Replacement Analysis and Processing

One of GPM Life's basic guidelines is not to support or condone either wholesale or indiscriminate replacement of existing life insurance policies. Replacement has many faces and names: twisting, churning, 1035 exchange, partial withdrawal, loaning, lapsing, forfeiting, surrendering, terminating, reissuing with a reduced cash value, reducing to paid up status, continuing as extended term insurance, automatic premium loan, surrendering dividends and reducing a face amount, reducing stopping or diverting premium to another policy, to name a few. In addition, replacement regulations generally apply even if the policy being replaced is not on the same insured.

A replacement situation exists whenever an agent knows, or should have known, that a change of policy status will, or is likely to occur, regardless of which company's policy is replaced. Our concern is that the purpose of a replacement is to improve the customer's situation, not just to generate new commissions.

We do understand, however, that there may be legitimate instances when a replacement is warranted. That is if, and only if, the insured's position is, in fact, improved. The burden of proving that a customer's position will be improved lies with the replacing agent tempered by the understanding that the Home Office always has the duty of oversight and must exercise due care and supervision regarding replacements.

GPM Life's position regarding replacements is as follows:

> *The selling of life insurance and annuity products should be based solely on the need of the client. To determine what those needs are, a fact-finding process is necessary. Full and accurate descriptions of products and services are required. A product must be "suitable." A suitable product is one that is appropriate for the client's needs and circumstances.*
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> *A client may want to replace an existing product with a new one rather than adding to what is already in place. It is rare that replacement of a policy is preferable to keeping or supplementing what is owned already. However, if after careful and complete study and full disclosure of all pertinent information, a replacement is clearly in the best interests of your client, it must be done in accordance with GPM Life's rules, and in accordance with replacement, churning, and twisting regulations in effect in that state.*

How should agents proceed after determining that replacement in a given situation might be a proper recommendation? Here are a few rules of thumb:

1. Provide all disclosures required by your state and by GPM Life:

PLEASE NOTE: Replacement business is **not accepted** for sales in KS, KY or WV.

For NAIC Model Replacement Regulation States: Use form "58A REPLMOD" in AL, AK, AR, AZ, CO, CT, HI, IA, KS, KY, LA, MD, ME, MS, MT, NC, NE, NH, NM, OH, OR, RI, SC, SD, TX, UT, VA, VT, WI, WV

For Non-NAIC Model Replacement Regulation States: Use the specific state's replacement form and GPM Life's "Understanding of Policy Replacement (form 01.56)" in CA, DE, FL, GA, IL, IN, MA, MO, NV, OK, PA, TN, WA, WY and EUROPE.

For states without any replacement form requirement: Use GPM Life's "Understanding of Policy Replacement (form 01.56)" in AK, CT, DC and ME.

2. Provide information that clearly demonstrates why the replacement Is In the best interest of the customer, based on some reasonable analysis.

Here are examples of *unacceptable* language we sometimes receive as responses to the statement on a replacement form:

"The existing policy or contract is being replaced because:____."

An agent:

- Omits any comparison; typically there is there no answer at all.
- States, "It's better"
- States, "Living Benefits"
- States, "Found better coverage"
- States, "Increase years, decreases premium"
- States, "Wants a term policy rather than whole"

3. Are you replacing an existing term policy with a GPM Life term policy that is cheaper, has a longer premium guarantee period, or has more insurance for the same money? Indicate that on the application. Those reasons are well understood and generally sufficient, but when omitted, could cause underwriting delay because the reason isn't clear.

4. Replacing an existing term policy issued by another company with a GPM Life permanent policy? Indicate that on the application. While it is like a term conversion, it is still a replacement in most states and requires normal replacement procedures to be followed. "Term to permanent" is a good and sufficient reason that, when omitted, can cause an underwriting delay because the reason isn't clear.

5. Describe why the policy you are recommending will be better than the policy your customer now owns at specific points in time in the future, such as the 5th and 10th year from now.

6. Discuss the situation with your GA, MGA or RDA to recommend the best information to provide to expedite your applications through the underwriting process.

7. Always keep the customer's best interest in mind. Be sure the customer understands that he/she should keep existing coverage in effect until after the application is through the underwriting process and a policy issued, if any. The new policy should be delivered and accepted before the existing coverage is dropped.

