

IUL Insurance Essentials to Grow Your Business

PART OF THE LIFE LESSONS SERIES



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IUL Insurance Essentials to Grow Your Business

Clients and prospects tend to have different expectations when it comes to life insurance. And the decision to purchase a policy may be met with hesitation, confusion or denial. As an agent, it is important for you to understand how to present this kind of solution, and to be able to separate fact from fiction so that your clients can make an informed decision. **Keep in mind that some myth-busting skills may be required!**

When most people think of life insurance, they think of death benefit protection, but what if they knew about tax-free income and living benefits? It is important to understand the essentials of Indexed Universal Life (IUL) insurance so that you can overcome objections and know when it might be appropriate for your clients. This will help you better incorporate IUL insurance into your practice and help you achieve business growth.

- Chapter 1 An Overview of IUL Insurance
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An Overview of IUL Insurance

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Indexed Universal Life (IUL) insurance is one of the fastest growing life insurance segments in the industry topping \$1.86 billion, an all-time high for the product¹.

IUL insurance is considered permanent insurance. The universal portion means that the premiums are flexible and the components of the life insurance policy (death benefit, savings element, and premium) can be altered throughout the contract. IUL insurance policies give the policyholder the opportunity to allocate cash value amounts to an index to potentially increase cash value. IUL insurance policies typically contain a minimum guaranteed, fixed-interest rate component along with the index allocation option. This helps reduce the impact of negative market conditions and can provide upside potential for the policyholder.

CLIENT MYTH:

Life insurance is confusing.

BUSTED!

We have dedicated employees with the knowledge, tools and resources to help you become comfortable with presenting IUL insurance policies.

¹SOURCE: WINK, INC.

<https://insurancenewsnet.com/innaarticle/indexed-life-sales-dip-1-3-4q-flat-2016>

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Key Product Features of IUL Insurance and Primary Benefits

There are numerous reasons why IUL insurance is one of the fastest growing life insurance products on the market today. Understanding the features and benefits of IUL insurance can help you decide when to incorporate it into your client's retirement plan. It's important to note that some of these features are options, such as riders, and may include a fee. There are many riders and features that are available to best suit your client's individual needs.

Some key product features and benefits include:

- Death benefit options
- Tax advantages
- Living benefits
- Flexibility and control
- Funding options
- Policy loans

CLIENT MYTH:

IUL insurance policies have limited upside potential.

BUSTED!

IUL insurance policies may include strategies that have high caps or NO caps that allow clients to capitalize on years where the market may have an increase.

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Death Benefit Options

There are different ways to structure an IUL insurance policy when considering death benefit options and the needs of your client.

There are two types of death benefits – **level and increasing**. With a level death benefit option, the death benefit remains unchanged throughout the policy. On an increasing death benefit, the death benefit equals the face amount plus any cash accumulation.

There are also both **guaranteed and non-guaranteed** death benefit options. For a guaranteed benefit, the client is assured a death benefit as long as the premiums are paid. With a non-guaranteed death benefit, the death benefit is based on the cash value of the policy. As long as there is \$1.00 of cash value in the policy, the policy would remain in force minus any loans, withdrawals, or acceleration of Accelerated Benefit Riders (ABRs).

