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VARIABLE LIFE SALES AND EDUCATION

OVERFUNDED VUL

THE GREED SALE

by Charles Arnold

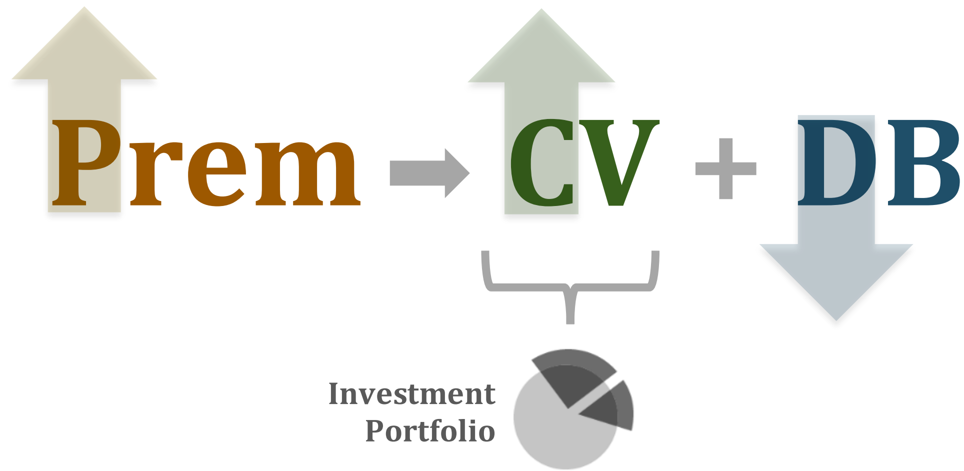
If you knew you were going to live to age 95, would you buy life insurance?

This fun, hypothetical question was asked over dinner during a life insurance conference I attended. It stemmed from a previous conversation about genetic testing and eventual uses in medical underwriting. Someday soon, it is likely that genetic testing will accurately estimate a client's life expectancy, so this question might not be so radical. The three gentlemen seated all quickly answered with their unique versions of "no." I sat there for a second and then I answered "definitely, because you can use it while you are alive."

This isn't a fear sale, like typical insurance. This is primarily a greed sale. Once that is understood, it becomes much more obvious. Mortality risk goes out the window with this assumption and it shifts to longevity risk. That means wealth accumulation is paramount. There is another side to life insurance other than death benefit, and it is called cash value.

Living to age 95 means you have boatloads of time. Without taking significant risk, time is required for wealth accumulation. Historically speaking, what long-term investment has delivered the greatest growth? Stocks. Where can you buy stocks that lets them grow tax-free and allows you access to that growth tax-free? A Roth IRA and variable universal life (VUL). Overfunded VUL for investment purposes deserves far more recognition than it gets:

> *The simple fact is that VUL is and will always be the most versatile and applicable product we sell. If you want proof of that, look no further than the trillions of dollars that retail investors put into financial products that are not general account life insurance contracts. The only product we have to offer to clients that looks like the other places they put their money is Variable UL. Simple as that. And on those merits, VUL should be a much larger market than it is today. That's why I'm bullish on VUL.*
>
> Bobby Samuelson, *The Case for VUL*
> The Life Product Review, December 18th, 2018



The above diagram is useful when explaining how overfunded VUL is designed. Usually for a life insurance sale, you start with the amount of coverage needed. The insurance professional then spreadsheets out the options ranked by premium amount respective to the client's underwriting class. The lowest cost option that provides the desired coverage is usually selected. This is entirely a death benefit driven sale.

For overfunded VUL, we flip this approach on its head. We start with a dollar amount that the client wishes to invest, which constitutes the total premium. We then run the options for a minimum non-MEC solve, which calculates the minimum insurance amount possible per premium dollar allowed by the IRS tax code. The desired investment portfolio is selected and allocated for the VUL illustrations. The products are then ranked by their 20-year cash value amount. The option that has the greatest accumulation at year 20 is usually selected; however, another option may be selected instead due to some rider, feature, or unique sub-account investment. Within the underlying investment portfolio, the client and advisor can select between 50 and 100 different sub-account options from the top investment managers in the world:

The overfunded VUL sale isn't about insurance at all, it is about the investments. This is very similar to how variable annuities are marketed and sold. For variable annuities, it is all about the power of tax-deferred growth. For overfunded VUL, it is almost the exact same premise, just with tax-free growth instead of tax-deferred. So, when speaking with a financial advisor, the insurance specialist needs to speak the investment language, relate to the financial advisor, and keep it simple. The word "insurance" shouldn't even come up until late in the conversation:

Wholesaler: Mr./Mrs. Advisor, what do your clients own in their Roth IRAs?

Advisor: Mutual funds. American Funds, Vanguard, and Dimensional Funds. But most my clients can't contribute to it anymore.

