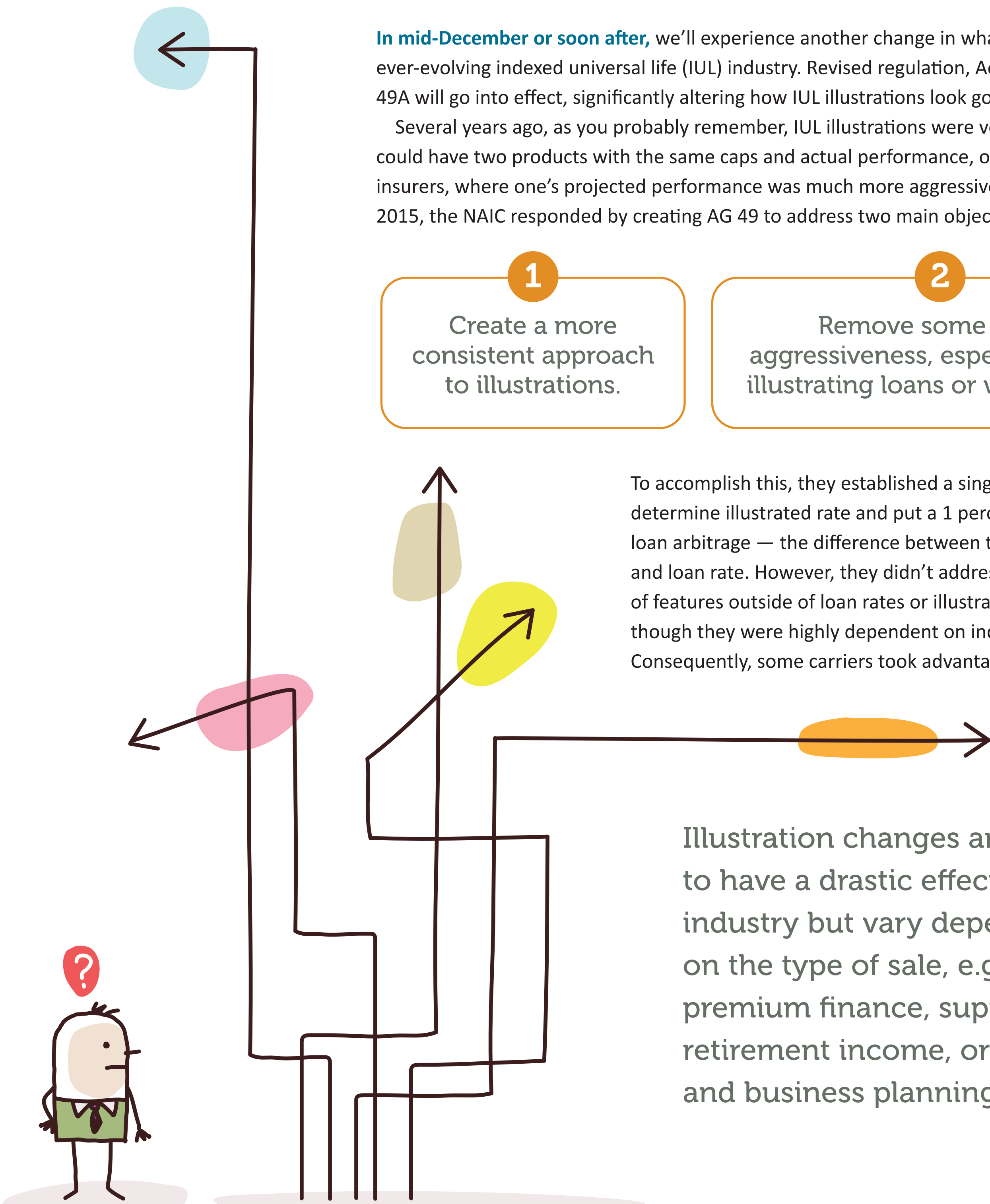
Indexed Universal Life after AG 49A

In mid-December or soon after, we'll experience another change in what seems to be an ever-evolving indexed universal life (IUL) industry. Revised regulation, Actuarial Guideline (AG) 49A will go into effect, significantly altering how IUL illustrations look going forward.