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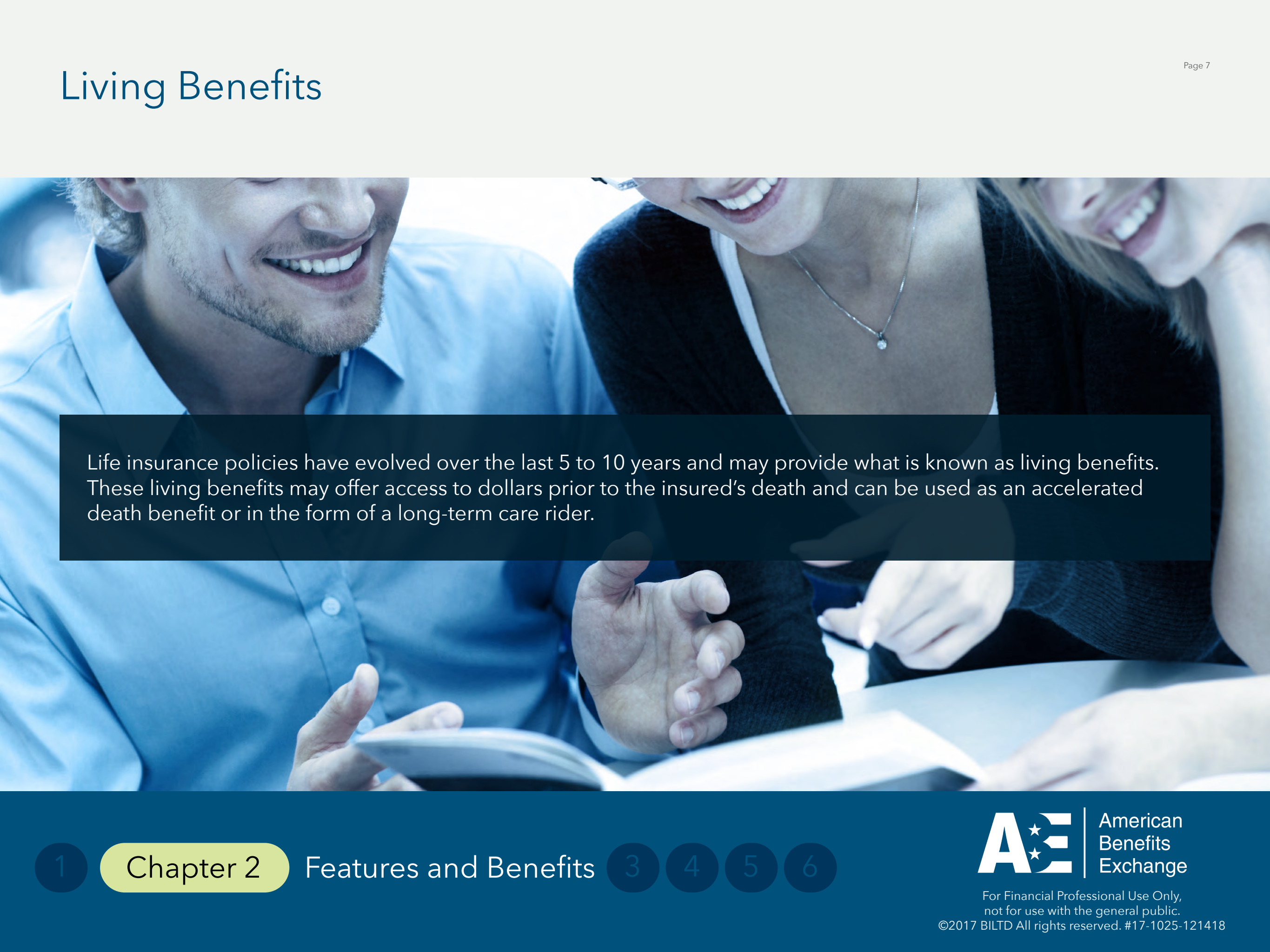
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Tax Advantages

There are three potentially impactful tax advantages to utilizing IUL insurance:

1. Tax-Free Death Benefit: Beneficiaries do not have to pay income taxes on the benefit.
2. Tax-Deferred Growth: Any accumulation within the policy will grow income tax deferred.
3. Income Tax-Free Distributions: Policy loans may be taken income-tax free and used for needs such as supplemental retirement income, college funding, medical or financial emergencies.

Living Benefits

A close-up photograph of a man and a woman smiling and looking at a document together. The man is on the left, wearing a light blue shirt, and the woman is on the right, wearing a dark top and a necklace. They are both looking down at a document held by the man.

Life insurance policies have evolved over the last 5 to 10 years and may provide what is known as living benefits. These living benefits may offer access to dollars prior to the insured's death and can be used as an accelerated death benefit or in the form of a long-term care rider.

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Living Benefits (cont.)

An Accelerated Benefit Rider (ABR), also known as a living benefit, allows your client to access death benefit proceeds prior to death to pay for health-related expenses such as terminal illness, nursing care, or a chronic illness. It can be paid out as a lump sum or in monthly payments and may be received free of federal income tax.

A few important facts to know about ABRs:

- With many insurance companies, clients do not pay for these riders unless they are exercised.
- The amount received by the policy owner is discounted because there was no upfront cost or underwriting done at the time the policy was issued.
- Living benefits, in combination with a long-term care plan, may be appropriate for some clients because a policyholder can obtain two forms of protection in just one policy.

