Tax-Free Income & Wealth Through Indexed Universal Life Insurance

I have found that the reason people often miss the very best in life is that they hold misconceptions and falsehoods closely as truth. It may be because of a parent or teacher, a book or television show, but somewhere along the line people create a series of truths that become inviolable, but in fact, are completely false.

It is my belief that the single best place to 'save' retirement dollars is in a permanent life insurance contract.

You may find the voice of some previous financial advisor or book or talk show host whispering in your ear, that can't be true. Why do I know this? For two reasons. First, I had that type of reaction myself; and secondly, so do many of the people I visit with.

When I ask them why they believe what they do, they often cannot produce an answer. That is because they're not really sure why they believe what they do. Until we visit, they have never looked into the truth or figured it out for themselves. They simply heard a statement somewhere along the line that they have thought to be true for years.

They think life insurance is about dying. With all of the jazzed up financial products on the market, how in the world can life insurance be the best place for the long-term savings and wealth accumulation?

Once you understand how permanent life insurance really works, you will understand why I think this way. Life insurance should be used as a strategy, not as a product. The best insurance policy and the least costly (long term), is one that is in force at death. Permanent policies will always be in force at death when used as a strategy.

Now you can understand why I hold a strong bias towards permanent insurance. However, I provide both permanent and term insurance to my clients, because the one feature that both term and permanent similarly provide is a death benefit. One of he most important issues in the life insurance discussion is the proper amount of coverage. If the amount of insurance that is wanted (not needed) can only be afforded through term insurance, then term it is.

Most people don't get excited figuring out the proper amount of death benefit. Many people see life insurance as a necessary evil. Many don't even see it as that. They avoid it all together.

However, if a person is looking for the best place to save and create wealth, a properly structured permanent life insurance policy can serve as one of the most powerful retirement strategies available anywhere.

There are many different kinds of permanent life insurance available in the marketplace; but the type of product that I believe best allows you to generate <u>the most tax-free income</u> is

called Universal Life insurance. It has been around since the early 1980's when it first entered the market. In particular I like Indexed Universal Life (IUL). The main deterrent to cash accumulation over time is the affect of negative calculations during any period, with a period being annually. The IUL has a crediting method that can never go negative in any year. This is a huge benefit when calculating what kind of return you will get over time. With negative returns in a year your actual return can never be close to your average rate of return.

The Indexed Universal Life policy is market driven off of some index for its growth. We only recommend ones that have zero floors, so they can't lose any money. As an example; if you have a $1,000 and you lose 50% the first year and gain 50% the second year you have an average rate of return of 0%. But you have actually lost $250 (25%). $1,000 losing 50% = $500. $500 gaining 50% = $750. So when you see mutual funds (or any other vehicle) claiming that their 5 or 10 year returns are an average of 'X%', it doesn't mean that you will actually have earned that much. Over the last 25 years the S & P 500 point-to-point index, with a maximum growth of 13% and without losses, has averaged 7.89% (an historical chart is available upon your request), and this is exactly what you would have received as a return in these type policies, because you had no losses during that time.

Here is a more realistic example. The 10-year period from 2000 to 2009, what the Wall Street Journal calls '*The Lost Decade*', had a negative 1% average rate of return using the S & P 500 point-to-point index (actual was closer to -2.7%). Without losses in, 2000, 2001, 2002 & 2008, the S & P 500 point-to-point index achieved a return of +5.45%, and that was with a 13% cap in all of those years. Obviously the eliminating of negative returns has a big impact on your moneys growth.

The policy should be from a quality 'A' rated insurance company and needs to be 'properly funded'. What do I mean by 'properly funded?' Traditionally, most agents and companies have calculated the *minimum* premium needed to fund a certain amount of death benefit. This is the manner in which most insurance policies have been sold to the public – the *most* life insurance for *least* amount of money. We believe you should use these policies primarily for cash value build up. You should fund them to maximize cash value (to create tax-free income). This assures that your premium amount buys the least amount of death benefit it can, and enables the maximum amount of the premium to be credited to 'your cash value'.

