Insurance Industry Woes Could Hit Consumers

by Reuters

WASHINGTON (Reuters) - Nobody wants to feel sorry for life insurance companies. They're just the annoying folk who make you think about death, cash your checks, and then give you grief if you ever have to file a claim, right?

Don't be so cynical. These are challenging times for the insurance industry. Company representatives meeting in Washington for the annual American Council of Life Insurers conference seemed downright gloomy, and were eager to tick off the troubles facing them.

Low interest rates mean insurers can't easily price or profit from the annuities they are selling. Bad and uninformed pricing decisions mean they may lose their shirts on some long-term care and annuity plans they sold years ago. Some companies are leaving markets they used to find profitable and trying to invent new and complex products to fit the "new normal." And they are afraid that forthcoming tax reform will hit their products big time.

You know what all that means: It's going to cost you. Here's how those industry challenges will hit your wallet and what to do about it.

-- Interest rates are low and staying there for a while. That's really the insurance industry's biggest challenge. When an insurance company sells fixed annuities (which promise purchasers monthly income for life), it typically buys bonds to secure the income it's promised to deliver. But with 10-year Treasuries paying less than 2 percent a year in interest, it's hard to guarantee that long-term stream of income.

How that affects you: If you're thinking of locking up your money for long-term retirement income, be aware that you're doing that near a market bottom, in terms of yield. Don't plunk down all the money you've set aside for annuities at once. Buy some now and some in a few years. Yields are likely to be better after 2014.

-- Mistakes were made in the long-term-care insurance field. Companies that jumped into that product space early didn't really understand just how pervasive and expensive such care was going to be. They may not be able to afford the bill for a generation of chronically ill baby boomers. Several insurers have walked away from issuing new policies.

Some companies are raising premiums - sometimes aggressively - on existing policies. Check this out: The California Public Employees' Retirement System (CalPERS) Board of Administration just approved an 85 percent increase in its long-term-care insurance premiums. It's not unusual to see rate hikes of 20 percent or more.

How that affects you: You may worry about needing long-term-care insurance, but you may not be able to afford it. If you're convinced, based on your health and finances, that you do need this coverage, look for a plan that limits payouts to three or five years, is issued by a company that has a sizeable long-term-care business and a top rating, and that you could afford to keep in place even if premiums were to rise by 50 percent.

-- Old variable annuities were too generous. It's ironic that they had a bad reputation as consumer ripoffs because of their high fees. Their structures, which allow investors to invest in the stock market and still keep fat guaranteed returns, are proving to be costly to insurance companies. Some firms are actually trying to buy back their old annuities by offering lump sum payments to policyholders.

How that affects you: If you own an older variable annuity, don't be surprised if you get a lump sum offer. You'll probably have to take that to a smart adviser - one who understands insurance, life expectancy, the financial markets and more. Together you'll have to decide which is the better long-term outcome for you, based on your own life expectancy, health, where you'd put that lump sum, and other factors. Just remember, there's a reason the company thinks it will save itself money by buying you out.

-- Tax breaks could disappear. The cash-value life insurance and annuities industries are built on the tax breaks that accrue to their policyholders. Money you earn within an insurance policy is typically tax-deferred or tax-free, depending on how the product is structured and how you access the benefits. If Washington gets its act together in 2013 and "fixes" the fiscal cliff by reforming the income tax system, the value of insurance could suffer. Tax breaks for earnings inside of insurance policies could be limited for big policies or high-earning policyholders. Top tax rates could conceivably drop, if enough "loopholes" were closed. That would hurt the insurance industry.

How it affects you: Unless you are in a stratospheric tax bracket, try not to let tax savings drive your insurance purchases; only buy products that make sense because you actually need insurance guarantees. If you are in that elevated tax bracket, call your insurance adviser, because there's a good likelihood that whatever made sense for you last year or the year before will need to be adjusted. A change is going to come.

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