It is not GPM Life's intention to tell any agent how to justify a replacement in such a manner that the agent essentially rubber-stamps our reasons on a state replacement form. Each agent must first evaluate the situation at hand and then determine if there are good and sufficient reasons for a replacement.

During an examination by a state insurance auditor, it would fairly obvious to that examiner that a reasonable evaluation has not taken place in every sales situation, if all of the reasons on all replacements are exactly the same. Many cases may have similar reasons, but not every single one and not every time. Options for corrective action as a result of failure to comply fully with replacement laws can be large monetary fines, license suspension or license revocation.

A significant aim of correctly completing replacement forms is for the protection of both the writing agent and the company, should there be future litigation regarding the purpose and suitability of the sale. A properly completed replacement form is a significant and vital piece of evidence regarding agent intent, customer concurrence and company compliance with the law.

Replacement Analysis

In order to determine whether replacement of an existing policy with a new one is justified, the agent should not select only one reason why it might be in the customer's best interest. Instead, a variety of factors should be evaluated:

Whole Life

If replacing a Whole Life with a new Whole Life, evaluation is much more straightforward. The agent can compare premium and cash values by doing a side-by-side comparison of illustrations and/or statements with projected values, review the contestable and suicide period changes, and whether the existing and new policy may be eligible to share in any dividends declared by the company.

If replacing a Universal Life with a Whole Life policy, the evaluation can involve a variety of things, including the values that are guaranteed on one policy versus the other. The agent should fully explain why the current policy no longer meets the needs of the proposed insured and why the new one better suits those needs. A side-by-side comparison of current and projected values, premiums and benefits will help determine why one may be better than the other. An Insured may prefer fully guaranteed cash values of Whole Life instead of the non-guaranteed elements of a Universal Life plan

Universal Life

One of the most complex replacements has to do with replacing of one universal life policy with another. Due to the nature of the product, Universal Life insurance involves a variety of factors that may change over the life of the policy. The only accurate way to do a comparison is by using a current illustration of the existing policy and an illustration for the proposed policy. More than one factor is going to affect a decision. As an example, a higher current interest rate alone is not enough. Gains from a current interest rate may be negated by a surrender charge on the existing policy. Only by thoroughly evaluating both the existing and proposed policy can a recommendation be made. Here are some of the factors for consideration:

a. Is there still a surrender charge? How is the proposed insured going to be able to recover the surrender charge? Is it to the advantage of the proposed insured to wait until the surrender charge is reduced?
b. What is the current interest rate on the existing policy versus the current interest rate on the proposed policy? How long is the current interest rate guaranteed on the new policy, if at all?
c. What is the guaranteed interest rate on the existing policy versus the proposed policy?
d. How do the policies compare at current rates, midpoint rates and guaranteed rates at 5 years, 10 years, etc.?
e. Is there a cost advantage to the proposed policy in premium or in the current cost of insurance and monthly deductions? Although one company may call rates "standard" versus

"preferred," a fair evaluation would be to compare actual dollar amounts for cost of insurance, policy fees and premium loads, at both current and guaranteed costs.

f. Keep in mind when doing an evaluation that Universal Life policies, due to the nature of the product, all rates are subject to change. Simply doing a point in time evaluation today is not enough to recommend replacement. Be sure that the customer understands that many factors in the mortality experience of the company and in the economy can affect future rates on both policies.
g. It is imperative that you, as the replacing agent, explain that replacement of existing insurance involves starting over with new contestable and suicide periods, and starting over with a surrender charge period.

After a thorough evaluation of the replacement and a comparison of the values on the existing policy versus the proposed policy, only then, if the agent and the proposed insured decide to proceed, should the replacement form be completed. The agent should give detailed reasons why it is to the advantage of the proposed insured based on the comparison he has made to the applicant.

Note: If the new application is not approved on at least as favorable a rate as applied for, a new review of the replacement by the Home Office will be needed. Replacement evaluation in the Home Office is done at the time the application is received based on the rating assumed by the agent on the illustration. If the application cannot be approved on that basis, the replacement will be evaluated again to see if the replacement can be approved.

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