Qualified Insanity™:

Is there a better way to save for retirement?

Let's start with a Reality Check

- Are you:
  - Currently participating in a "Qualified (to pay taxes later) Retirement Plan" like a 401(k) or IRA?
- Do you:
  - Understand the 4 Wealth Eroders in Qualified Plans?
    - Exposure to Market Losses
    - Exposure to Future Tax Increases
    - Costly Fees & Expenses
    - Limitations on Liquidity

History of Qualified Plans

- Qualified Plan = employee contributes to savings account with pre-tax dollars; taxed at time of distribution
  - The employer may match some or all of your contribution
- IRA & 401(k) created by Congress in 1970's
  - Never designed to be a standalone retirement plan
  - At the time:
    - Most employers offered "Defined Benefit"/Pension Plan
    - Social Security was solvent

Wall Street Loved Them! WHY?

- Opened up huge opportunity to sell mutual funds to Middle America
  - Employers literally let them in front door to sell to employees
  - Supported/reinforced with multi-billion dollar ads
- Qualified Plans were a huge win for employers
  - Got them out of defined benefit/pension business
  - Shifted risk to the employee
  - Today only about 11% of private employers offer defined benefit pension plans

Meet the 4 Wealth Eroders

- Exposure to Market Losses
- Exposure to Future Tax Increases
- Costly Fees & Expenses
- Liquidity Penalties

Exposure to Market Losses

"Rule #1: Never Lose Money.
Rule #2: Never Forget Rule #1."

\- Warren Buffett

Exposure to Market Losses

- Since 2000, the S&P 500® has had two years of **declines greater than 20%**
- Going back to 1900, history suggests we can expect a market "correction" (decline) of at least 10% once every 3 or 4 years
- History also suggests the market is nearly impossible to time consistently

Market Losses Aren't Easy to Recover

- Consider this: a 40% decline requires a 67% increase just to get back to even.
- A 40% decrease followed by a 40% increase means your account is *still down 16%*
- You have to be *up 66.6%* just to break even following a 40% decrease

Start = 100
Down 40% (year 1)
End = 60
Up 66.6% (year 2)
End = 100 (net/even)

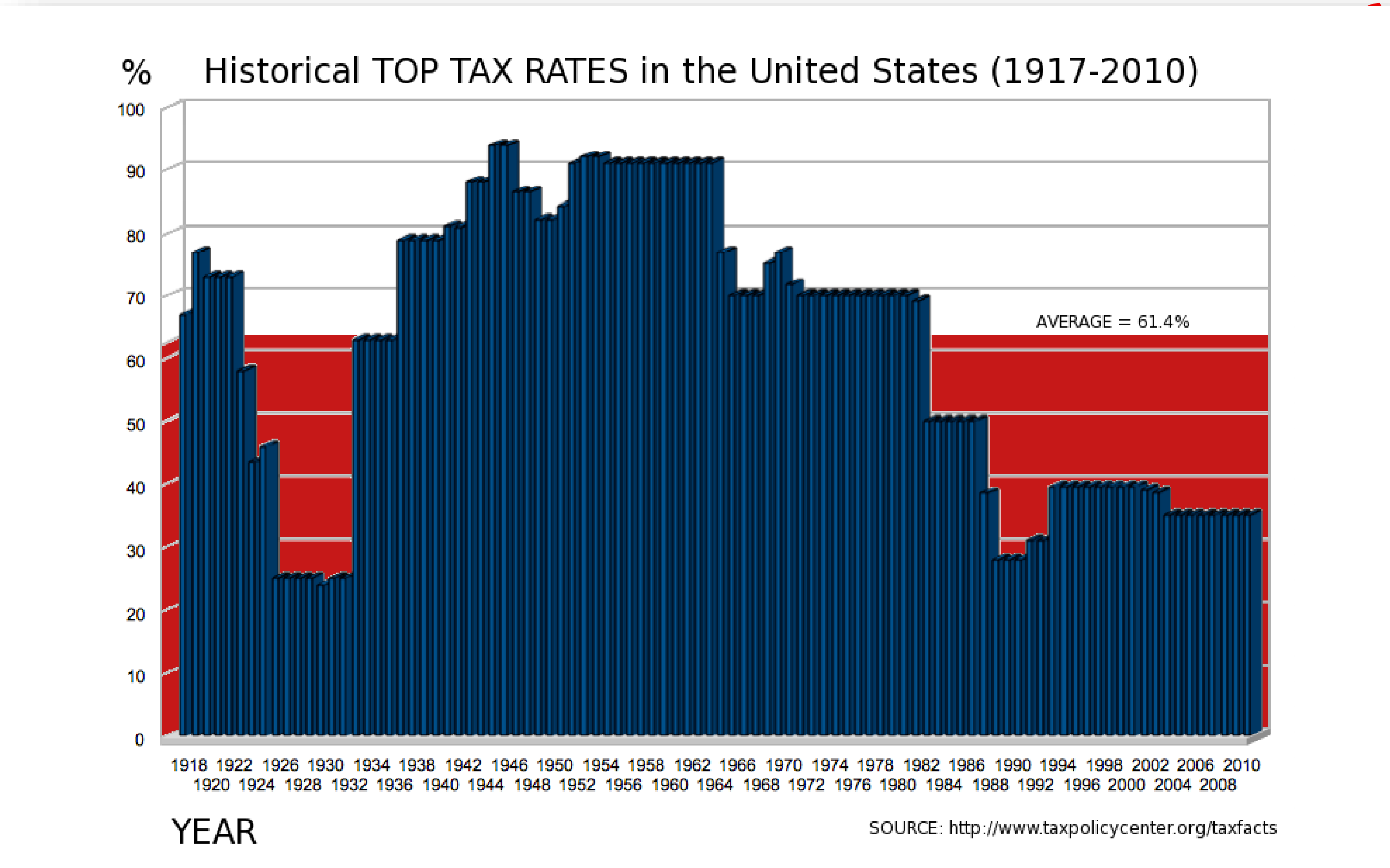
Start = 100
Down 40% (year 1)
End = 60
Up 40% (year 2)
End = 84 (net down 16%)

