

Life Insurance Policy Evaluation Report: Termination Options

Sample Life Insurance Policy #XXXX

Prepared for:

by Anthony Steuer, CLU, Life Insurance Analyst

Evaluation:

Per our discussion, the primary issue is whether CLIENT should continue this policy or surrender it and the consequences of doing so. Based on our discussions, CLIENT has no current need for life insurance.

In regards to the policy, according to the submitted in-force illustrations and most recent annual statements, the current dividend option is "dividends paid in cash" and they are applied to pay premiums.

IF A POLICY LOAN: The policy as of March 28, 2008 has a loan balance of \$12,289.49. The loan has a negative impact on the overall policy performance. LIFE COMPANY has provided 3 in-force scenarios.

LIFE COMPANY has not provided clear information on these in-force illustrations, however, as the main concern is not continuing the policy this should not be an issue. While it is not explicitly mentioned, it appears that the interest on the loan is borrowed each year. The effect of using additional policy loans to pay the interest will continue to have an increasingly negative impact on the policy resulting in a scenario whereby loan interest will need to be paid out of pocket or the policy will lapse. The good news is that based on the current dividend scale and other current assumptions (costs of insurance and expenses) - will at the outset be minimal - though it will steadily increase (values appear on the second page of this evaluation in the options section). And even if the loan interest is paid out of pocket, once the loan balance is subtracted, the net death benefit will be minimal.

If loan interest is paid out of pocket, CLIENT will be able to continue the policy to its maturity date of policy age 95. However, by the last year of the policy, the annual outlay (based on current assumptions) will be \$462 and the policy would mature (terminate) with a net cash surrender value of \$686. Income taxes would also be due at that time on any gain in the policy.

Note: The life expectancy projection is from the 2001 Commissioner's Standard Ordinary Mortality Table. This figure is based on the average American Female and CLIENT life expectancy is most likely longer.

Recommended Action:

As CLIENT does not have a current need for life insurance, and the net death benefit is minimal as well as the fact that loan interest payments are projected to be required in the next few years, this policy should be surrendered. As illustrated in option 1 on the second page of this report, the situation will deteriorate. An article on policy loans is being sent as a supporting document on this subject.

Surrendering the policy will create a taxable event for CLIENT as follows: taxable income is calculated based on total gain in the policy less basis. Based on the summary of data dated March 20, 2008, an approximate calculation would result in a estimated net taxable gain of \$6,049.73 (the net cash surrender value was \$2,370 and the loan balance was \$12,289.49 for a total gain of \$14,660.12 less the basis of \$8,610.39). Therefore, assuming that CLIENT tax rate is 35% then the tax would be approximately \$2,117.41 which is slightly less than the net cash surrender value resulting in no additional cash out of pocket.

Please note that this is based upon my understanding of the tax law and that this not tax advice nor am I a tax advisor. Please consult your tax advisor.

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Options for CLIENT:

- Continue the policy as is. This year's net death benefit is \$40,336. Based on the current projected dividend scale, costs of insurance and policy expense charges combined with continuing the loan and paying the minimum loan interest: the net death benefit will decrease each year and will be \$31,422 in ten years and \$21,724 in twenty years. The net cash surrender value will decrease to \$686 and remain at that level for the duration of the policy. Payments will also start to be required to be paid out of pocket in four years in the amount of \$63; \$37 in ten years, \$162 in twenty years and \$452 in thirty years. If the assumptions are accurate (which is not likely) and CLIENT lives to the policy maturity date of age 95, her taxable gain subject to income tax at that point would be \$36,458 (net cash surrender value of \$686 plus loan balance of \$44,382 less basis of \$8,610). Also, she will have paid close to \$10,000 for the loan interest. If the performance of the policy is less favorable than the projections then the impact will be worse.
- Continue the policy and pay off the loan. This will require a payment of approximately \$12,400+ out of pocket for a policy with a net death benefit of \$40,000+ at that point. LIFE COMPANY did not provide the requested in-force illustration for this scenario. However, it does not seem likely that this would be worthwhile.
- Surrender the policy which will create a taxable event for CLIENT as follows: taxable income is calculated based on total gain in the policy less basis. Based on the summary of data dated March 20, 2008, an approximate calculation would result in a estimated net taxable gain of \$6,049.73 (the net cash surrender value was \$2,370 and the loan balance was \$12,289.49 for a total gain of \$14,660.12 less the basis of \$8,610.39). Therefore, assuming that CLIENT's tax rate is 35% then the tax would be approximately \$2,117.41 which is slightly less than the net cash surrender value resulting in no additional cash out of pocket.
- Sell the policy in the secondary marketplace

This evaluation was performed on June 23, 2009 and is only valid for that date.

This evaluation was based on the information provided and makes no guarantees or obligations

Financial Strength Ratings:

The financial strength of a life insurance is highly important as a life insurance policy is a long term investment. Life insurance companies are evaluated by ratings services and represent their independent opinions after evaluating a company's financial condition and operating performance, using their specific criteria. The ratings agencies assign ratings of a company's financial strength and ability to meet obligations to policyholders. The following are the financial strength ratings for your submitted life insurance policy's current company (due to mergers and spin-offs), your current company may not be the same as the original company which is a good reason to continue to monitor the financial strength. The relative rank is included to give you a sense of how the ratings compare. Some insurance companies are not rated by all of the rating services. For further information on ratings (and contact information for the rating services), please visit the ratings area on my main website at www.tonysteu.com in the resources section:

Please see the attached life insurer financial profile for ratings for LIFE COMPANY. Further financial information is available upon request.

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