IUL & Related Terminology

IUL - What does it stand for?

Indexed

- The cash value in the account will grow LINKED (not invested in) an index, such as the S&P 500. When the market goes up, your cash value goes up. When the market tanks, the floor, discussed later, protects your cash value.

Universal

- FLEXIBLE. Not locked in stone. If we need to make any changes to the contributions, to the death benefit, in a month or a year, we can

Life

- Self explanatory. Life insurance. In real estate, if you have a mortgage, that's not a loan against your house, but a loan against your INCOME. With life insurance, the death benefit is going to be the collateral. So if someone takes out a loan and they get hit by the bus the next day, the loan will be subtracted from the DB.

Uninterrupted Compound Interest

Fancy marketing term. Sounds sexy. But if it wasn't for this, the IUL wouldn't be that great. This is similar to a cash-out refinance on a house. When you take a loan against your house, your house is still valued and growing off the entire amount

MEC - Modified Endowment Contract

Once a policy becomes a MEC, it cannot be undone. If you create a MEC, in normal people talk, you pretty much blew up your tax advantage status of a life insurance contract. Now, even when you take loans out, the gains will be reported as taxable income. And in some instances, you'll even have a penalty before the age of 60. Some people MAY want to MEC a policy because they just really like the benefits of the downside protection with upside potential.

When in an illustration, you will see a "MEC Premium." That is the most that a client can put in, in a given year, before turning their policy into a MEC. And they typically can't accidentally MEC it, they would have to sign off on a document saying they understand what they're doing to their policy.

The higher the Death Benefit, the higher the MEC. This isn't necessarily a good thing unless someone really wants to DUMP money into the policy the first couple years. If the MEC is way too high, that means their Death Benefit will most likely eat out of their cash value, and not be good for the policy

Minimum Death Benefit, Maximum Cash Value

This is ALWAYS how you want to structure a policy for MAXIMUM cash growth. Typically, when people want insurance, they say "Hey I want 1M in coverage, what's the CHEAPEST you can get it for me?" This is OPPOSITE. This is pretty much, this is saying "Hey IRS, I want to put in 1k/m, what's the LITTLEST amount of insurance I need for this to still be considered an insurance contract? Within this strategy, you can then use a Level Death Benefit, and Increasing Death Benefit, or an Increasing to Level Death Benefit, discussed more below

Higher DB = Lower Cash Value

Lower DB = Higher Cash Value

Level Death Benefit vs Increasing Death Benefit vs Increasing to Level DB

Level Death Benefit (Option A)

- This is still "Min DB Max CV" but will have a slightly higher Death Benefit out of the gate than an increasing. This will be good for people who:
    - Want to fund it for <10 years
    - Are 55+
    - Want to put in, say $500/m, but DUMP some extra money in from time to time. Since this will have more DB than an Increasing DB, the MEC will be higher, and allow you to throw in more money

Increasing DB (Option B)

- This is the conventional way to max fund an IUL. The death benefit will start WAY small, and increase every year. Each year, you're getting very close to MEC-ing the policy, but never actually happens. In this scenario, the cost of insurance is way lower out of the gate, so it would typically help you grow the money better. BUT, in most scenarios, the MEC is very low so you can't just dump extra money in w/o redesigning the policy.
- If a client starts putting in ~1-2k+, I will typically look at an increasing as my preferred option. Because when they start funding it this much, the MEC limit is typically a bit higher and they still have room to dump in more money.
- This CAN be dangerous if a client forgets to change their DB to Level. Why? Because then you're telling the DB to go up when it doesn't need to be. Thus, making our cost of insurance more expensive which will eat into your cash value.

Increasing to Level

- This is how my personal IUL is set up. When I stop funding it, I will change the strategy to a level strategy to do everything I can to prevent the death benefit from going up when it doesn't need to be

Crediting Strategies: Participation Rate, Floor, Cap

These are the three most important terms when it comes to "how does my money grow?" We all love the S&P 500, but withinside an IUL, it may not be the best option. Keep in mind, your money is never actually invested in the markets. These are solely how the insurance companies credit your account.

