Episode #171: Will AG-49A Lead to the Death of IUL Sales?

Video Transcription

Hi, welcome to another episode of "Money Script Monday." My name is Brian Manderscheid. Today, I want to answer the question: will AG-49A lead to the death of IUL sales? Before I answer that, I did want to give a quick backstory. Back when I first came into the industry back in 2006, IUL was a new up-and-coming product and only a handful of companies offered it and some of the major insurance companies thought that this was a fad product that wouldn't stand the test of time. Fast forward to today, IUL sales have continued to grow over the years and most major insurance companies have an IUL policy in their product portfolio. The reason being, it offers a ton of consumer value clients are looking to capture and medium to high rates of return while also not having the stock market risk with all of the tax advantages that life insurance companies offer. To answer the question “will AG-49A lead to the death of IUL sales?”, I first want to talk about why these regulations are needed. This is not new. AG-49 is not something new. We had phase 1 back in 2015. Back at that time, there was a whole life coalition of five of the major insurance companies, whole life companies, that saw IUL sales continue to soar while their market shares started to dwindle. They wanted to have the difference between whole life and IUL illustrations to be more similar, even though IUL offers much higher long-term upside potential. AG-49 went into effect back in 2015, which essentially reduces the illustrated income and reduces the illustrated arbitrage when you go to access the money via an indexed loan.

What happened as a result of these regulations? Many insurance companies went back to the drawing board and created new features and benefits for their IUL policies, which include things like persistency bonuses and multiplier bonuses. One company back in 2018 started to push the envelope and created a very high charge, a very high multiplier bonus product to get around these AG-49 rules that prevented companies from illustrating in the excess of 10-12%. With this multiplier feature, they can illustrate a 12-13% gross rate of return, even though the maximum AG-49 illustrated rate was closer to around 6%. In addition, they had a high charge of 7.5%, with the old adage of 0% no longer being your hero. If you had a stock market drop, the client would have no rates of return in the policy plus a 7.5% charge, plus all the high mortality fees of that policy, that can drag your account value backward in a hurry.

As a result of these companies coming out with these very aggressive rogue products with high multiplier bonuses and very high expenses, there've been some class-action lawsuits because of these types of abusive products and sales, and these have claimed things like fraud and deceit, intentional misrepresentation, and even professional negligence. What the clients have said, the plaintiffs have said is that what they were shown isn't what they received. They didn't receive proper disclosure. Why this new regulation is needed is because these rogue companies are coming out with products that went around the spirit of AG-49, which was to reduce the projections that we're providing to consumers.

What are the changes in this new round of AG-49A? First, the intention previously was to create a more standard playing field and reduce the projections. The same mindset applies today. The regulations are aimed to reduce the projections that we're showing in IULs, as well as create a more level-playing field in the industry where non-multiplier bonus products and multiplier bonus products are showing relatively similar benefits. The actual changes are two-fold. Number one is that it's going to prohibit not the actual multiplier bonus but prohibit illustrating the multiplier bonus in excess of the maximum AG-49 rate. So, you can still have products and still have these bonuses, and they can still be illustrated, but they just can't go over and above the illustrated rate like they currently can in today's climate. For example, let's say you had a policy with a 6.4% maximum AG-49 illustrated rate, this is the maximum ceiling that you can illustrate on a projection. And let's just say, hypothetically, you are reducing the illustrated rate in the software down to 6%. Let's also say this policy had a 15% multiplier bonus. For the consumer, they would get a 6% indexed return, plus a 15% multiplier bonus which would be a total gross return of 6.9%. This would violate this new round of AG-49A because 6.9% is greater than the 6.4% illustrated rate. While you can illustrate the multiplier bonus, it can't exceed the 6.4% in this example. If you were illustrating the maximum illustrated rate, 6.4%, in this example, you'd be able to show no multiplier bonus because you can't go over and above that limit.

