

IUL Basics

Brian Leising, CLU, ChFC, CASL
Life Insurance Specialist
Financial Brokerage,
a division of Art Jetter & Company Insurance Marketing



IUL Basics

- **History**
- **Index interest crediting**
- **Tax advantages**
- **Costs**
- **Where does IUL fit in retirement planning?**



History

How did we get here?



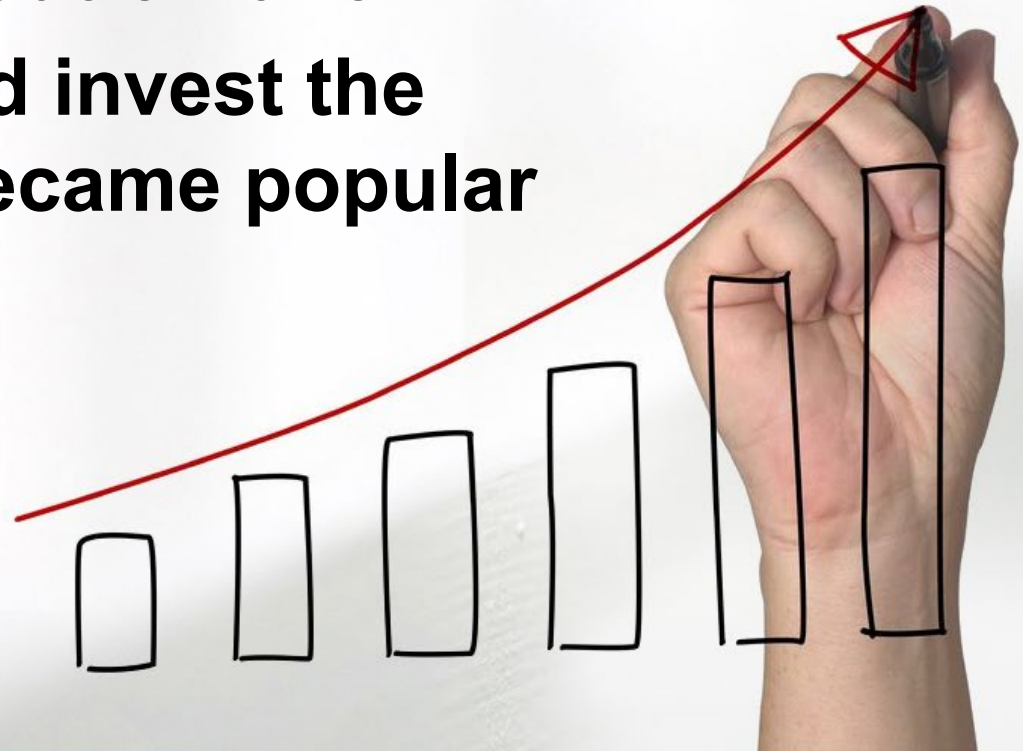
Life Insurance types

- **Whole Life – cash value, lifetime coverage**
- **Term Life – no frills temporary coverage**
- **Universal Life – whole life disassembled**
- **Variable Universal Life – UL with direct stock market participation**
- **Index Universal Life – UL with interest rates based on formulas based on stock market performance**



1979

- **CD's yielded 12%+**
- **Whole life insurance policies began to fall out of favor**
- **“Buy term and invest the difference” became popular**



1986

Introduction of VUL

Consumers had access to life insurance coverage with a policy value accumulation component directly tied to the performance of equity or fixed income investment options



1995

Introduction of Fixed Index Annuities



1997

- **Due to the success of Fixed Index Annuities, Index Universal Life Insurance was introduced**
- **The index-linked crediting strategies provide upside potential without the downside risk posed by Variable Universal Life Insurance (VUL)**



Index Universal Life Market

2006: \$ 350,000,000

2012: \$1,400,000,000

2018: \$2,100,000,000

2024: \$3,800,000,000



Product Uses

- **Protection**
- **Accumulation and Distribution**



Index Universal Life

How does index interest crediting work?