Exposure to Future Tax Increases

- One primary advantage of Qualified Plan is tax-deferral
  - Don't have to pay taxes now
- Reality Check:
  - Right now, statutory tax rates are historically low
  - For many families, the common saying that you'll have a lower tax rate in retirement is a myth

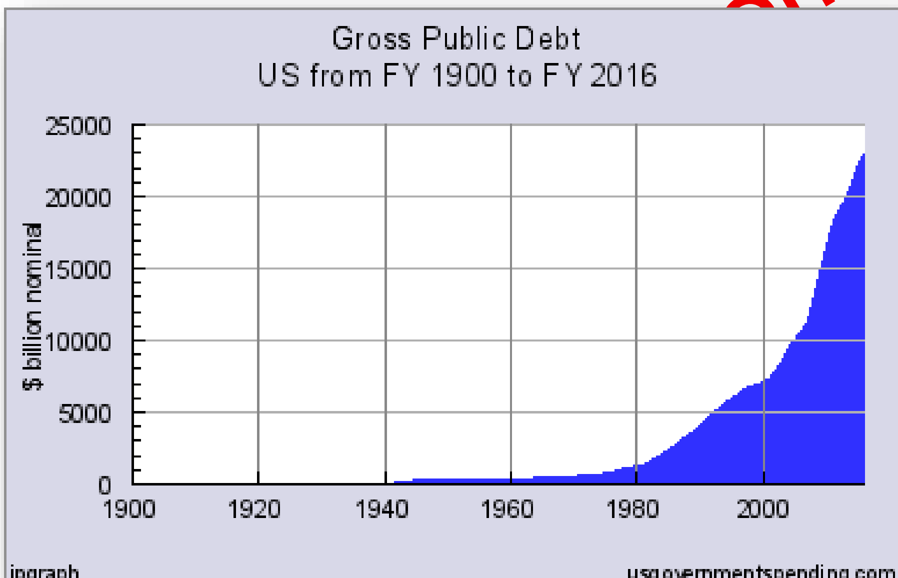
You are deferring taxes, but you may be deferring them to a future time when you must pay a higher rate!

Statutory Tax Rates are Historically Low



Government Spending > Revenue

What do you think this may mean for your future tax rates?



