Episode #165: Whole Life vs IUL: Which One is Better?

Video Transcription

Hello, welcome to another episode of "Money Script Monday." My name is Marcus Kiel. Today, we'll be covering the topic of whole life versus IUL, which one is better? But before we do, I'd like to start with a little story. I cleaned out my car recently, and it's fairly old. And I gathered a bunch of stuff and put it in a box and brought it into the house, and I'm saying like over a decade worth of stuff. And my daughter goes through the box, and she pulls out a flip phone, says, "Daddy, what's this?" I said, "Baby, this is a phone. This is what we used predates you. And it's what we made calls on, but it doesn't have all the bells and whistles of a smartphone. You can't watch cartoons on it. You can't play games on it, maybe Snake, but nothing with color, no great games." The difference between the two was the motivation between talking about the difference between whole life versus IUL and which one is better, particularly when it comes to retirement income.

So, let's get started. My background is that I came from a very large mutual life insurance company, one of the largest, and really just learned a lot about whole life. And when I got over to LifePro Financial, the concept of IUL, indexed universal life was brought up, and I had no clue what it was. I knew what a UL was, but I didn't know what IUL was. And it really opened my eyes. And I was able to look at older whole life policies and compare them to IUL and saw some drastic differences?

I'm going to go through a few bullet points and then talk about which one is better with regards to income. The first point is interest credit. Whole life, they have the dividend rate and interest credit, and they may say 5%, 6%, 7%, but really after costs, it boils down to right around 3%. And so, that barely keeps up with inflation, and we've seen that on numerous policies? Conversely, when we talk about an IUL, we illustrate right now, 6.5%, but there are some years where there's double-digit growth. You may see 10%, 11%, 14% interest credit that year, and guess what? That's after costs. So, that's gross. This number is after costs, 6%, 6.5% is the illustration, but there are some years that you're going to see double digits. Now, there will be some years that you see a 0. It won't be fully transparent, but over time, it's going to definitely outpace whole life at 3%. And it's based on external indexes; you can track that. Let's take the S&P 500; you mark it one day, you are pausing the anniversary day, 365 days later the annual point to point, if it's higher up to the cap, you'll get that percentage. Conversely, if it's beneath that, you can get a 0. But over time, it's going to be a lot higher than whole life. So, interest credit.

The second bullet point I want to bring up is talking about loans. With whole life, there isn't a positive arbitrage on loans? What do I mean by that? So, even if it's a non-direct recognition carrier, meaning let's say you have $100,000 of cash value and you take out $50,000, you can be credited on the entire $100,000? That's the non-direct recognition. Only a handful of whole life carriers have that. Most will be direct. Direct just means you have that $100,000; you take out $50,000, you'll only be credited on the $50,000. Let's say the loan rate is 5%, and we know that we're going to be credited right around 3% after costs, every year there's a negative. Loan rate 5%, interest credit 3%? There's a 2% difference there negatively, and so, there's no positive arbitrage? There's no increase in interest on the loan money. Now, conversely, with an IUL, they have participating loans. Let's use that same example, $100,000. You take out $50,000; you can be credited on the entire amount. And over time, the positive interest accrues over the loan rate.

Let's use that same low rate of 5%. We're illustrating 6.5%, but as I mentioned before, there's going to be some double-digit years. There are some years that you can see 5%, 6% interest credit on the loaned-out values. And so, that positive arbitrage, once again, positive interest over the loan rate is possible with an IUL. It's illustrated. It's possible. I've seen it happen. With whole life, that's not really the case. Even in your best years, let's say you got 5% after costs, 5% interest credit plus dividends, 5% loan rate, it's a wash. You don't have that spread. So, that's the second point.

The third point is transparency. With whole life, we talked about the black box here with dividends. They're not guaranteed, and the dividend rate depends on the company's success. in a positive year and mortality is low, you can receive a high dividend. But once again, we know after costs what that number is going to be. But if the company is not doing as well, and mortality is high, that dividend rate can be lower?

You're guaranteed to get something, that something could be 1%? With an IUL, it's fully transparent. You can check the external indexes S&P 500 on your smartphone or other allocations. There's a company where you can even lock in interest credit. Let's say you reach that 10% or that 12%, you could lock in that 12% for the remainder of the year. I mean, you can do that right on your phone. So, that's very impressive there. The cost is itemized and listed in the illustration. When we talk about if you're still paying the premium, premium load, administration costs, cost of insurance, expenses, other credits, it's all listed on the IUL. It's fully transparent, so you can see all that. You can't see that with the whole life. If you go shopping and get a receipt, you want to check everything on that receipt or something or bigger purchases. You want to know exactly what's going on, with an IUL, you can, with whole life, you cannot?

For those three reasons, interest credit, positive arbitrage, transparency, we talk about income? With whole life, because there's really no positive arbitrage and you're only receiving 3% after costs, there really isn't a chance for income? Whole life is the guaranteed death benefit, and the icing on the cake is the savings account? I have some money, some accumulation years from now. If we purchase an IUL and use the same amount of years, you get a higher interest credit; you have the positive arbitrage of the costs and fees. You can receive yearly income from a starter retirement until age 100. Forty-year-old paying in for 25 years, income year 26 through age 100 for the individual is possible because of these reasons? An IUL is for supplemental retirement income, and the icing on the cake is the death benefit. Okay.

Hopefully, from today's lesson, we can see, based on the bullet points here, the differences between whole life and IUL. Whole life, which has been around for a very long time, IUL has been around for maybe a couple of decades but definitely a better vehicle. And I believe the answer is clear when we talk about whole life versus IUL and, particularly, retirement, income tax-free. Tax-free supplemental retirement income, the answer is clear, IUL is better. Please contact your local financial advisor to see if an IUL fits your needs. Thank you.