In addition to the restrictions on multiplier bonuses and how that can be illustrated, the second thing is a reduction of the maximum illustrated spread on indexed loans. Currently, there's a 100-basis point or 1% maximum spread between the borrowing cost in the IUL and what the borrowed portion of cash value can earn. That's been cut in half with AG-49A down to 50 basis points. For example, let's say you had an IUL with a 5% loan and you borrowed an indexed loan from the policy. On the illustration, that borrowed cash value can only earn 5.5%, which is a 50-basis point arbitrage. A consumer could borrow at 5% and cap out and earn 10% or 12% and have 5% arbitrage, but on the illustration, we're only able to show 50 basis points for the maximum arbitrage. All these changes are going to come into effect on December 14th, 2020. It's coming up right around the corner. The next thing you may be asking yourself is how is this going to impact and affect IUL illustrations?

Here at our firm, we've always had the mindset to underpromise and over-deliver. With AG-49, the first round in 2015 didn't affect us because we were already illustrating at those guidelines even back before those regulations went into play. Today, we're likely going to see about a 10-15% reduction in illustrated income on an illustration. Let's say hypothetically we were showing $100,000 of illustrated tax-free income for a policyholder. We're only going to show roughly $90,000 because of these new regulations.

$90,000 of income tax-free is still a great amount of benefit when we put an indexed universal life policy into someone's overall holistic retirement plan. We feel that the consumer value is there, and we feel that in our planning process, we're still going to show a considerable amount of value and benefit to the policyholder, even in these AG-49A reduced climates. Again, we've known this was coming. We've been paying attention to what's going on in the industry. Behind the scenes, we've been building a bridge to get down to these lower projections. Over the last few months, we've been even more conservative on how we illustrate IULs as far as greater reductions on the illustrated rate and a greater reduction in the illustrated income. When we go into this new climate again, we shouldn't see much of a change at all, and we should continue to thrive in this environment. Industry-wide, we're likely to see more like a 25% reduction in the illustrated income. Let's say that same $100,000 income in the current climate may be more like $75,000 industry-wide. The reason being is most agencies and advisors currently illustrate the maximum benefits that the IUL will provide with no changes in the illustrated rate and no changes in the illustrated income.

These other agencies may have a harder time adjusting to this climate. Showing a much greater reduction from $100,000 to $75,000 is a little bit harder to swallow for consumers looking at IUL for the first time. For highly leveraged designs, like these types of products or concepts like premium finance, they're likely to see a much greater reduction in the illustrated income because those products and concepts rely on a high amount of arbitrage when you borrow via an indexed loan. We're likely to see more of a 60-75% reduction in the income drawdowns on these highly leveraged types of products and designs. That same $100,000 of income may only be $25,000 or $40,000 with these changes. That's likely to be a harder conversation for your prospects when you were relying upon a high amount of leverage in an IUL sale. Lastly, we've been talking about illustrations and how these policies will project. The key thing I want you to take away from this is the consumer value does not change with an IUL. The only thing AG-49A does is restrict the illustrated rate with multiplier bonuses and reduce the illustrated income on an illustration on a projection for a policyholder. We feel the consumer value is still extremely strong. We're in a low-interest-rate environment.

People are looking for yield without having to take a conservative amount of risk. We feel IUL fits in perfectly for today's climate, especially when you throw in all the tax advantages that IULs provide in a situation where debt is climbing and people are looking for ways to reduce their taxes in retirement.

To wrap things up, to answer the question: will AG-49A lead to the death of IUL sales? We as a firm believe the answer's no. We continue to see IUL sales climb even in the previous round of AG-49A. We've made plans. We have created plans here at the home office to build a bridge and provide more conservative illustrations. Once these guidelines take place on December 14th, you shouldn't see any interruption. IULs will still look the same or close to the same, and we'll still, most importantly, deliver the same amount of consumer value to your policyholders and clients. If you have any questions, please feel free to contact your field support representative. We'll be happy to go into this topic in more detail and provide you illustrations on how this would look for your policyholders. Thank you very much. We'll see you next time.