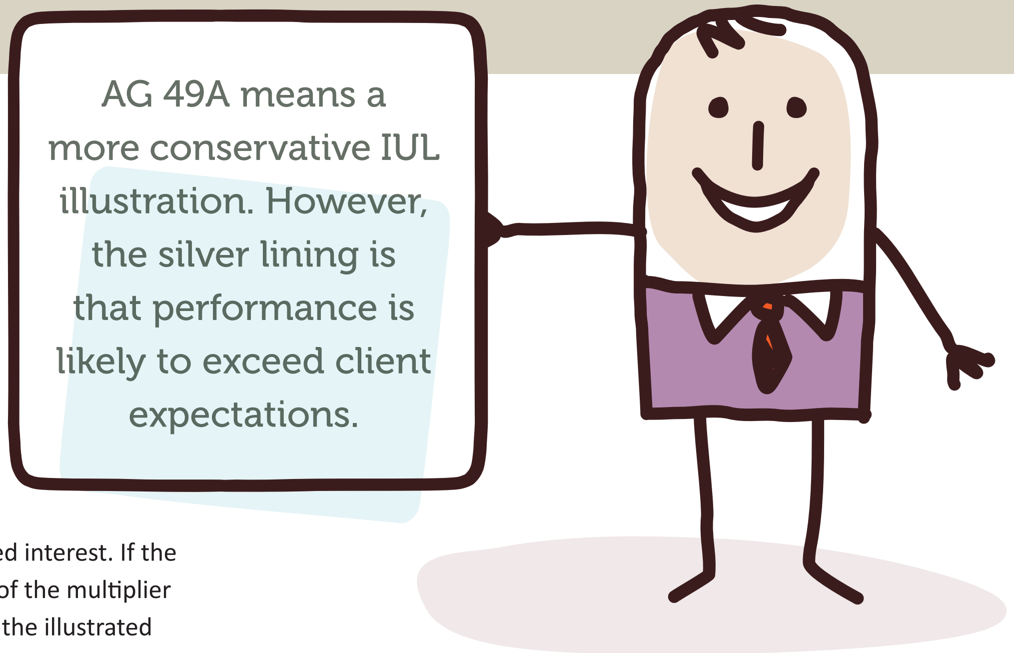
Several years ago, as you probably remember, IUL illustrations were very inconsistent — you could have two products with the same caps and actual performance, offered by different insurers, where one's projected performance was much more aggressive than the other. In 2015, the NAIC responded by creating AG 49 to address two main objectives:

1. Create a more consistent approach to illustrations.
2. Remove some of the aggressiveness, especially when illustrating loans or withdrawals.



To accomplish this, they established a single standard to determine illustrated rate and put a 1 percent cap on maximum loan arbitrage — the difference between the illustrated rate and loan rate. However, they didn't address benefit projections of features outside of loan rates or illustrated rates — even though they were highly dependent on index performance. Consequently, some carriers took advantage.

Illustration changes are likely to have a drastic effect on the industry but vary depending on the type of sale, e.g., premium finance, supplemental retirement income, or estate and business planning.



Carriers' response and the impact on products

In 2015, when AG 49 was enacted, carriers were facing five years of historic low interest rates with no end in sight. That downward cap pressure combined with new regulation drove many IUL carriers to develop bonuses and multipliers to illustrate more favorable long-term performance potential.

For example, a carrier could charge an additional 4 percent on the account value in exchange for a 200 percent multiplier on credited interest. If the illustrated rate was 6 percent, the combination of the multiplier minus the account value charge would increase the illustrated growth in the account value from 6 to 8 percent. It's important to understand that even if there's a year with a zero percent credited rate and no bonus is applied, the policy is still saddled with the 4 percent annual expense charge in addition to all traditional expense charges within an IUL.

While the features themselves aren't inherently good or bad, it made the illustrations look like they did pre-AG 49, attracting attention and sales for products that likely would underdeliver on the projections — for instance, if a zero was credited. As you can see, the performance is drastically affected.

The effects of 0% indexed interest every fourth year

Standard: Based on hypothetical illustration based on best-case market scenario[1]
0% 4th year: Based on hypothetical illustration based on typical market scenario[2]

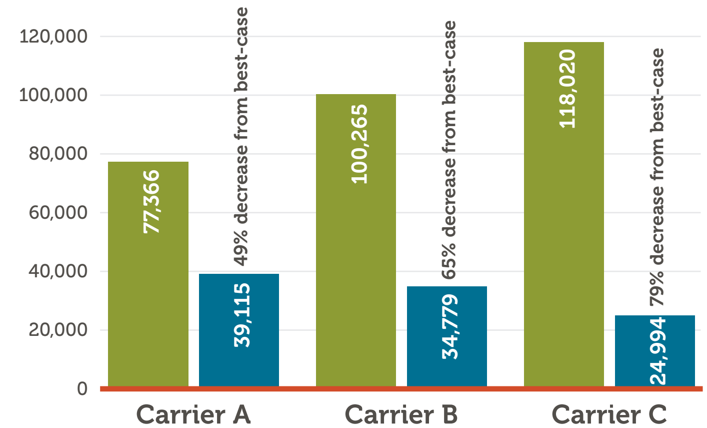


Illustration assumptions: Male, age 45 preferred non-tobacco, $25,000 premium ages 45–64 (20-years), max distributions ages 65–84 (20-years) using the illustration default variable income loan rate.