Living Benefits (cont.)

Accelerated Benefit Riders (ABRs) - IRS Code Section 101(g):

These riders all use the indemnity model of benefit payment. However, the term “long-term care” may **not** be used in marketing these products. The physician must certify the chronic illness “is likely to last the rest of the insured’s life.”

The main differentiator among chronic illness riders is whether the rider is paid for by an additional charge added to the policy or is included as a policy feature with no underwriting. Instead of charging for the rider, the death benefit is discounted when the rider benefits are actually needed.

Long-Term Care (LTC) Riders - IRS Code Section 7702B:

Riders with the classification of 7702B offer more comprehensive coverage. That means a physician must certify that the insured, for a period of at least 90 days, is unable to perform at least two Activities of Daily Living (ADLs) or suffers from severe cognitive impairment. Keep in mind, LTC riders are available for an additional charge, generally require underwriting and will add to the policy premium cost.

Flexibility and Control

Flexibility and control are some of the benefits of IUL insurance policies. These policies have premium flexibility so the limitations or eligibility requirements are not the same as with a qualified plan (such as a Roth IRA). Individuals also have the ability to adjust premium payments, so they can increase, decrease or even stop payments based on their personal situations.

For example:

- If your client loses his/her job, the cash value in the policy can cover the cost of insurance and fees.
- Or, if your client receives a bonus at work, he/she can contribute additional money into the policy without penalties.

Your clients will also have some flexibility and control with distributions as there are limited restrictions within IUL insurance. They will have the ability to withdraw funds prior to age 59 ½ without an IRS penalty of 10% **AND** there are no Required Minimum Distributions (RMD) at age 70 ½.

Funding Options

There are several options when it comes to funding a policy. Clients may make **periodic payments** as well as **single premium payments**. Guidelines are set for both maximum and minimum premium amounts required (such as to keep the policy from lapsing). If your client is choosing a single premium option, there are rules and guidelines your client needs to understand. The following pages will define a **Modified Endowment Contract (MEC)** and a **Premium Deposit Fund (PDF)**.

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Modified Endowment Contract (MEC)

A MEC policy is when the premium payment is over the maximum amount allowed by the IRS. If a policy becomes a MEC, it will always be a MEC and the loans/withdrawals become taxed like ordinary income. Therefore, a MEC may not be a good choice for those that are planning to take loans/withdrawals to supplement income, fund a college education, etc. But, if loans/withdrawals will not be needed, a MEC policy may be positive because the death benefit is still passed on income tax free.

Consider the pro and con below regarding a MEC status:

PRO: Death benefit passes tax free

CON: Tax implications on any distributions

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Premium Deposit Fund (PDF)

A PDF may be a great way to fund an IUL insurance product with a lump sum and possibly avoid creating a MEC status.

Here is how a PDF works:

- The lump-sum payment goes into a holding account and then funds the life insurance policy over a period of time, typically 5 to 10 years.
- The dollars in the holding account are used to pay the policy premiums and earn a nominal interest rate.

Benefits of using a PDF include:

- Simplicity. You and your client determine how much to deposit and the number of years to fund the life insurance policy.
- It's automatic. The annual planned premium is automatically transferred from the PDF account into the life insurance policy, giving your client a disciplined premium payment approach.
- It avoids a MEC status, which may provide the client more flexibility from an income perspective.
- There is a premium discount. In other words, since the funds in the PDF earn a nominal interest rate, the premiums that are utilized to pay for the life insurance policy will be more than the single premium amount.
- The client has committed. The premium is paid in full and he/she does not have the flexibility to spend the money over time on other things or use the dollars elsewhere.

Policy Loans

One of the more popular features of an IUL insurance policy is the ability to take policy loans on a tax-free basis. In most cases, companies provide two different loan options, a fixed option and an indexed loan.

With a fixed-interest loan, a fixed-interest rate is charged to the client on the outstanding balance. With an indexed loan, the loan rate is charged in advance on an annual basis. The amount that is borrowed continues to earn the credited indexed interest each year. This gives your client the opportunity to earn interest on dollars that they borrowed and help offset the cost of the loan.