Exposure to Future Tax Increases

- No one knows for sure what future tax rates will be
- Here's what we do know:
  - Right now, tax rates are historically low
  - Our government spends more money than it takes in
  - Common sense says the current state of affairs is not sustainable in the long run

Exposure to Future Tax Increases

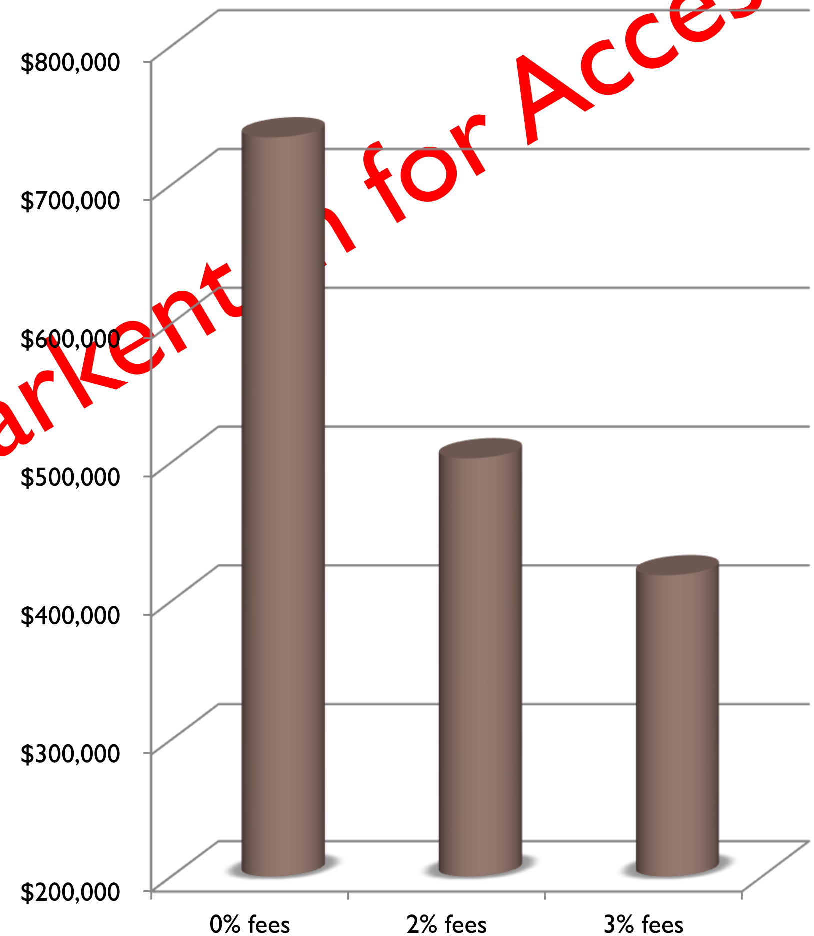
- The case against your tax bracket decreasing in retirement:
  - Many of your deductions go away
    - Mortgage Interest on Personal Residence
    - Children (both a deduction & credit!)
    - Qualified Plan Contributions

Costly Fees & Expenses

- Secure Retirement Institute research indicates most people don't know what their Qualified Plan costs them
  - 50% have no idea what the fees are
  - 40% think they pay no fees
- Research indicates average plan costs 1.4% in fees & expenses
- Actively managed funds can add another 2% or more
- Total fees/expenses can take 3% or more out of returns

Just Math: What does 2% or 3% mean?

- Individual contributes $500/month ($6,000/year) to something for 30 years.
- After 30 years, an 8% rate of return would yield $734K
- But what if he paid 3% in fees and expenses?
  - **Then he only realized a 5% return, which would be $419K (43% less!)**
- Only 2% in fees and expenses?
  - **A 6% return means he'd have a slightly better $503K (or only a 32% haircut!)**



Liquidity Penalties

- Generally speaking, withdrawals from your qualified plan prior to age 59½ are subject to a **10% penalty**, (apart from normal income taxes owed on distributions)
- Life Happens – even for emergencies, you still pay a penalty to access YOUR money:
  - Lose your job?
  - Need to pay for kid's education?
  - Want to start a business?
  - Want to retire early?
- Americans paid $5.8 billion in penalties in 2010!

