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Research Brief #2

What is the value of an extended maturity provision?

Most life insurance policies mature at age 95 or 100. The contract usually explains what happens at maturity.

If the policy does not have an extended maturity provision, the insurance company will pay the cash value to the policyowner, and the policy terminates. This will cause any gain to become taxable to the policyowner.

An extended maturity provision keeps the policy in force beyond the original maturity date. Premiums and policy charges stop, although interest usually continues to accrue. The death benefit may be equal to the cash value, or it may be equal to the death benefit before the maturity date.

When potential buyers estimate the value of a life insurance policy, they take account of the possibility that the insured will still be alive when the policy matures. Buyers usually pay the minimum premiums to keep a policy in force, so a policy with no extended maturity provision will be worthless at maturity, because the cash value is likely to be zero. The same is true if there is an extended maturity provision that provides a continuing death benefit equal to the cash value.

However, an extended maturity provision that maintains the pre-maturity death benefit does have value. How much could it be worth? Here’s an example.

Suppose a universal life policy has a level death benefit of $800,000, and it matures at age 95. It does not have an extended maturity provision. The insured is now 83 years old. The current cash value is about $39,000. This will cover the policy charges for the first nine months, but then the buyer will have to pay a monthly premium that gradually rises to about $9,500.

The potential buyer has obtained three life expectancy appraisals, showing these probabilities of survival:

Life expectancy source	Mean life expectancy (in months)	Probability of survival to age 95
Appraisal #1	69	8.7%
Appraisal #2	66	3.3%
Appraisal #3	58	0.2%

Here are the estimated purchase prices of the policy for each life expectancy appraisal, using four discount rates representing the buyer's targeted rate of return on investment.

Gross purchase price without extended maturity provision

(before deducting broker's commission and income tax)

	Buyer's rate of return			
Life expectancy source	8%	10%	12%	14%
Appraisal #1	$255,000	$235,000	$218,000	$203,000
Appraisal #2	283,000	258,000	235,000	216,000
Appraisal #3	342,000	313,000	287,000	264,000

Here are the estimated purchase prices if the policy had an extended maturity provision that maintained the $800,000 death benefit with no further premiums.

Gross purchase price with extended maturity provision

(before deducting broker's commission and income tax)

	Buyer's rate of return			
Life expectancy source	8%	10%	12%	14%
Appraisal #1	$279,000	$254,000	$233,000	$215,000
Appraisal #2	293,000	266,000	241,000	221,000
Appraisal #3	343,000	313,000	287,000	264,000

In this example, an extended maturity provision could increase the purchase price by thousands of dollars.

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