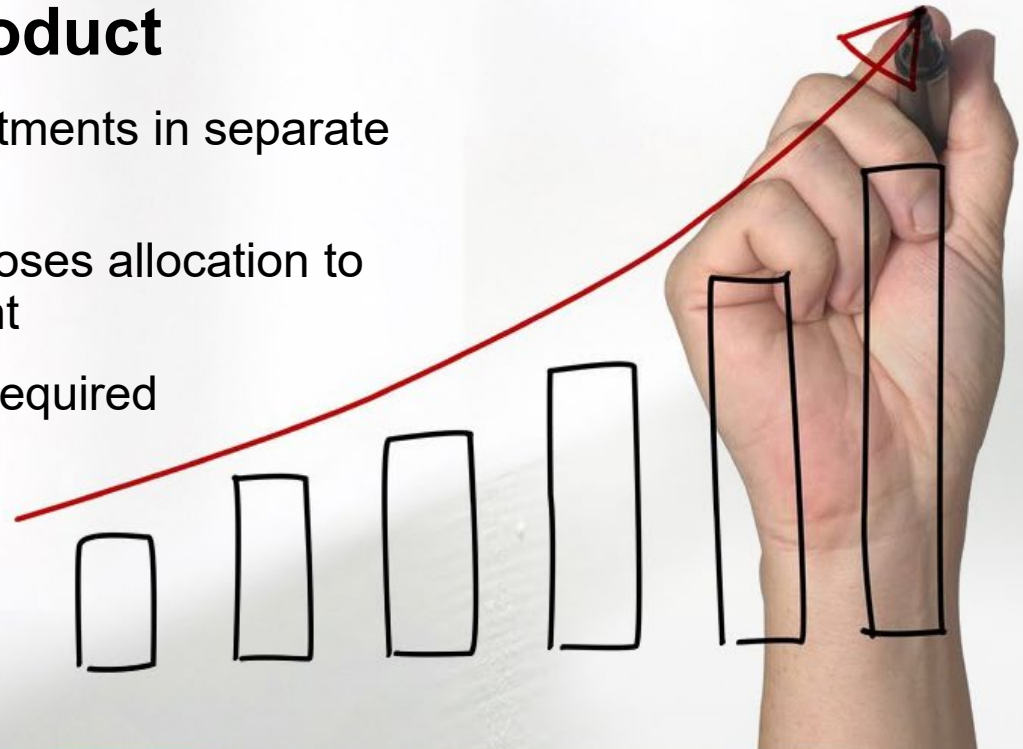
Different method for determining and crediting

Non-guaranteed interest

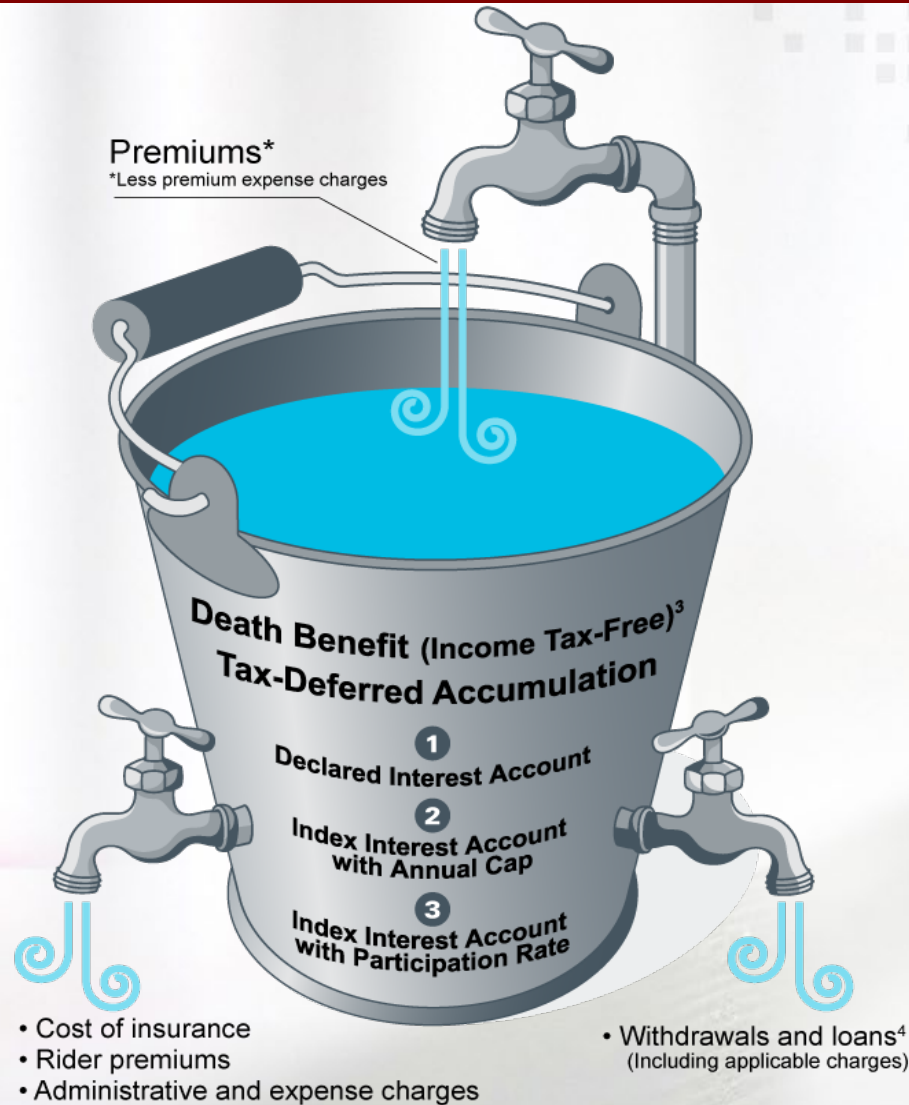
- **Fixed UL:** declared interest - by carrier (how are they determined?)
- **Index UL:** indexed interest - reference stock market index (formula based on **PUBLIC and PUBLISHED** information)

