free death benefit to your heirs.

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