NAEPC
Journal
of Estate & Tax Planning

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The Life Insurance-Other Financial Services Sectors Communications Gap

The author contends that the solution is preparing hypothetical illustrations using common market return assumptions.

By **Mark Whitelaw** | February 27, 2019

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A recent ThinkAdvisor Life/Health article raised this question: Can members of the life insurance community explain themselves to other players in the financial services sector?

(Related: 5 Questions About Life Insurance for 2019 (https://www.thinkadvisor.com/2018/12/26/5-questions-about-life-insurance-for-2019/))

Here's my response, with my comments focused on how members of the life insurance community *can* explain themselves.

Whether life insurance community members have the ability to explain themselves to counterparts in other financial services sectors is a multi-faceted topic.

- Can all agents serve in this role? No. Only those that are FINRA registered representatives have access to the full array of products and can use financial services consistent language.
- Can hypothetical illustrations of insurance products be prepared consistent with financial services alternatives? Variable and fixed indexed annuity and life insurance products can, fixed insurance not linked to the market can't.
- Can a FINRA registered rep provide hypothetical illustration of all consumer alternatives? That's a broker-dealer question.
- Can hypothetical illustrations of a consumers planning alternatives be prepared in a manner consistent with both FINRA and the National Association of Insurance Commissioners (NAIC) using the consumers' financial planning assumptions? Yes.

The "Math" Perspective

My comments here are strictly limited to whether it is mathematically possible to prepare hypothetical illustrations of today's financial planning alternatives in a FINRA- and NAIC-consistent manner. I am not commenting on whether a broker dealer or FINRA rules would allow you to show these illustrations to a consumer.

In 2012, FINRA announced Rule 2210(d)(4)(C) (effective 2/2013) defining the calculation for comparing tax-deferred and taxable alternatives – "Hypothetical illustrations of mathematical principles." FINRA Notice 12-29 states "By placing this rule language in FINRA Rule 2210, FINRA is clarifying that these standards apply to any illustration of tax-deferred versus taxable compounding, regardless of whether it appears in a communication promoting variable insurance products or some other communication, such as one discussing the benefits of investing through a 401(k) retirement plan or individual retirement account."

No more fuzzy math, but a prescribed calculation to be used across any tax structure offering fund investing. As an example, the ability to calculate the net result of an un-capped 401(k) vs 409A NQDC vs un-capped Roth IRA v. variable universal life (VUL) v. non-qualified variable annuities v. a taxable brokerage account with the only material illustration variable being the tax structure.

In 2015, the NAIC announced the Actuarial Guideline 49 calculation for setting the maximum permitted illustration rate for an indexed universal life (IUL) policy. That's a calculation where the S&P 500 Total Return (dividends reinvested) can be applied to calculate the S&P 500 Total Return equivalent return.

The NAIC illustration rate calculations for IUL and indexed annuity products encompass every one-year ending return within a calendar year. By averaging all 250 plus ending returns along with reporting the minimum and maximum within that year you have a better understanding of how Indexed products could have performed compared the same calculation applied to fund alternatives where daily share prices for the same period is available.

FINRA + NAIC = Complementary Planning Best Practices

Variable and indexed insurance products are planning complements.

- Full fund based asset allocation.
- Structural allocation by utilizing both indexed and variable products in an allocation.

Combining FINRA and NAIC math allows financial planners to demonstrate these alternatives based on the consumers market and tax assumptions … and health.

"How's Your Health?"

Medical science extending life expectancy, reducing insurance costs, has changed the old life insurance/investment tradeoff.

- Life insurance: Helps if you die early.
- Investments: Help if you live.

FINRA's calculation, if applied to a VUL policy and taxable fund investing, typically illustrates the performance of the VUL policy this way:

- Comparable or greater lifetime benefits through illustration age 120.
- Added lifetime death benefits regardless of how long you live.

Today, non-qualified asset financial decisions are divided into those that are healthy, or not. "How's your health?" has evolved from a life insurance question into a non-qualified asset suitability/qualification question.

The Collaborative "Puck"

Americans own $9.9 trillion of mutual funds in taxable structures outside retirement accounts, according to the Investment Company Institute 2018 Fact Book.

- How much of that $9.9 trillion is held by healthy individuals with death benefit needs and need those fund objectives to accumulate in value as efficiently as possible by their RIA/trustee?

The need for this level of insurance–financial services collaboration/disclosure/dispute-defensible documentation is quickly evolving from a "nice-to-have" to a "need-to-have."

So, to sum up: Can the life insurance community support the financial services sector collaborate in the best interest of the client?

The math is available to prepare hypothetical illustrations using common market return assumptions.

Will medical advancements extending highly compensated white-collar life expectancy continue to reduce retail and institutional (VUL/IUL) life insurance costs and continue to increase the mathematical advantage of using the Internal Revenue Code Section 7702 pricing and tax structure as an investment, tax and risk management alternative over other taxable alternatives?

Yes. And that's not a life insurance pitch, but the math behind the economics of longevity.

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