General account product

- No policy owner investments in separate accounts (unlike VUL)
- Policy owner only chooses allocation to index crediting account
- No securities license required



Crediting Process



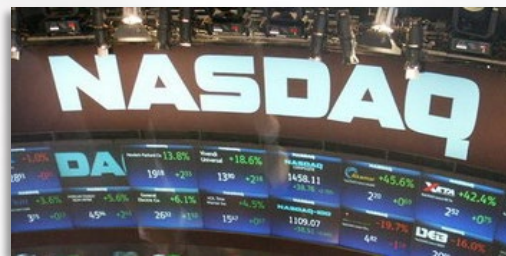
What Determines The Possible Interest Credits?



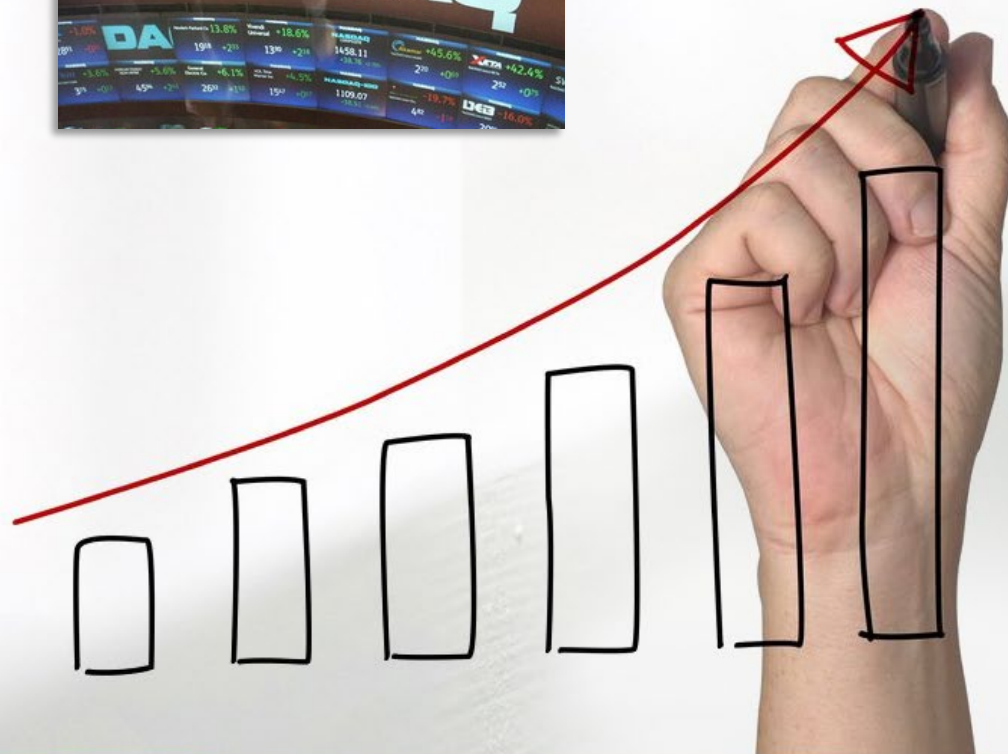
**STANDARD
& POOR'S 500**

DOW JONES

50
EuroStoxx



恆生指數
HANG SENG INDEX
23436.05
↑ 400.60



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Index Strategies

An indexed strategy uses a formula that calculates interest based in part on the movement of a stock market index, such as the S&P 500 Index

Index UL has different index strategies where your clients can direct their money in an effort to take advantage of positive movements in a stock market index