Participation Rate

- What percentage of the gains will I see? For example, if the crediting strategy we're working with went up 10%, and the PAR Rate was 120%, my cash value account would get credited 12%

Floor

- How LOW can my money go? Inside an IUL, the floor will typically be 0%. This is one of the best features of an IUL. That means when the markets tank, your account will not go belly up. BUT, there still will be some "loss" in the form of your cost of insurance. So let's say you have 100k in cash value, and the markets tank. If you're cost of insurance was 2k, you'd now have 98k in your cash value.
- In most cases, when companies have a higher floor, the Cap Rate will usually be lower. More guarantees = less growth

Cap

- How HIGH can my money go? Here's where sometimes the S&P 500 indexing strategies don't make sense. The S&P can be a great strategy when it comes to investing, but lots of times inside an IUL, the CAP Rate will be ~9-10%. So if the S&P 500 went up 30%, your account would only get credited that 9-10%.
- National Life Group, by default, links the indexing strategy to the US Pacesetter. This strategy does NOT have a cap.

Accumulated Value
This is like the VALUE of your house. Even when you take out loans, the accumulated value still grows off the entire amount.

Surrender Value
This is like the EQUITY in your house. How much of the value do we have access to? THIS IS YOUR ACCESSIBLE CASH. When you take out a loan, your surrender value will decrease.

Net Death Benefit
This is the Death Benefit, minus any outstanding loans. If you illustrate someone taking out a loan, here's where you will notice the death benefit decreases. That's because the death benefit is the collateral.

Loans vs Withdraws
There are 2 ways to take out money from an insurance contract: 1) Loan, or 2) Withdraw

1) I ALWAYS recommend loans as a a loan is tax free
2) When you take out a withdraw, you're 100% taking money OUT of your contract. A portion of this would be considered taxable income

Loan Types
There are three basic loan strategies. First, it's important to know the term "Participating." Participating means when you take, let's say 100k, out of your account via a loan, that same 100k is sitting in your Accumulated Value accruing interest like it never left.
Most companies, the loan is linked up to Moody's. As of 03/09/2023, it is 4.6%
<u>Participating Variable Loan</u>

- When you take out 100k, that 100k is still growing inside the account. Variable, just like a variable mortgage loan, means that the loan may fluctuate dependent on market conditions

<u>Participating Fixed Loan</u>

- When you take out that 100k, that 100k is still growing inside the account. Fixed, just like a fixed 30 year mortgage, means the rate is locked in. This will typically be a few points higher than the Variable Loan

<u>Standard Loan (Wash Loan)</u>

- A Standard Loan, also known as a wash loan, works a little bit different than a participating loan. Let's say you take out 100k via a loan. And that loan interest is 5%. What they will do is credit you almost 5% back to your cash value. So it gets very close to zero-ing out. As in it didn't cost you to take out the loan.

A Participating Loan would typically be better when the index is outperforming the loan rate. That's because you're money is growing at say 10%, and the loan was at 5%. A Standard Loan could be better for the policy when the market is tanking. That's because if you're money wasn't growing, this strategy would credit you back the interest on your loan. So instead of the loan “costing” you 5%, you simply got credited just about all of that back to your account

Net Amount At Risk
Insurance companies WANT to grow your money. Why? Because the higher your cash value is, the less the insurance company needs to pay out. The NAR (Net Amount at Risk), is the difference between your death benefit and the cash value. This is how an IUL can actually get a bunch cheaper as the insured ages.

Annual Renewable Term
An IUL is built on an Annual Renewable Term. The “cost of insurance” for the policy will be super low at the beginning, and increase each year. This will also be based on the NAR.

Lifetime Income Benefit Rider
This rider guarantees a tax-free income stream for the rest of the client’s lifetime. A client can turn this on at the age of 60, and at least have the policy for 10 years. They can toggle this feature on and off. If they take out a bunch of money, the LIBR would obviously then be less when they turn it back on.

Balance Sheet Benefit Rider
This gets rid of the difference between the Accumulated Value and the Surrender Value in the first 10 years. This does come at a nominal cost, but the AV and the SV will 100% be the same from the onset of the policy.
This rider would be good for HNW (High net worth) clients who want to dump money into the policy and take out money quickly. I typically do not recommend the “dump money in and take it out immediately strategy.”
Your commissions will be paid out over ~6 years

Overloan Protection Rider
If you took out a SHIT ton of a loan from your policy and you’re not paying any of it back and the markets are tanking (kinda a doomsday scenario), you’re policy would be at jeopardy of lapsing and creating a taxable event. This rider PREVENTS that from happening. If this is about to happen, they would consider your policy “paid up.” Meaning you’d have no cash value left, and there would be a small death benefit remaining.
As of 03/09/2023, this comes attached to NLG policies.