1 "Best case market scenario" uses AG 49 max illustrated rate every year
2 "Typical market scenario" uses AG 49 max illustrated rate with 0% every 4th year

The NAIC saw how this might lead to potential risk and confusion and updated AG 49 with additional guidelines intended to provide more protection to clients.

What's new

With these updates, dubbed AG 49A, the illustrated rate will be tied to carrier economics rather than cap rate, index, crediting strategy, or other features offered at any given time. Meaning, they will assess a carrier's ability to buy options to back a product and translate that to a cap rate. The backtesting of that cap dictates how much growth can be illustrated. Additionally, maximum arbitrage will drop from 1 percent to 50 basis points. This naturally leads to a more conservative illustration, increasing the importance of selling IUL off benefits rather than projected performance. To many, this could be a rude awakening.

What it means to the industry

Although carriers will no longer be able to use bonuses and multipliers to illustrate their product more favorably, it doesn't mean they won't be able to offer them. Whether they do, remains to be seen. Either way, client-conscious carriers will differentiate based on pricing and product development advantages.

Illustration changes are likely to have a drastic effect on the industry but vary depending on the type of sale, e.g., premium finance, supplemental retirement income, or estate and business planning. However, if an aggressive illustration is needed to sell IUL — you're likely speaking to the wrong client.

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Why IUL is even more valuable today

Between the economic environment, global pandemic and now AG 49A, 2020 has shook up the life insurance industry, but it hasn't diminished the value of IUL. In fact, it highlights four reasons why selling IUL is even more critical.

In short

AG 49A means a more conservative IUL illustration. However, the silver lining is that performance is likely to exceed client expectations. When you consider that and the inherent benefits of the product, it's still a great time to sell IUL.

1

Death benefit

Whether a client is concerned about their mortality because of COVID-19 or not, it's all around us, making it one of the easiest times in history to have a conversation about the importance of a death benefit that exceeds account value and protects family and business.

2

Tax benefits

Once money is put into a properly structured and managed permanent life insurance product like IUL, no additional taxes are due on that premium or growth. Most economic experts are predicting future tax increases and a life insurance product could help immunize a policyholder against that.

3

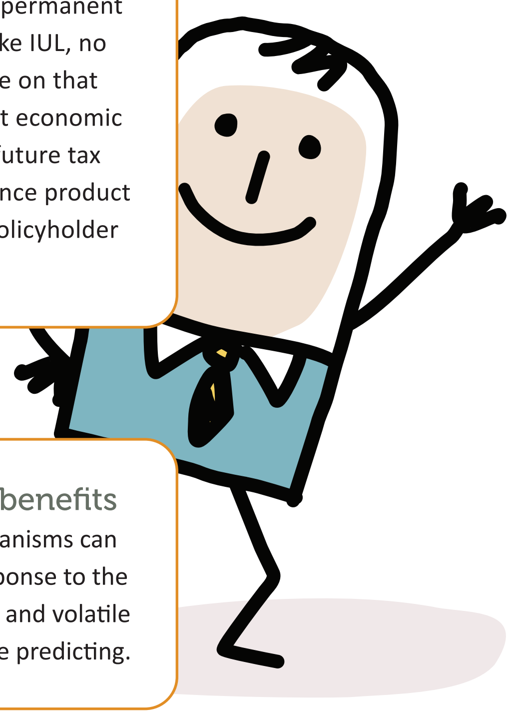
Living benefits

Permanent life insurance isn't only valuable once the insured dies. During their lifetime it can be used as a retirement income supplement, emergency fund, college funding, or to offset long-term care costs.

4

Indexed crediting benefits

The floor and reset mechanisms can be a viable solution in response to the extended low interest rate and volatile stock market that many are predicting.



Jason Konopik F.S.A., MAAA

Area President

Partners Advantage Insurance Services, a Gallagher Company

Jason Konopik has over 25 years of industry experience and has helped develop more than 10 products with industry-recognized life insurance carriers represented by Partners Advantage, an IMO providing agent development and recruiting support to producers and managing general agents.

Louis Slagle

Area Senior Vice President

Advantage Distribution Partners Advantage Insurance Services, a Gallagher Company

Louis has 15 years of industry experience in financial planning, wholesaling, advanced markets, product development and distribution management. Twelve of those years focused primarily on indexed universal life (IUL), where he was involved in building three of the industry's leading IUL products.