There IS a Way to Stop the Qualified Insanity™

- It's called **Indexed Universal Life (IUL) Insurance**
- Avoids and/or minimizes the Four Wealth Eroders
  - Exposure to Market Losses
  - Exposure to Future Tax Increases
  - Costly Fees & Expenses
  - Liquidity Penalties
- One Bonus Benefit
  - Comes with a permanent death benefit, so your plan self-completes if you die prematurely

Universal Life

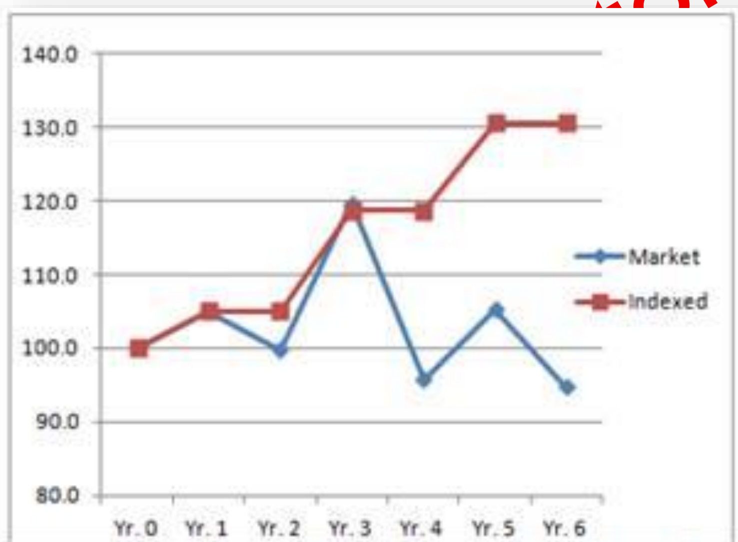
- Flexible, adjustable-premium life insurance
- Every month, cost of insurance & policy costs are deducted, the rest goes into an interest-earning cash accumulation account

Indexed Universal Life (IUL)

- Universal Life *plus:*
  - The option of having interest credited based upon an external index (such as the S&P 500®)
- All of your gains are protected – never lose principal due to a market downturn
  - If the index goes up, you are credited interest for a portion of the gain
  - If the index goes down, you receive no interest during the period, but you do not lose any value either
- How do insurance companies offer this?
  - Achieved though safe hedging strategy like call options

What does it look like?

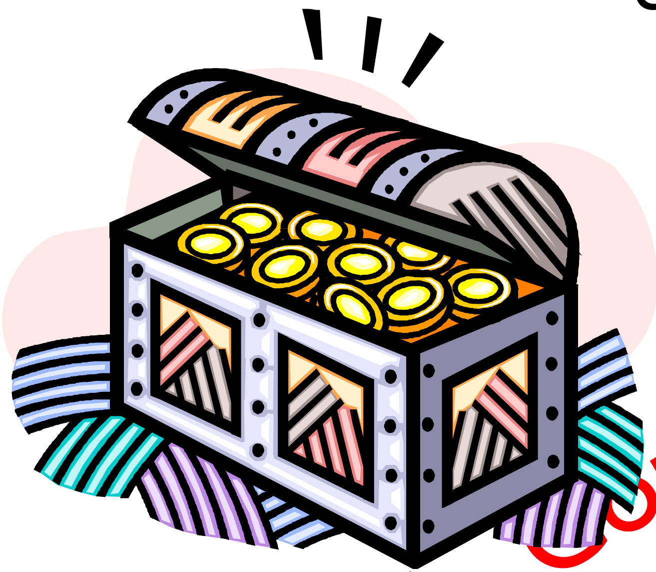
The Cash Account in the IUL (red line) increases when the index increases, but does not decrease even when market declines (blue line).



	Yr. 0	Yr. 1	Yr. 2	Yr. 3	Yr. 4	Yr. 5	Yr. 6
Market	100.0	105.0	99.8	119.7	95.8	105.3	94.8
Indexed	100.0	105.0	105.0	118.7	118.7	130.5	130.5
	Delta	5%	-5%	20%	-20%	10%	-10%