Wholesaler: We have those managers available. Think of a specific client with a Roth IRA. How much money would they contribute to their Roth if they could? Just a ballpark guess.

Advisor: Probably Mr. Johnson. I'd have to ask, but probably $20,000 a year at least. What are you getting at? Some Roth alternative?

Wholesaler: The same as the Roth IRA from a taxation standpoint, but without any contribution restrictions. And your clients can invest in the same great managers and funds they already own. Would you like to see an example? (Use: 5 Step Guide to Reading the Illustration and IRR)

Advisor: What is this, is this variable life? Life insurance is expensive.

Wholesaler: Cost is only relevant in the absence of value. For insurance, it largely depends on the client and the design. This solution is good for healthy, younger clients who have time to accumulate. Over the life of the client, it is not any more expensive than a variable annuity, and certainly brings more value on an after-tax basis. Think of it this way, your client must assume either the cost of tax (COT) or the cost of insurance (COI). In many cases, it makes sense to buy the insurance wrapper and eliminate taxation.

COT **vs.** **COI**

Cost of Tax **Cost of Insurance**

Advisor: Underwriting is a pain in the butt. I like transactional business.

Wholesaler: We can use accelerated underwriting that takes days, not weeks or months. This works for clients ages 25 to 60, in good health, and looking to invest $50,000 to $200,000 over the next several years. These programs have a short form application, or tele-app, where the carrier calls the client directly for an interview and takes them through the process, often times without any lab tests. We are also here to help them.

Advisor: I sold VUL in the late 1990s, you guys really screwed over my clients.

Wholesaler: Agents were illustrating VUL at 12% and drastically underfunding the cash value. Today, we know that is a recipe for disaster and we illustrate between 6% and 7%, which is more in-line with long-term market performance, and we use a resilient, overfunded design. The VULs sold today have a standard no-lapse guarantee for at least five to ten years as well, for some added protection. The client overfunds the VUL policy to its maximum allowed by the IRS tax code. We then levelize the death benefit at or around when the client stops paying premiums, which allows the cash value to grow more efficiently (called a death benefit option 2 to 1 switch).

Advisor: Why wouldn't I use indexed life, or IUL, for downside protection?

Wholesaler: We can look at IUL for some folks who prefer that protection. But for accumulation, nothing will come close to overfunded VUL as far as growth potential. A thought here would be to consider a VUL product with indexed sub-account options. That way the client isn't locked into one indexed strategy. They can allocate a portion or all of their funds into those strategies, along with the investments, as they see fit; either as their risk tolerance changes or they decide to start taking income. Some of these indexed sub-accounts also have participating loans associated with them, which is an added benefit.

> *See, the biggest challenge for VUL is Indexed UL. Our industry has decided to convince itself that Indexed UL is truly the better solution, that we have created an asset class that is a superior application for life insurance than traditional asset classes. That we, the life insurance industry, have cracked the code on a low risk, high return asset that apparently no one else can see or create. Doesn't that seem more than just a little bit preposterous? Not when there's so much money being made in believing that it's actually quite reasonable. And until we get straight on Indexed UL, attempting to grow VUL is going to be a hard bargain – despite the fact that it is actually the inherently superior product chassis.*
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> Bobby Samuelson, *The Case for VUL*
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Ideal Client and Product Profile:

Annual Income > $100,000
Health = Good to Excellent
Age 25 to 60
Years Paying VUL Premium >= 5 Years
Investment Horizon >= 20 Years
Total Investment / Premiums > $50,000

VUL Design: Minimum Non-MEC, Optimal 2-1 Switch
Underwriting: Accelerated Program, Lab-Free if Possible
Indexed Sub-Account Options Available w/ 50+ Investment Options
LTC / Chronic Illness Rider Availability

To conclude, overfunded VUL is a fantastic accumulation product that doesn't get any attention from either advisors or wholesale professionals. It is a story based on cash value and investment, and has less to do with how insurance is traditionally sold. The root issue is relating to distribution, much more so than to product. Today's wholesale insurance professionals represent at least 10 different carriers with 5 different products each, with a focus on death benefit, or fear driven sales. That would be over 50 different potential solutions on the low end; which would be overwhelming for any sales person.

It will take a conscious choice by a distribution firm to focus on the story of overfunded VUL. They will need to have buy-in and support from top executives at a specific VUL carrier to promote the story, together with fund management companies to drive the investment-oriented sale. The fund management companies will need to be convinced of the sticky, asset gathering potential of VUL, just as they have bought into variable annuities for instance. Joint marketing pieces will need to be developed from the fund management company and the insurance carrier to highlight and provide optional investment portfolios. If indexed accounts are available, those would also be highlighted. Preferably a carrier with an accelerated underwriting program that can offer a more transactional experience. I believe that only when these parameters are met, will overfunded VUL find mass-market appeal.