Wait, What? How Much Can You Accelerate With A Chronic Illness Rider?

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Product Trends

Taking a look back at life insurance trends we've seen products fall in and out of favor. Fifteen years ago, guaranteed universal life (GUL) enjoyed its heyday. Then, we watched alternatives to GULs rise, focused on a similar value proposition. Sometimes this took the form of a current assumption UL with life expectancy guarantees or perhaps a variable UL (VUL) chassis with an extended no-lapse guarantee. During the same 15-year period, whole life (WL) sales remained consistently stable in all market and interest rate environments. Meanwhile, the major emphasis for insurers not focused on WL has been indexed universal life (IUL). For some, IULs continue to be the perfect alternative to low interest crediting offered on UL and volatile returns on VUL (some protection-focused IULs even offer lifetime death benefit guarantees).

Long Term Care – Life Insurance Trends

What's truly fascinating is that there has been one life insurance trend which transcends all product categories. Specifically, long term care (LTC)- life insurance solutions (combination products) have enjoyed remarkable success. Per LIMRA, as of 2019, 30% of total individual life premium included some form of combination product (LTC riders, chronic illness riders or hybrid products). Think about that for a moment, 30%! Interestingly, 15 years ago, you could have counted the number of insurers offering a LTC or chronic illness rider on one hand. Today, you would be hard pressed to find a life insurance product which does not offer at least one of these options. (Some chronic illness riders can even be found on term insurance). Hybrid products have also enjoyed substantial growth with three times the number of carriers in the market since 2005, offering their uniquely positioned solution, whether it be on a WL, UL, IUL, or VUL chassis.

Chronic Illness Riders

For our purposes today, we will be zeroing in on the riders available on life insurance. The most prevalent are the chronic illness riders, in particular those which have no charge until acceleration (the charge and benefit amount is applied at acceleration via a discount or lien method). In addition to the obvious appeal of not charging until acceleration, these riders typically require no additional underwriting and are automatically included on the policy, up to a certain age/table rating. Translation: a lot of them have been "sold," and a lot of them are currently being sold. Per LIMRA, 81% of chronic illness riders required no additional premium at issue (source: Life Combination Product Sales, 1st Half 2020). Many advisors promote these riders since consumers find the living benefits so attractive, particularly in the midst of a pandemic.

Comparing Chronic Illness Rider Payouts

Benchmarking life insurance has always been essential to the sales process for firms and advisors. Interestingly, as prevalent as the chronic illness riders that do not charge until acceleration have become, far less attention has been given to how widely benefit amounts can vary or what the actual cost to accelerate is (at the time of claim). This makes sense, considering the priority of a life insurance sale should be on the life insurance need. Additional benefits like cash value growth or accelerated benefits are a secondary focus. Still, as these riders continue to grow in popularity with many advisors focused on their value proposition, maybe it's time to lift up the rug and compare?

How Much Can you Accelerate Assuming $500k Death Benefit Comparing 7 IUL Products?

Well, it depends.

Company	Payment	Accel Benefit Amt Age 50	Accel Benefit Amt Age 75	Accel Benefit Amt Age 85
Discounting A	Total Amount	219,000	406,000	552,000
Discounting B	Total Amount	383,000	401,000	470,000
Discounting C	1st yr. payout Amt	94,000	117,000	146,000
Discounting D	1st yr. payout Amt	65,000	99,000	109,000
Discounting E	1st yr. payout Amt	61,000	97,000	108,000
Discounting F	1st yr. payout Amt	82,000	108,000	113,000
Lien Method G	Total Amount	250,000	250,000	250,000

Values in the chart are rounded to the nearest $1,000 for simplicity.

Assumptions: Male Age 45, Preferred Non-tobacco, $6,500 Annul Premium Paid to Maturity, $500k DB, 5% illustrated rate, S&P 500 Annual PtP (where available), GPT.

Benchmarking Observations

- **1st Year Payment or Total Payment?:** Companies A, B, and G reflect the total cumulative maximum benefit amount eligible to be accelerated. Others are reflecting the total maximum amount eligible to be accelerated for the 1st year on claim. Note that even if a total lump sum payout is available, some companies limit the maximum amount paid out in any given year.
- **Maximum Amount:** All the company benefits reflect the maximum acceleration amount whether that is an annual or total amount. This means that the actual benefit amount can be lower depending on the severity of the condition (life expectancy) or interest rates (discounting) that the company assumes at the time of claim. Note that some companies are able to reflect a higher benefit since they assume HIPAA per diem amounts being adjusted for inflation, which are projected out to the time of claim.
- **Discount Method:** With the discounting method, both the charge and benefit amount are unknown until the time of claim. Discounting factors can vary by age, life expectancy, severity of condition, gender, future premiums, cash value, permanent or term product, and interest rate. We can see some of this interplay explicitly when less is eligible to be accelerated at the younger age of 50 as compared to age 75/85.
- **Lien Method:** With Company G we see that the dollar amount is the same for ages 50, 75 and 85. As with all the other companies, the $250k is reflecting the maximum amount eligible to be accelerated. With a lien, the chronic illness benefit amount is known at issue, but the death benefit paid out is unknown. The charge (lien) is applied against the declining death benefit. The longer the insured lives after acceleration, the larger the lien amount grows reducing the remainder death benefit.

- **Cost to Accelerate Total Amount:** As an example, with Company A, the cost to accelerate at age 50 would be $281,000 ($500k – $219k benefit paid out = $281k charge).
- **Cost to Accelerate 1st Year Payment:** As an example, with Company E the cost to accelerate at age 50 would be approximately $256,000. ($61k annual benefit paid x 4 years = $244k. $500k – $244k paid out = $256k charge).
- **Benefit Amounts Vary:** No matter if it's an annual payment or total cumulative amount, benefit amounts vary substantially. For example, at age 50, Company C is approximately: $94k x 3 years = $282k vs. Company B at $383k.
- **How is it Possible to Accelerate more than $500k?:** At age 85, Company A reflects more being accelerated ($552k) than the initial specified amount ($500k). This assumes the policy had hit corridor increasing the death benefit based on the favorable illustration assumptions. However, it doesn't mean this amount will be available, since policy premium patterns and performance will impact the death benefit. Also, some carriers like Company A reserve the right to reduce the maximum chronic illness acceleration amount after policy issue.
- **Pay Premiums while on Claim:** Typically, premiums are still required to be paid after acceleration, and failure to pay can result in the policy lapsing even while on claim.

Conclusion – Apples and Oranges and Pears

At the outset, our hypothesis was to demonstrate the value of benchmarking these "no charge" chronic illness rider benefits and their associated costs as a potential best practice. However, since there are currently no industry standards in illustrating them, it is like comparing apples to oranges and pears. Given how drastically benefits and costs vary from company to company in just one underwriting scenario, it becomes an incredibly complex task to effectively benchmark these riders, much less when accounting for other factors when going on claim. They simply are not fair comparisons. For the time being, it seems that the better option is to become keenly aware of how widely benefits and costs can vary, and to make sure they are adequately disclosed so that firms, advisors, and most importantly, consumers can have a better understanding of how they work.

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