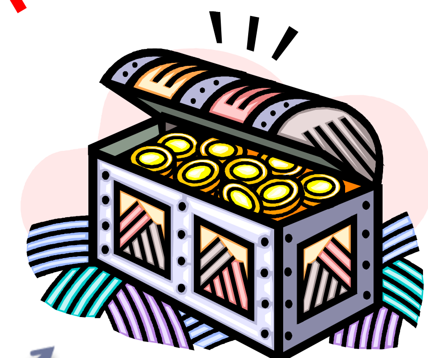
Living Benefits

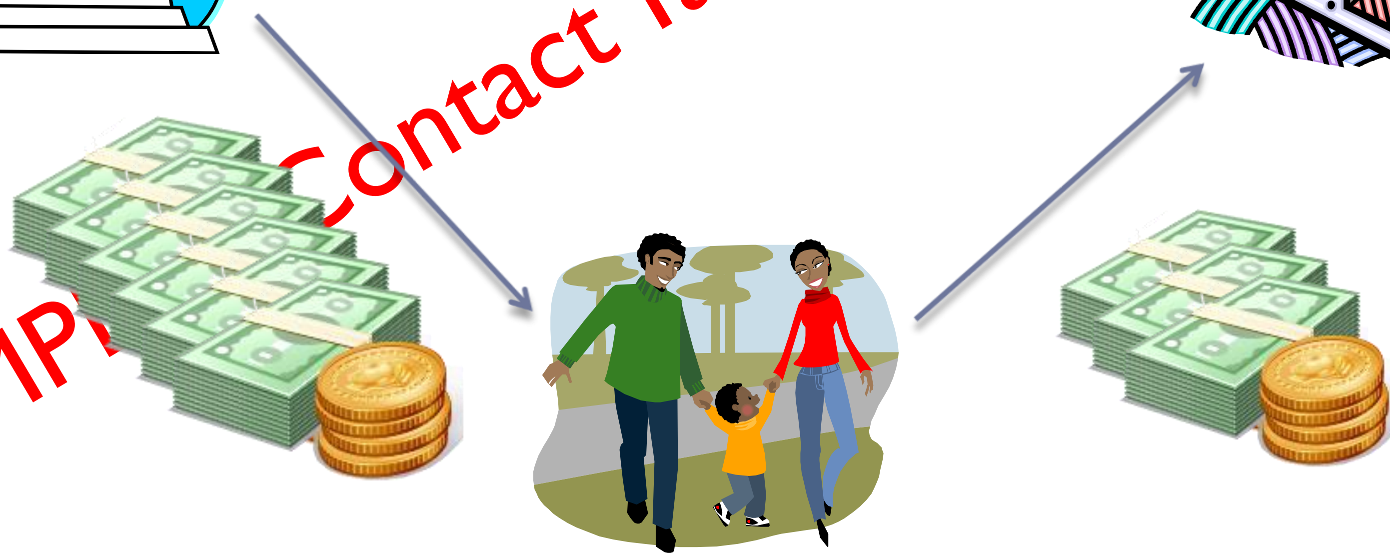
Policy loan from the cash accumulation account creates **tax-free** cash flow you can use



Death Benefits

At death, your beneficiaries use the death benefit to repay any loans, then keep the balance





IUL = Viable Alternative to a Qualified Plan

- IUL can potentially grow cash value that can be accessed via policy loans:
  - In effect, you create a **tax-free cash flow for life**
- Addresses 4 Wealth Eroders
  - Market Losses
  - Higher Taxes
  - Costly Fees & Expenses
  - Lack of Liquidity
- Bonus Benefit
  - Permanent Death Benefit

Addresses Exposure to Market Losses

- This one is simple: you will **never** lose money in an IUL because of declines in the market index
- Any gains are locked in via "Annual Reset" feature
- Possible because of safe hedging strategy/options used by insurance company

Addresses Future Tax Increases

- IUL premium payments are made with after-tax dollars
- Pretty simple: when/if you access your money via policy loans, you are not taxed again on your money

"Would you rather pay taxes on the seed or the harvest?"

Addresses Fees & Expenses

- You will have fees & expenses in the IUL
- IUL expenses are clearly itemized in your annual statement
- One of biggest costs – cost of insurance – is nevertheless quite useful: *it's what creates your permanent death benefit!*
- Even considering cost of insurance, over the long haul, IUL can often be a lower-cost retirement savings option

Addresses Liquidity Penalties

- Access your money any time you want to (subject to the terms of your contract):
  - Many contracts have "surrender charges" that limit the amount you can withdraw without penalty in the first few years
- However, there's no need to wait until you are 59½
- Best of all, there are no restrictions on what you can use YOUR money for!