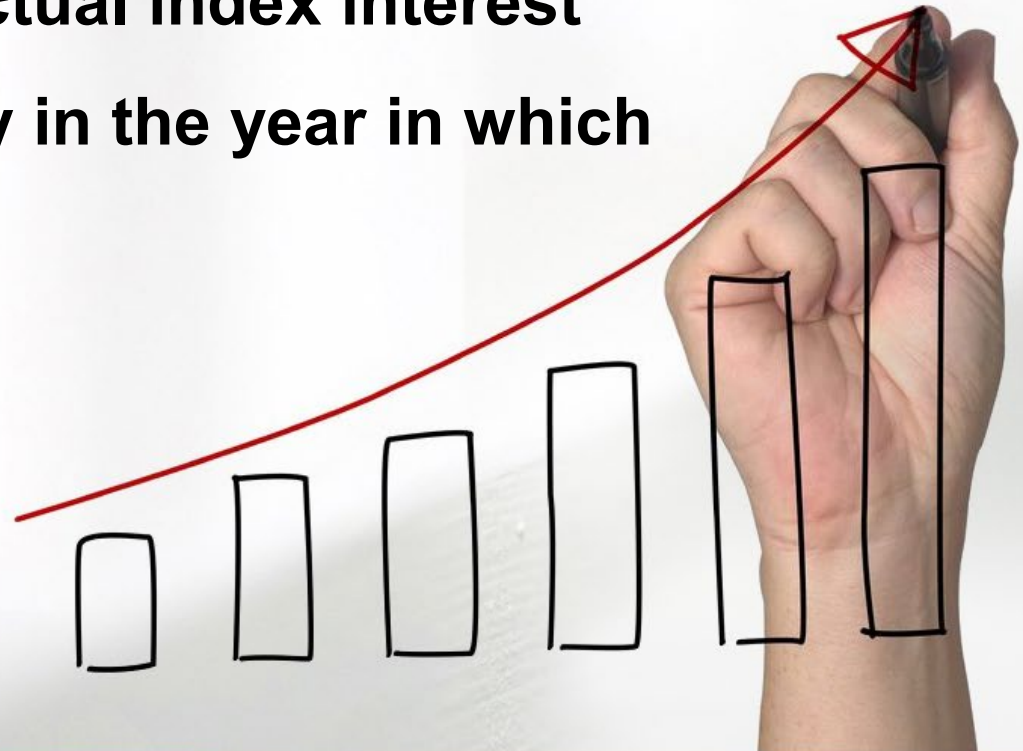


What Are The Moving Parts?



Participation Rate

The Participation Rate is the percentage of index interest growth (if any) the policy owner receives as actual index interest credited to the policy in the year in which crediting occurs



Cap Rate

The Cap Rate is the maximum point-to-point index interest growth (if any) the policy owner can receive as actual index interest credited to the policy



Determining Cap & Participation Rates

Step 1 - Premium invested in fixed income investments

Step 2 - Net investment earnings provide guaranteed interest rate

Step 3 - Remaining earnings purchase one-year or longer call options on the specific index or indices.

- Price of call options relative to investment earnings is primary factor in determining participation rate
- This is commonly referred to as a carrier's "option budget"



What Happens Next?

Market rises, call options are exercised

- Policy credited with indexed interest

Market decreases, options expire (worthless)

- Policy credited with guarantee, or
- Other selected policy options



Earned Rates Impact on IUL

6.0%

Company's Earned Rate on Assets

- 2.0%

Interest Spread/Guaranteed Interest

4.0%

Option Budget

(amount company has available to purchase options)

3.0%

Company's Earned Rate on Assets

- 1.0%

Interest Spread/Guaranteed Interest

2.0%

Option Budget

(amount company has available to purchase options)



Index Crediting Methods

- **Annual point-to-point**
- **Monthly point-to-point**
- **Daily or Monthly averaging**
- **Multi-Index weighted annual point-to-point**
- **Actively managed volatility control**



Annual point-to-point

S&P 500 6-3-24 5283.40

S&P 500 6-3-25 5970.37

+ 13%



Monthly point-to-point

Month	S&P	Cap	Credited Interest
January	5%	3%	3%
February	3%	3%	3%
March	2%	3%	2%
April	-2%	3%	-2%
May	-4%	3%	-4%
June	3%	3%	3%
July	8%	3%	3%
August	12%	3%	3%
September	-6%	3%	-8%
October	1%	3%	1%
November	0%	3%	0%
December	7%	3%	3%
Total			9%

Monthly Averaging

Month	Index Value
1	1,025
2	1,050
3	1,125
4	1,100
5	1,000
6	975
7	1,100
8	1,125
9	1,100
10	1,150
11	1,140
12	1,100

Average = 1,074

**Example of S&P® 500
Index Values on 14th Day
of Each Month**



Multi Index Weighted Point-to-Point

- **3 Indices used (S&P, EURO STOXX, Hang Seng)**
- **50% weighting to best performing index**
- **30% to second best**
- **20% to third best**



