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Fusty Insurance Lures Buyers Seeking Safety

Whole-Life Policies Offer Steady Ride, but Figuring Actual Returns Can Be Tricky

By M.P. MCQUEEN

(See Correction & Amplification below.)

As the economy sinks, a growing number of Americans are turning to a stodgy financial product favored by their parents and grandparents: whole-life insurance.

These policies' steady, tax-deferred returns, many now in the 4% to 5.5% range or more over 20 years, look enticing after the 40%-plus declines in the stock market over the past year and a half. Indeed, investor angst is helping insurance agents sell whole-life insurance.

Whole-life policies are "permanent" policies that include a guaranteed savings component, as well as a death benefit. They differ from less-expensive term-life insurance, which provides only a death benefit in return for premiums paid over a specific period and offers no cash buildup.

But potential buyers of whole-life insurance should be aware of its downsides. Because it isn't a transparent product, it's difficult to assess what its actual returns are. Part of the policy's returns may also include a partial return of premiums paid. In other words, you may be getting some of your own money back.

Though many risk-averse consumers are attracted to whole life, the insurance presents its own set of risks. A whole-life policy can bind the owner to the fate of a single company for decades, with steep costs to get out early. Some insurers now struggling looked very strong as recently as two years ago.

For all these reasons, many financial advisers recommend against purchasing whole-life insurance primarily as an investment vehicle.

Additionally, whole-life policies often must be held for 20 years to realize any actual gains because of stiff charges loaded in the early years of the policy -- including commissions and administrative fees. Yet 44% of whole-life policies lapse in the first 10 years, according to

Limra, the insurance industry research group -- which means that policies terminate after people stop paying premiums.

Term life insurance, by contrast, provides a larger death benefit for less money than whole life. Most families are better off using it to protect against the death of a breadwinner, says James Hunt, life actuary for the Consumer Federation of America.

The insurance industry, for its part, says whole life fills a key need for consumers when the stock market and other investments are hurting. "Life insurance offers the combination of death protection and some elements of accumulation," says Robert Chappell, the chairman, president and CEO of Penn Mutual Life Insurance Co. "It doesn't give you high return opportunities, but it gives you a steady source of accumulation along with life insurance protection."

Lynne Mazin, a 33-years-old bond seller in Larchmont, N.Y., recently purchased a whole-life policy for more than $200,000 from New York Life Insurance Co. Ms. Mazin, who is single, says she made the purchase knowing that many financial experts don't recommend life insurance for individuals without dependents, though she helps support her parents and a brother.

"I know I'm young and it is not traditional, and it is against some investment advisers' recommendations," says Ms. Mazin. "But we are in a new world in terms of overall market conditions." She also owns stocks and other assets.

Whole-life sales have been a bright spot in an otherwise tough landscape for the life-insurance industry. Many insurers have been rocked by declines in the value of their own investments, and some insurers have seen the stock of their publicly traded parent companies tank.

First-year premiums of whole-life insurance policies rose 2% last year at a time when life-insurance premiums overall were down 7%, according to Limra.

The lion's share of sales came from mutual insurance companies, which are owned by their policyholders. At New York Life, for example, new sales of whole-life measured in first-year premiums rose 11% in 2008 over 2007. At MassMutual Financial Group, first-year premiums rose 16% and the number of whole-life policies sold increased 13% in 2008 over 2007, according to the company. New whole-life premiums were up 6% in 2008 at Northwestern Mutual Life Insurance Co.

Mutual insurance companies argue that lack of shareholder pressure helps them adhere to more-conservative, long-term investment strategies. But that alone doesn't assure every mutual company's stability or the safety of its policies. A whole-life policy may not perform as expected if insurers' own investments aren't doing well.

Consumers are coming back to whole-life insurance after many years in which better returns were available in the stock market, and easy-to-understand, easy-to-buy term policies were getting cheaper.

Now, they are purchasing whole-life policies to replace "the lost or diminished value of their assets," said Steve Spiro, a spokesman for the Independent Insurance Agents and Brokers of America-New York in Valley Stream.

New buyers include affluent families who are worried about the possibility of higher federal and state estate taxes. They buy whole life and "permanent cash-value" policies to pay off taxes and preserve the rest of their estates for heirs. Others are using whole-life policies to endow charities.

Some consumers also buy whole-life policies because they can borrow against their cash value and use the funds to supplement their retirement or college savings. Small-business owners have long used them for business-succession protection.

Lou Kumar, 39, a cardiologist in Arlington, Va., says he probably wouldn't have given a whole-life policy a second look a few years ago when stocks were rising. But since then, he saw his mother's retirement plan shrink just as she was about to need it. Dr. Kumar says it made him worry about his own wife and child, and his ability to provide for them if he should die during a down market. He also owns mutual funds and real estate, he says.

"I like that fact that it was both protection and savings together," Dr. Kumar says. "My 401(k) looks like a 201(k). And who knows if Social Security will be around in 40 years when I retire?"

He acknowledges, however, that many of his friends weren't convinced, telling him to buy a term policy and invest the rest. He is paying a hefty $4,000 a month in premiums for a $2 million policy from New York Life with a $1 million term-insurance rider. Under the terms of the customized plan, he's scheduled to stop paying premiums at age 55 for lifetime protection. A 10-year term-life insurance policy for $3 million would cost him just $1,820 a year from the same company.

Whole-life customers can spread their risk by buying policies from several companies, but that may be impractical and costly. Because of long surrender periods and high surrender charges, it also doesn't make sense to buy a whole life policy for any short-term purpose, financial planners say.

Consumers should carefully research insurers and the whole-life policies themselves. You can check an insurers' financial-strength ratings -- a measure of its ability to pay claims -- by going to Web sites like Insure.com, which features ratings from Standard & Poor's. Or you can go to the ratings firms themselves, such as Moody's Investors Service, Fitch Inc. or A.M. Best Co., though you may have to pay a fee.

The Consumer Federation runs a Web site, EvaluateLifeInsurance.org, where buyers can purchase an evaluation of insurance policies. Consumers can also compare a whole-life policy against a similar amount of term insurance plus an equivalent fixed-income investment such as a municipal bond or bond fund, says Glenn Daily, a fee-only insurance consultant in New York.

"If you don't understand what you are buying, don't buy it," Mr. Daily says. "Whole life is one of the most complex financial products consumers are likely to buy."

Corrections & Amplifications

Standard & Poor's, Moody's Investors Service, Fitch Inc. and A.M. Best Co. don't charge fees for checking the financial-strength ratings of insurers on their Web sites. This article incorrectly implied that the firms may charge for the service.

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