

# Ten for ten: 10 lessons learned from Indexed Universal Life's first 10 years

By R. Marshall Jones  
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**1. Alert: Indexed Universal Life (IUL) Insurance can boost bond returns safely.** Ten years of experience with IUL has confirmed that good IUL policies are an excellent addition to a life insurance portfolio. They are more flexible than fixed premium whole life, can provide higher returns than Universal Life and be less risky than Variable Life stock market investments.

IUL combines a guaranteed "no loss" investment floor with the ability to purchase options on stock market indexes. The most popular uses the 1-Year S&P 500 Index without dividends.

You choose the allocations.

With the 1-Year S&P 500 Indexed Option, you receive 100 percent of the market upside (with a cap based on the cost of the options). If the Index is negative, the options simply expire. Meanwhile, you have a Guaranteed "no-loss" Floor provided by the cash values that remain invested in the insurance company's General Account.

**2. Be wary of overly optimistic investment assumptions.** "The illustration is NOT the contract!" Illustrations that over-promise may under-perform. Stress test your design; use conservative assumptions. Actual results are NEVER linear. An illustrated rate of 7 percent every year is the equivalent of assuming the stock market





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with dividends will earn 10 percent every year.

**3. Watch for gimmick Indexed Options.** It's hard to beat the S&P. When in doubt, keep it simple. Recent regulations, intended to reduce the use of unrealistic assumptions, require sales illustrations to use a rate that is no higher than a Benchmark rate based on the 1-Year S&P 500 Index without dividends.

**4. The Best Carriers Treat In-Force Policyholders like they own the company.** Be on the lookout for "bait and switch" possibilities. How will you be treated after you become a client?

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Look for carriers who fully hedge your option risk, pass through 100 percent of your option gains, maintain the highest cap rates that can be supported, and don't change the deal after you become a client.

**5. Look for Carriers that don't charge more for IUL than for Universal Life.** Basis points matter, especially when they compound in a tax-deferred cash value account. Some carriers use the allure of IUL to build in extra charges that reduce overall policy performance. With the best carriers, your indexing costs are funded solely with your policy's options budget.

**6. For Best Performance, Think Very Long Term. This is a lifetime investment.** Plan as if the insured will live well beyond age 100. Use a policy design that will last more than 20 years regardless of investment results. Allocate your Indexed Accounts so that 1/12th of your cash value segments mature each month. Good design allows you to select a planning rate that will equal or exceed your target cash values as you approach life expectancy.

**7. Have Overloan Protection if you**

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intend to use Policy Loan Arbitrage. Positive arbitrage can turn negative. If needed, a properly managed policy can provide significant arbitrage that leverages the tax benefits of life insurance. New regulations will restrict illustrations to showing no more than a 1 percent difference between the illustrated cash value growth rate and the assumed loan cost. IUL cash values can be distributed without income tax during life with tax-free distributions up to cost basis followed by non-taxable policy loans that accrue interest. An Overloan Protection Rider can keep the policy from lapsing with zero net cash value and a huge "phantom" income tax on the "forgiven" loan balance.

**8. Consider diversification by policy type and carrier.** One size doesn't fit all and circumstances change. The Indexed option may be the primary product design driver or it may be an available option with another product type. Some clients want the added security of no-lapse guarantees combined with IUL. Other clients

want the added flexibility of multiple investment options. Or the ability to take advantage of rising interest rates when they occur. IUL alone will not always be the most suitable product chassis. Large life insurance portfolios may perform better with diversification to mitigate risk.

**9. Policy Plan Management is CRITICAL.** It could be the difference between success and failure. Do you still receive reports and in-force policy updates from the people who sold you your policies? Most life insurance policies today are not managed by the same people who sold them. In effect, they have become "orphaned" for policy service. Only 1 in 5 new agents is even in the business after 5 years. Work with your advisors to establish an effective policy management plan.

**10. Good Life Insurance serves as a non-correlated investment for your portfolio.** Include your life insurance policies when reviewing your other investments. Efficient life insurance policies provide investment returns at and beyond life expectancy that equal or exceed expected returns for the underlying investment.