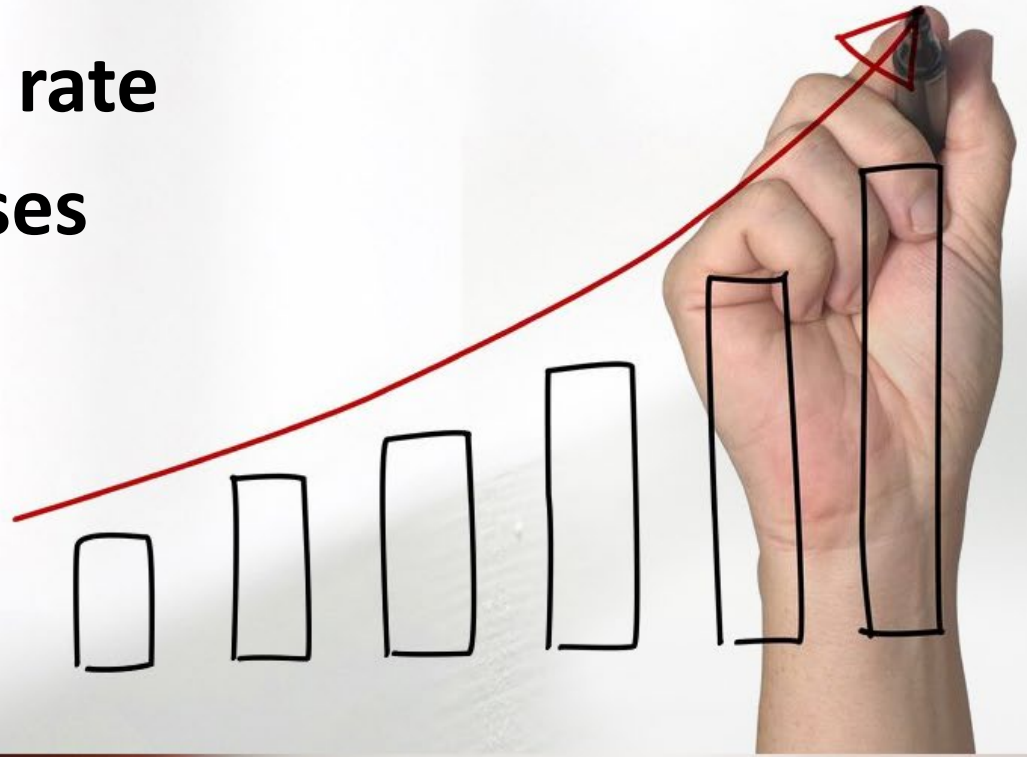
Actively Managed Volatility Control

- **Multiple indices**
- **Actively managed**
- **Volatility control (goal to minimize zero returns)**
- **Often uncapped**
- **Participation rate may exceed 100%**



Other Index Alterations

- **Uncapped**
- **High Cap**
- **Asset Fee**
- **High Participation rate**
- **Conditional bonuses**



What are we doing with this money?

- **Protection Focused IUL**
 - Typically lower caps and par rates
 - Money used to keep policy in force
 - Alternative to a GUL
 - Trading contractual guarantees for historical probabilities



What are we doing with this money?

- **Accumulation Focused IUL**
 - Typically higher caps and par rates
 - Money intended to be spent



Why Use Life Insurance?

(Why not index annuities?)