Carriers and products have different loan guarantees. It's also important to know what these guarantees and/or maximum rates are so once the loan provision is exercised, you can feel comfortable that your client is getting what they expected.

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Expenses

Below is a list of some of the main charges and fees that impact IUL insurance policies.

- Premium load or charge: This will cover the insurance carrier's state premium taxes as well as the sales expense and state and local taxes.
- Administrative fee: Typically a monthly fee in the \$5 to \$10 range, however this amount will vary by carrier.
- Cost of insurance: A monthly charge goes towards paying for the death benefit. It is based on the carrier's mortality charts and varies by age, gender, underwriting class, policy year, and face amount.
- Expense charge: Covers costs associated with underwriting and is calculated per \$1,000 of the policy's death benefit.
- Surrender charge: A charge for surrendering your policy for a select number of years, which is usually 10 to 20 years.

CLIENT MYTH:

Life insurance is too expensive.

BUSTED!

According to the 2015 Insurance Barometer Study by Life Happens and LIMRA, 65% of people say that life insurance is too expensive. This perception isn't based on reality however! Nearly 80% of people overrate the cost of life insurance.*

*source: <https://kazsource.com/overestimating-cost-life-insurance/>

Index-Crediting Strategies

The index-crediting strategy chosen determines how the universal life policy will earn interest credits. There are many different types of crediting strategies and they have some similarities. The following five items will impact the interest-crediting strategy.

1. **The market index** utilized dictates what index is tracked to determine the interest rate credited.
2. **The participation rate** determines how much of the increase in the index's value is taken into consideration in calculating the interest credit. A 100% participation rate means that the insured will participate in 100% of the index return.
3. **The cap rate** is the maximum percentage of indexed interest that will be applied to the cash value. Cap rates may be reset on a periodic basis.
4. **Index time frame** is the length of time that the carrier will track the index. One of the most popular time frames is 1 year and is called a 1-Year Point-to-Point. Carriers may also offer longer or shorter time frames.
5. **Index segments** are when an insurance company pools their dollars to purchase either one or a combination of indexed strategies that were selected for a specific term.

CLIENT MYTH:

Indexed Universal Life insurance has only been around since 1997, so there is no way to know if it can meet my objectives.

BUSTED!

Showcasing crediting histories for each strategy can help tell the story. Read more in the next chapter.

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Most Common Index-Crediting Strategies

Below is a list of some of the most common index-crediting strategies. This is not an all-inclusive list.

1-Year Point-to-Point: The 1-Year Point-to-Point strategy typically utilizes the S&P 500 and is the most popular indexing strategy. The index credit rate for this option is based on the percentage change in the index over the course of a 1-year period.

Increased Participation: The increased participation strategy offers the opportunity to get more than a 100% participation rate. Some carriers may provide anywhere from a 150% to 200% participation rate. If the participation rate is 200%, they will double the index return.

Uncapped: As the name suggests, this strategy removes the caps, but uses another method to limit returns in the form of a spread. This spread is set for a period of time and then reset by the insurer, usually on an annual basis.

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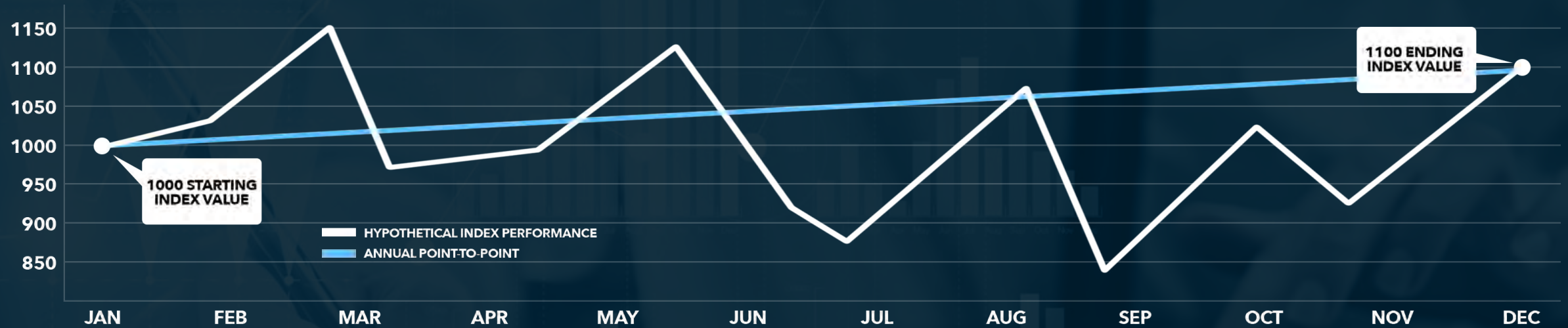
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1-Year Point-to-Point Hypothetical Example

Below is a hypothetical example utilizing the 1-Year Point-to-Point strategy with the S&P 500.