Tax Codes
Here are some tax codes that you should know, and to help you sound smart to the clients
- **101(A) -** Your Death Benefit transfers tax free to your beneficiary
- **72E -** Your money grows tax free within an life insurance contract
- **7702** - Money is accessible tax free because of the policy loan provision

Inflation
It’s a thing. It steals your wealth. Every year you keep money in a bank, we’re losing money. A dollar today is worth more than a dollar tomorrow. So people better be preparing. I like to use an inflation calculator from smartasset to figure out how much you’ll need at retirement to live your

same 100k lifestyle today. I put in the average inflation at 3%. https://smartasset.com/investing/inflation-calculator

Tax-Deferred vs Tax Free

Tax deferred accounts are like a 401k, or TSP. We haven't paid taxes on it YET, so we will have to pay taxes on it when we take it out. I love 401ks when they come with a match. It's FREE money. BUT, if someone is putting above the match, I'd ask them "why"? Because they're most likely just delaying lower taxes today for higher ones tomorrow

Tax free accounts are like Roth IRAs or IULs. Not necessarily "tax free." BUT, you pay your dues today so you don't have to pay them in retirement. After you read The Power of Zero, you'll understand how important these accounts are. If people are making too much "taxable" income in retirement, up to 85% of their social security will also be taxed. Great system, right? lol

Simple Interest vs Compound Interest

Simple Interest

This is the type of interest you get at a bank. They give you interest ONLY based on your principal. NOT your principle + Interest

Compound Interest

Your interest is gaining interest. This is the whole tale of: "Would you rather have 1M today or a penny doubled for 30 days?"

- Most people say 1M today. WRONG. A penny doubled after 15 days would be $164, and after another 15 days, $5.4M

Roth IRA

Advantages

- Tax Free distributions on all your money after 59.5
- Can still withdraw your contributions before 59.5 without penalty
- Market exposure

Disadvantages

- Have to wait until 59.5 to use most of your money
- 10% penalty if you take your money out before 59.5
- Low income limitations. If you start making over ~120k/year, you're phased out of putting money into a Roth IRA. After ~150k, you can no longer contribute to a Roth
- Market exposure

401K

Advantages

- Delay taxes until "tomorrow"
- Market exposure
- Typically get an employer match, let's say if you put in 3% of your monthly income, they'll also put in 3%. FREE MONEY. This is fantastic
- Higher limit than a Roth IRA, typically ~23k/year

Disadvantages

- Delay taxes until tomorrow. If taxes skyrocket in our future….. Uh oh.
- People think they have all this money in the account… they don't. A good chunk belongs to the government
- Can't access most of the money until 59.5 without a 10% penalty

- Market exposure
- LImit on contributions

Roth 401
I love these plans. Very similar to a 401k, but these are with AFTER tax dollars.

IUL
<u>Advantages</u>
- Tax free growth on the money
- Very loose income restrictions. Can THROW money into this
- GUARANTEED tax free retirement options
- Death Benefit
- Living Benefits
- Market Upside with little downside exposure

<u>Disadvantages</u>
- FEE heavy in the first 10 years
- Death Benefit (buy term invest the risk people would fall into this category)
- Not true market exposure

Paid up Addition (PUA)
If someone ever talks about this, this has to do with funding a whole life policy. We'll leave that, at that

Cash out refinance
Refinance = any change to a mortgage structure, whether that's increasing / decreasing the years you're paying into it, or changing your interest rate. CASH OUT means you're pulling money out of your house, you're using your EQUITY. And even though you're using your equity, your house is still appreciating off the whole amount. Very similar to taking loans out on an IUL

BRRR Strategy in Real Estate
BUY - REHAB - RENT - REFINANCE
This is a strategy that many real estate investors use to build MASSIVE wealth and pretty much keep using the same money. Example:
BUY a distressed property for 100k.
REHAB the property to improve the value to 200k .Let's say between the buy and rehab, you're all in at 50k
RENT to tenants to pay your loan
REFINANCE and pull out your same 50k that you put in

Now, you got a "free" house and can go employ that same 50k in another property. Rinse and Repeat

4% Rule (for investing examples)
"But hey, I could just have a lot more in my Roth IRA or Investment Account than the IUL!"
Yes, you could. But are you familiar with the 4% rule? This let's you know how much, at a high level, you could take out in retirement each year and not have to worry about running out of money.

This is a little strategy I use for when folks say something stupid like that. Retirement isn't all about "how much" can I accumulate, but "how much" can I use and never how to worry about outliving?

Play around with investment calculators, such as this one, https://smartasset.com/investing/inflation-calculator. Yes, an investment SHOULD "return" more money. But in regards to accessing money… not too different