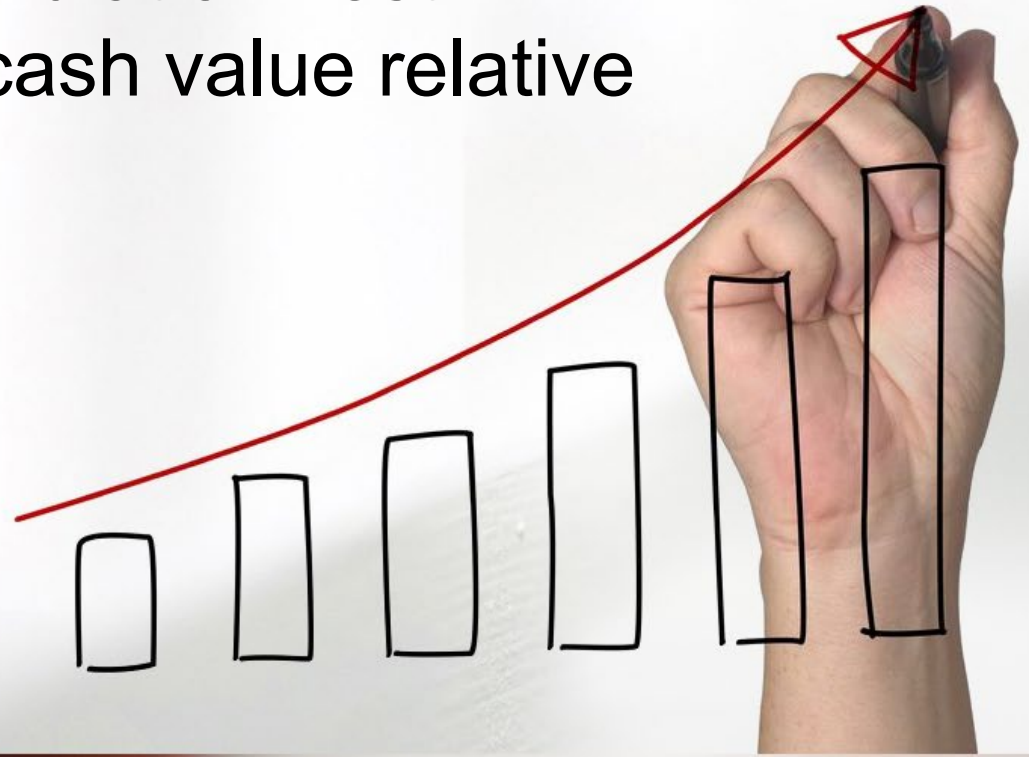
Taxation of Retirement Funds

1. **FREE-** inheritances
2. **TAX-FREE-** Roth IRA's, Life Insurance, Municipal Bonds
3. **TAX-DEFERRED-** Annuities, 401(k)'s, IRA's
4. **TAXABLE**



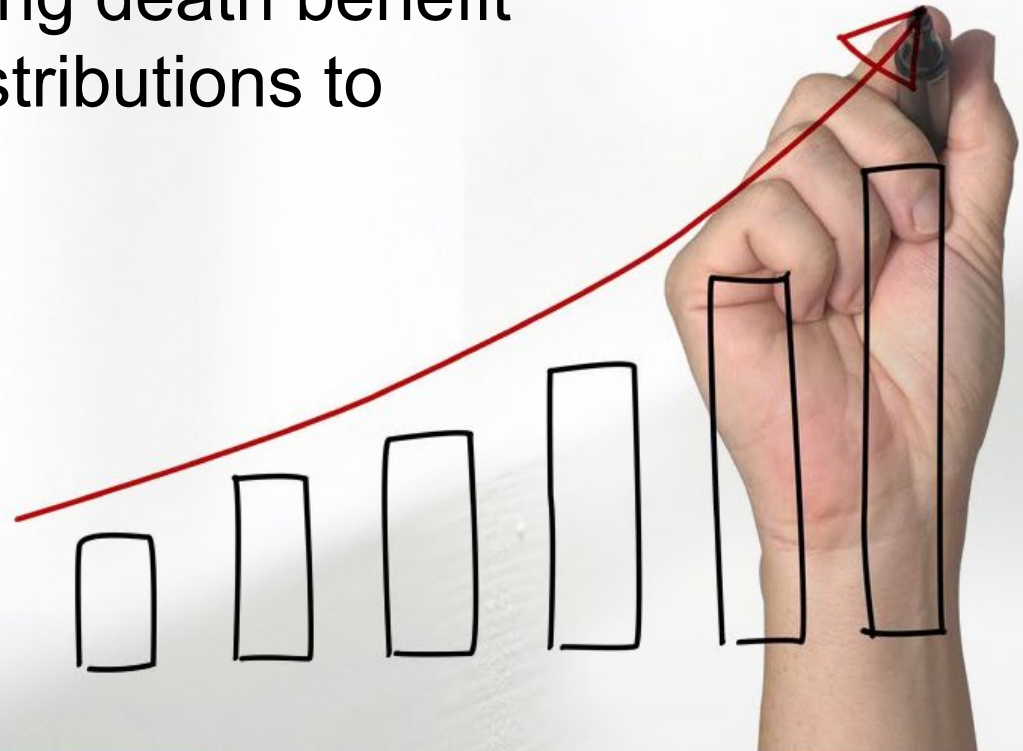
What Makes Life Insurance Tax-Free?

- Guideline Premium Test (GPT)- restricts paid premium relative to death benefit
- Cash Value Accumulation Test (CVAT)- restricts cash value relative to death benefit