CONTRACT YEAR	ANNUAL INDEX CHANGE	CAPPED ANNUAL CHANGE
JANUARY 1ST TO DECEMBER 31ST	10%	10%

In this example, the client had a 10% annual change and his/her account would be credited the entire 10%.

This hypothetical example is intended to show the potential effects of index fluctuations on contract values. Not intended to predict or project future interest crediting.

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Who May Benefit from IUL Insurance?

The client profile for IUL insurance is very broad, from individuals looking for death benefit protection for their families, to more advanced estate and business planning cases. It is important to understand the objective of your client and then tailor the product to his/her specific needs - such as death benefit, cash accumulation, guarantees, living benefits, etc.

IUL insurance can be utilized for many purposes, including:

- Retirement planning
- College funding
- Wealth transfer
- Annuity & IRA optimization
- Legacy building
- Longevity planning
- Business continuation and preservation²
- Estate planning
- Diversification

²These concepts are reviewed in detail in *Attracting Small-Business Owners to Your Practice* eBook. Please contact us for a copy.



How to Identify an IUL Opportunity

There are a large variety of life scenarios that may trigger the potential need for IUL insurance, and having an understanding of those key situations is important. If your client makes any of the statements below, there may be an opportunity to present IUL insurance as an option.

Key indicators during fact finding:

- I have children or just had a new baby
- I just got married
- I am the sole provider for my family
- I am self-employed

CLIENT MYTH:

My employer provides adequate coverage in case I die.

BUSTED!

That may not be the case. 50% of US households would feel a financial impact within six months if the primary wage earner died³. In many cases, added coverage may be necessary.

³"2016 Insurance Barometer Study," LIMRA

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Additional Discussion Topics

When Discussing *Retirement*:

- I have maxed out my 401(k).
- I contribute above my employer match on my 401(k).
- I receive an annual bonus and am interested in diversifying my retirement.
- I am worried about taxes in retirement.
- I would like more control over my retirement income.
- All of my retirement assets are in qualified plans.
- I would like to retire prior to age 59 ½.
- I'm worried about long-term care expenses in retirement.

When Discussing *Wealth Transfer*:

- What should I do with my RMDs?
- I have a CD earning very little interest, and chances are I will not need the money so it will just be passed on to my heirs. What are the best options?

When Discussing *Any of the Following*:

- I would like a life policy that will build value but also be flexible (perhaps an employee bonus is guaranteed every year and there are no plans for its use).
- I need life insurance, but also need to plan for future college funding for my kids.
- I own a small business and am looking for other retirement options.
- I would like to get something out of my life insurance policy (what's in it for me?).

CLIENT MYTH:

I'm too young and don't need life insurance yet.

BUSTED!

This myth could not be further from the truth. No matter age, if your client has loved ones, debt, or assets to protect, life insurance should be a significant consideration. Policy rates may increase as age does, or as health concerns may arise, so now may be the best time for your client to purchase a policy.

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Ready to Get Started?

IUL insurance primarily focuses on a death benefit, but it can also be utilized in many different ways, such as a vehicle for cash accumulation, to supplement retirement, college tuition, life events, and even long-term care. Presenting it might open doors to an entirely different client base and possibly provide better suited opportunities for existing clients.

You must be prepared with the knowledge to level set your clients expectations and *bust some of the life insurance myths*. Doing so may help you better incorporate life insurance into your practice, better meet the needs of your clients and it may ultimately help you achieve your overall business goals.

There are many variables that need to be considered with structuring an IUL insurance policy, and we have the expertise to assist you.

Call us at 512.430.5511 to learn more or to discuss your next case.

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Ready to Get Started?



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