Filling the retirement portfolio gap with Indexed Universal Life

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Life insurance is often bought and sold based on the size of a death benefit. That is, after all, the long-established value proposition of a life insurance policy: it is an asset that provides financial protection in the event of death. However, in recent years, product development efforts have focused on making life insurance policies valuable during one's lifetime, in addition to providing death benefit protection.

One of the compelling "living benefits" of a properly designed **Indexed Universal Life (IUL)** insurance policy is supplemental retirement income. Today, with retirement confidence levels continuing to slip, and projections that the Social Security retirement and disability trust funds will become depleted by 2031, clients need options to complement workplace retirement savings plans and close gaps in their retirement portfolio. While investments such as stocks, bonds, and mutual funds may be the typical retirement portfolio selections, the tax-advantaged growth potential and tax-efficient cash distributions of Indexed Universal Life (IUL) insurance are desirable and rich portfolio ingredients.

In addition to a tax-free death benefit, single-life and survivorship IUL policies offer cash value growth potential through crediting options that credit interest based on the performance of a market index, such as the S&P 500, but without the risk associated with investing in the actual index. When a knowledgeable agent familiar with structuring a non-modified endowment contract designs the IUL policy, the cash accumulation and distributions are tax-free, similar to a Roth retirement account. An IUL policy's account value is able to grow tax-free, and cash value accessed from the policy in the form of loans or withdrawals is not taxed because it is not considered income under current law. This results in greater net cash flow without impacting the policyholder's tax status.

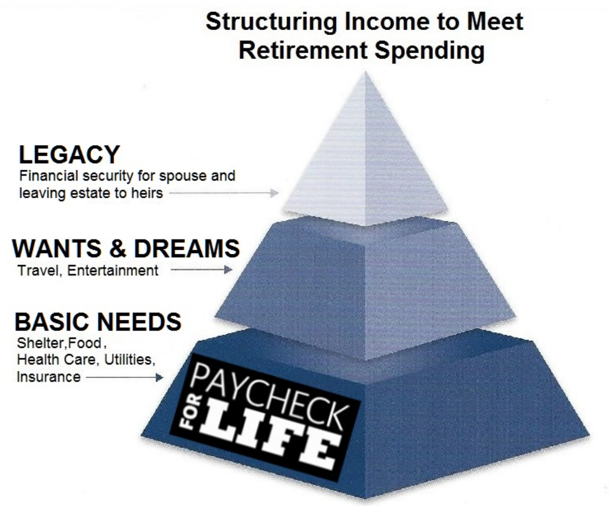
This is significant as taxes are often an overlooked aspect of retirement planning.
The "non-income" categorization of the distributions also means there is no effect on how much clients receive in Social Security benefits, pay in capital gains or Medicare premiums, all of which are impacted by Adjusted Gross Income or Modified Adjusted Gross Income, and commonly impacted by other classes of retirement assets.

Putting the advantages to work
When considering post-retirement expenses, generally speaking there are four categories (see chart): 'Needs,' 'Wants,' 'Dreams' and 'Legacy.' Often, the distribution phase of retirement is structured where:

● traditional assets such as a 401K or social security fund the 'needs' and some of the 'wants';

● annuities, dividends, and interest are used for the 'wants' and 'dreams'; and

● the 'legacy' is usually a conversion of unused assets.



This traditional planning model, however, can be supplemented using the tax advantaged living benefits of IUL policies for greater purchasing power for some of the 'needs', 'wants', and 'dreams', along with the death benefit to fund the 'legacy'.

Using an IUL policy for retirement planning can also give clients greater flexibility in choosing when to retire. For example, clients retiring at age 65 with a plan of depleting assets to life expectancy can use the IUL cash value as a source of backup income should they live past life expectancy, while knowing they can transfer a tax-free death benefit to heirs if not.

Conversely, individuals who choose to retire early can use an IUL policy to provide a cash stream for the years until they can access money in a 401(k) or other retirement account without early withdrawal fees. Likewise, clients retiring early can access their IUL account value in the years before taking Social Security so as not to reduce the benefit for which they are eligible through the program.

Whether retirement is 5 years away or 30, it is essential that clients have a comprehensive plan that takes into account the expected, and perhaps more importantly, the unexpected. Everyone has notions of what the future might hold, but as life moves forward, circumstances change and goals change.

That is perhaps where IUL living benefits yield their greatest value. As a complement to traditional retirement assets, these benefits provide increased flexibility and control, and allow traditional assets to be used more efficiently, with the added benefit of knowing that a legacy is in place through the policy's death benefit.

While most clients will have one or more of the traditional types of retirement assets — taxable investments, tax-deferred contribution, or tax-advantaged investments that generate tax-free income like Roth IRAs — the living benefits of IUL policies may provide a supplemental cash source that can help clients enjoy retirement as intended without the worries of impacting modified adjusted gross income, tax brackets, capital gains or access to government programs.

1. SSA, 2014 Annual Social Security and Medicare Trust Fund Reports.
2. Loans and withdrawals will reduce the policy's account value and death benefit, may affect guarantees, may cause the policy to lapse, and may have tax consequences.
3. Withdrawals and surrenders are tax-free up to the cost basis, provided the policy is not a modified endowment contract (MEC). A MEC policy is one in which the life insurance limits exceed certain high levels of premium, or the cumulative premium payments exceed certain amounts specified under the Internal Revenue Code. For policies that are MECs, distributions during the life of the insured, including loans, are first treated as taxable to the extent of income in the contract; and an additional 10% federal income tax may apply for withdrawals made prior to age 59½.
4. "2013 – Expense Challenges of Age 62-75 Retirees ," June 2014.