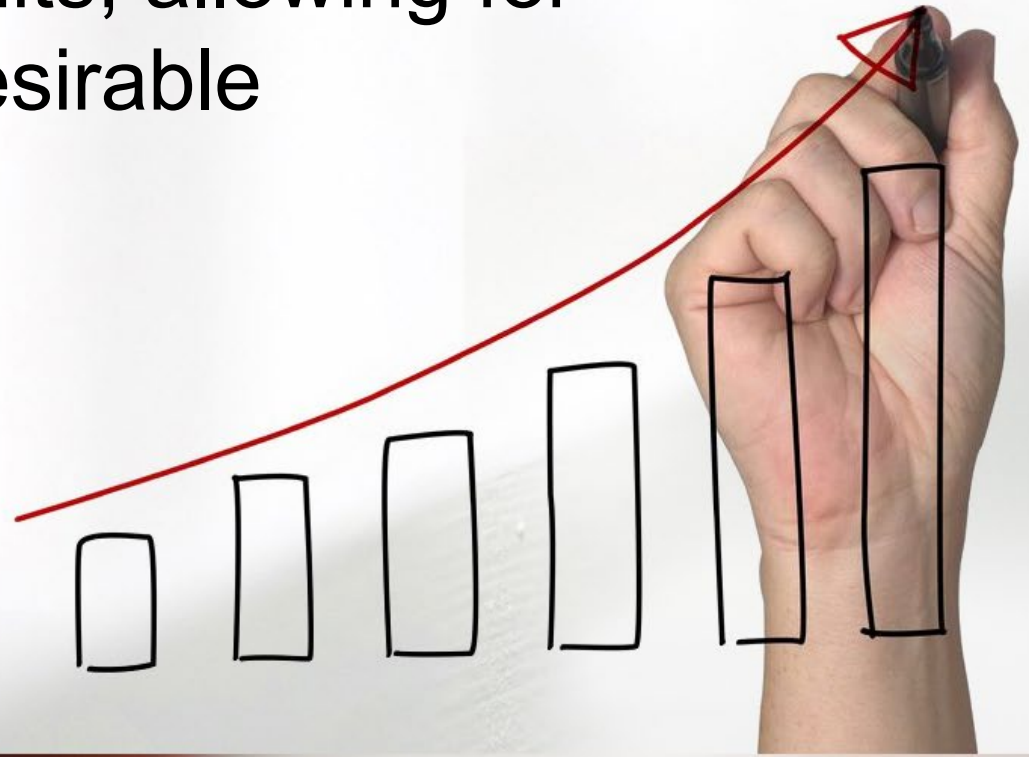
When to Use GPT?

- Paying max premium for 10+ years
- Desire max cash value and death benefit @ 100+
- Switch from increasing death benefit to level at start of distributions to maximize



When to Use CVAT?

- Short-pay scenarios
- Dump-ins, including 1035 exchanges
- No premium limits, allowing for MEC's when desirable



How Do We Get the Money?

- Withdrawals to basis
- Loans
 - Fixed (usually wash loans after year 10)
 - Participating/Variable/Index
 - Can keep policy value earning the full interest crediting rate, may or may not offset cost of loan



No Arbitrage (wash loan)

- Index credited rate 10%
- Traditional fixed loan 10%
- Net result 0%



Positive Arbitrage

Example 1

- Index credit 10%
- Loan interest 5%
- Net gain on loaned money 5%



Positive Arbitrage

Example 2

- Index credit 2%
- Loan interest 5%
- Net *charge* to loaned funds 3%



What are the costs?



Costs Compared

Account	Typical Fees
Variable Annuity	3.00%
Managed Accounts	2.04%
Small Employer 401(k)	1.27%
Large Employer 401(k)	1.03%
Index Universal Life	Less than 1.00%

*Source – “The No-Compromise Retirement Plan” by Martin H. Ruby

401(k) and IUL compared

Actual 401(k) fees

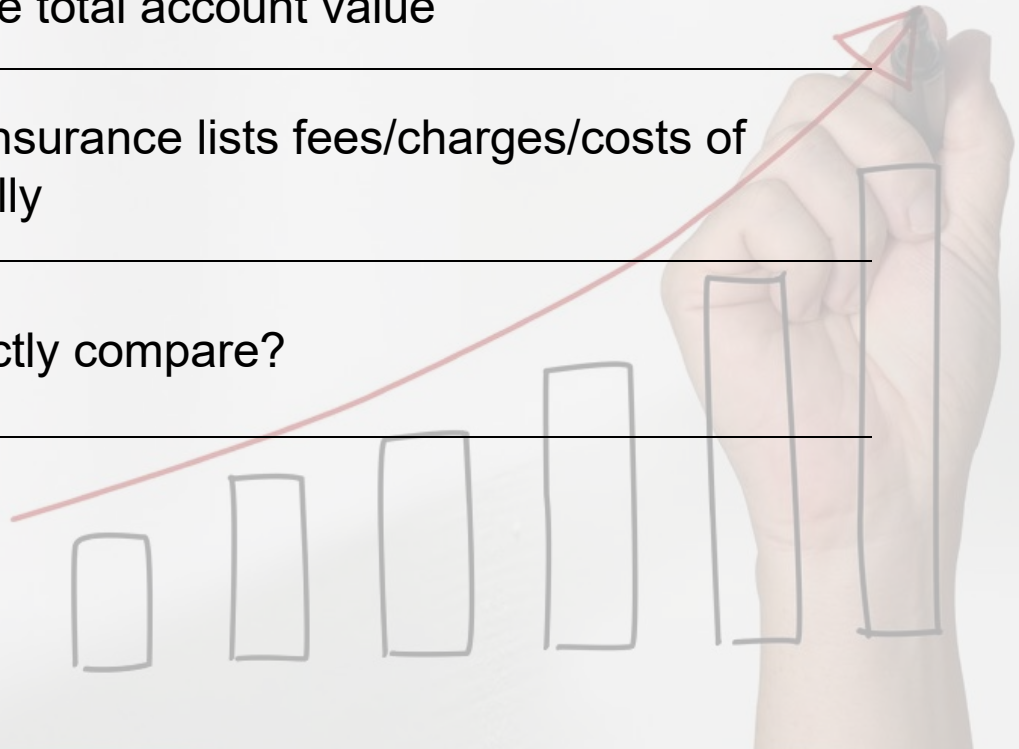
- ✓ 2017
- ✓ \$130,000 account value
- ✓ \$6000 annualized contributions
- ✓ \$352 annualized administrative charges
- ✓ 1.06% average expense ratios
- ✓ **\$1,731** total fees for the year