These policies should be funded to the maximum that the government will allow. Yes, the government has some say in this. You know if the government (IRS) is interested in limiting how much you can put into a policy, it must be a good tax haven. Back in the mid 1980's the government decided that these vehicles were too good at avoiding taxes and drew a line in the sand that said if you contribute over a certain amount, based on the death benefit, the cash value would be treated like an qualified account (IRA) and be taxed and penalized upon withdrawal. We certainly don't want that, so we make sure that the funding stays below the MEC (Modified Endowment Contract) line. This allows you to maximize your cash value accumulation. (*We can provide you with a 10-minute video that explains this in more detail – just ask us for a copy to watch)*

Life insurance companies have set up provision within their policy features that allow the client to take a loan against their cash value. Not *from* their cash value but *against* (as collateral) their cash value. Your initial reaction might be, 'that doesn't sound good during my retirement years. I don't want to be taking loans.' But what if I told you that this loan charged you little interest, and that it *never* needed to be paid back during your lifetime? Does that change the picture? You bet it does. Let's explore how this works.

A key component of these policies - that being the withdrawal phase (tax-free income), is just as important, if not more so, than the accumulation phase. Since withdrawing as much money out tax-free for life is the main objective, you want a policy that handles back end loans as efficiently as possible. The policy must offer a participating loan with a guaranteed fixed loan rate for the life of the policy, not a wash loan with a variable loan interest rate. Participating means that the loan amount is still participating in the cash value growth. Policies that use the wash loan concept (loans are not participating in growing cash value) will provide much lower tax-free income withdrawals. One more benefit is the positive arbitrage when the crediting percentage is greater than the loan interest. If you receive 13% return in any year (current cap), and the fixed interest rate is 5.3%, then there is a positive 7.7% arbitrage, which allows the policy owner to borrow more money each year. *(An illustration can be provided for your particular situation)*

Does the government tax loans? No. When you borrow money for anything it is not taxed. It shows up nowhere on your tax return. The same is true when a loan is taken from a life insurance company.

The last component you need to understand is how the life insurance death benefit is taxed, because it is the death benefit that makes this whole strategy work. Without the death benefit, this strategy would not be available. At death, all the proceeds of a life insurance contract are paid to the beneficiary completely income tax-free.

Tax-free dollars while you're living and tax-fee dollars distributed to whomever you choose upon your death. Anyone who says that life insurance cost too much, just doesn't understand how to structure it and use it as a strategy. Wouldn't you agree?

You might be asking yourself two questions about now. One, what's the catch? Two, if it is so good why isn't everyone doing this? Two great questions, but I can tell you this; there really is no catch. There is one caution. As long as you understand that you are buying life insurance – it is not like other savings plans, there is no catch. Most people need life insurance anyway so purchasing it in this format is a great way to get the life insurance they want (need) and tax benefits they didn't know existed.

Why isn't everyone saving this way? The primary reason is that most people don't know about it, or how to structure it. Did you? I didn't know about it until I studied about it. My insurance person never explained it to me. It has been far too long that this great benefit has been hidden from mainstream America.

Most people are more concerned about having a retirement account versus having adequate life insurance. The tragedy is that few Americans realize that permanent life insurance can be a protection plan, a savings plan, and a viable methodology to provide additional retirement income. Retirement plans such as 401(k)s and IRAs have never been able to perform multiple economic jobs simultaneously like life insurance.

This strategy is not for everybody. Though it is open to everybody who can qualify for life insurance, it is best suited for a couple of target groups: those currently contributing near the maximum to a tax-qualified plan such as a 401(k), SEP, SIMPLE, IRA, etc., those who earn a relatively large income, or those who want to reposition taxable assets into a non-taxable vehicle and let them remain in a tax-free environment. People who want a 'permission slip' to spend down their other assets and still leave a legacy.

Since it is the tax-free income and tax-free death benefit that makes this strategy work, it is ***imperative*** that the policy stays in force until the insured's death. I know is sounds pretty basic, but it is too important to gloss over. If the policy lapses or cancels then all that money you have taken out as a tax-free loan now suddenly becomes taxable; and that is one tax bill you *never* want to see.

How to make sure? First, don't take out too much money. When you see an illustration, make sure that they run the income out to at least age 100, not 90 or 95. Second, make sure that it is run conservatively, not with the maximum potential return. And, of course, review your policy annually with the person who sold it to you. If you buy this policy from a reputable agent who ***fully*** understands how this strategy works, you won't have any problem. Obviously, we are qualified to help you with this strategy.

In these permanent policies, all of the money you put into them will be returned to you, **ALWAYS**, either while you are alive, as tax-free income, or it will go to your heir's income tax free. If you are going to get all of your money back sometime in the future, what does that mean? It means that there is really no cost (only a cash flow issue). Is that the way you understood it?

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