IUL illustration

- ✓ Same \$6000 contributed to IUL (male 44)
- ✓ average annual expenses (years 1, 10 and 20) = **\$1,000**

Comparing Expenses

- Other retirement products display charges as a percentage of the total account value
- Cash Value life insurance lists fees/charges/costs of insurance annually
- How can we directly compare?



Calculating average IUL expenses

- ✓ Life insurance fees/charges front loaded
- ✓ Cost of insurance charges change annually, increasing over time
- ✓ Consider the average charges over client's life expectancy (age 90)
- ✓ Illustrated rate of return minus surrender value internal rate of return equals average cost as a percentage of the cash value
- ✓ Formula: **Rate – CSV IRR = Costs**

Actual illustrated cost percentages

Male 40 best rate class \$6000/ year contribution for 25 years

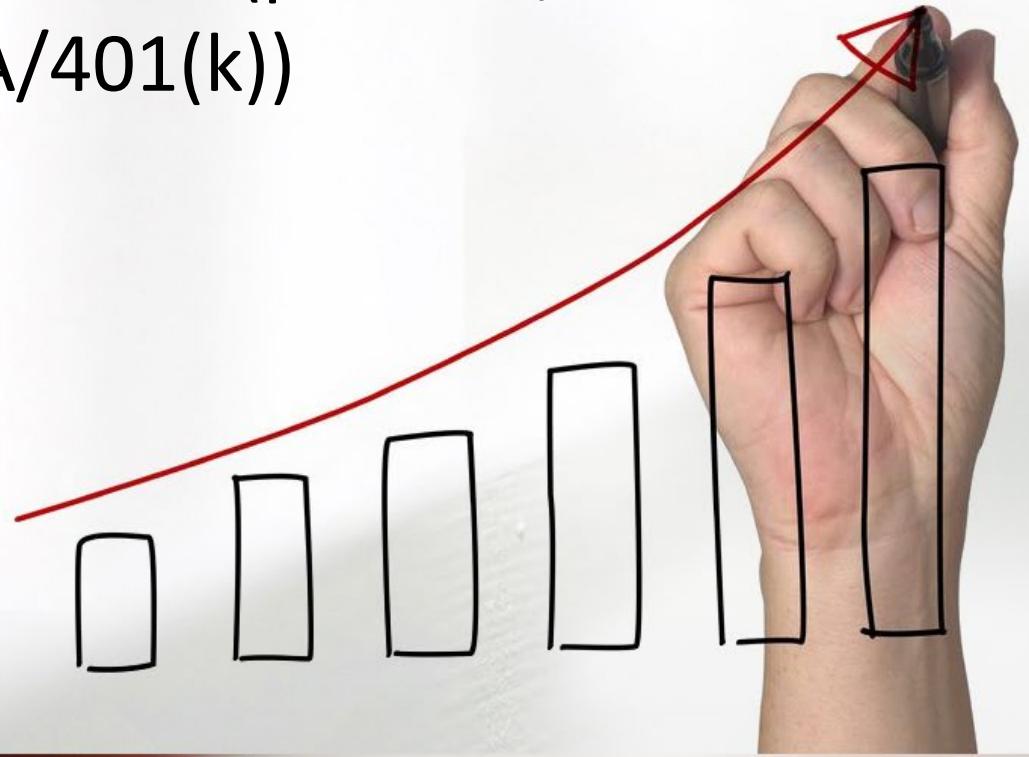
Company	Rate	IRR @ 90	Average Expense
A	6.20%	6.29%	-.09%
B	6.03%	6.28%	-.25%
C	5.59%	5.37%	.22%
D	5.70%	6.20%	-.50%
E	6.24%	6.89%	-.65%
F	5.47%	5.59%	-.12%

Where does IUL fit in retirement planning?



How does IUL fit into a retirement plan?

- Standard deduction (can take taxable income)
- Social security income (taxable?)
- Other sources of income (pension, taxable accounts, Roth IRA/401(k))



Determine premium

- Inquire about client's budget?
- Copy retirement plan contribution?
- Treat as piece of total retirement income needs?



Designing an accumulation illustration

- Determine premium
- Solve for minimum non-MEC face amount
- Death benefit type: Level, Increasing, Return of Premium?
- Illustrate withdrawals or loans?



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