Bonus Benefit: Permanent Death Benefit

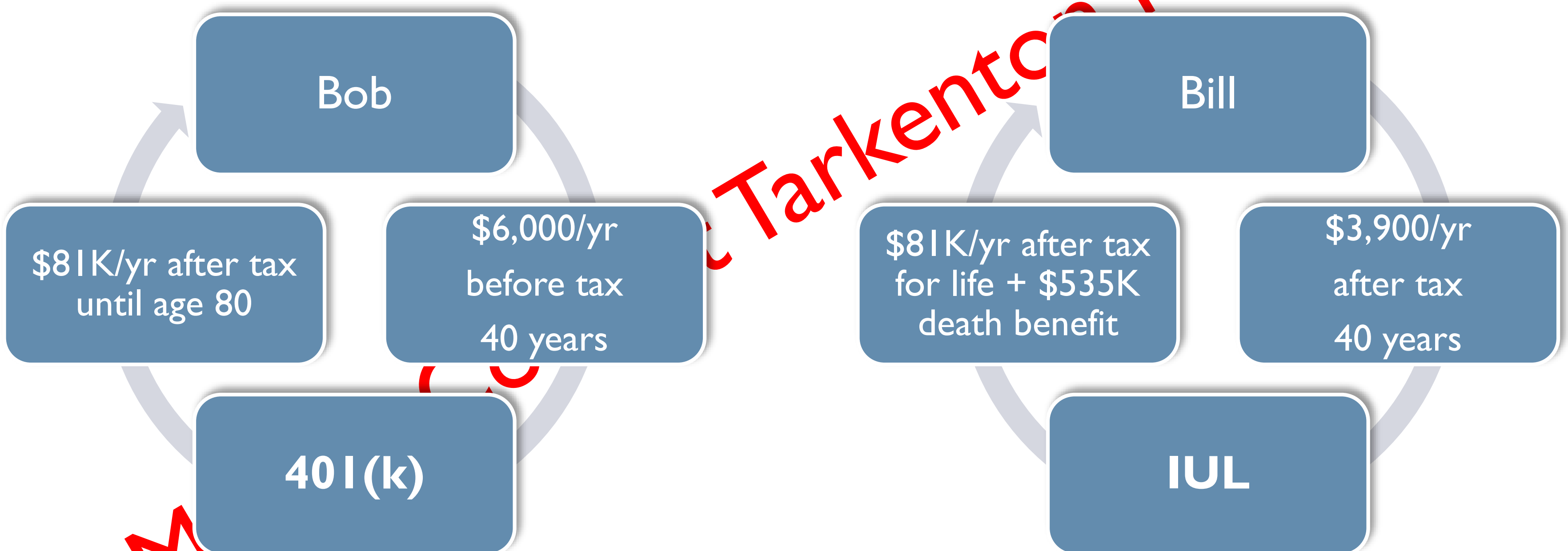
- How much is a 401(k) worth, that you **plan** to put a bunch of money into over the next 40 years, if you die in an accident next month?
- How about the worth of the guaranteed permanent death benefit provided by IUL?
- There are also many other applications for IUL beyond retirement savings:
  - Leveraging flexible policy chassis
  - Leveraging the tax-advantaged status of life insurance

So…What's the Catch?

- There really isn't a catch, other than this: **IUL is a long term commitment, and you should have a long term planning horizon, say 10+ years**
  - Of course, participating in a Qualified Plan (401(k) or IRA) is also a long term commitment, even though many people don't think twice before enrolling
- There are a number of moving parts in IUL policies, and many companies are offering them
  - Work with an advisor and licensed agent that **specializes in IUL** and knows how to **properly structure** a policy for best results

Case Study #1: Bob & Bill

Bob and Bill are 25-year-old twin brothers. Bob takes the 401(k) route, while Bill goes with an IUL policy…



Case Study #1: Bob & Bill

Bob

- $6000/year into the plan for 40 years
- Assume an avg. annual return of 7.5% reduced by 1% for fees and expenses
- 40 years later, he has account value of $1,112,000
- Starting at 66, takes $112,000/yr (taxed at 35%), giving him $81,000/yr
- However, his account value is depleted at **age 80**

Bill

- $3900/year into IUL ($6000 minus $2100 in taxes he pays yearly at 35% tax rate) for 40 years
- Assume yearly credited interest at 7.5%
- 40 years later, he has only $758,000
- Starting at 66, he can take $81,000/yr **tax-free for life** as policy loans
- Bill's family *also* has a death benefit of $535,000 (assuming he dies at age 90)

Bill is also leveraging the power of a participating loan. *He is being charged a contractually guaranteed interest rate of 5% on policy loans while his account is growing at 7.5%. He's still earning money on his money while he has use of it.*

This hypothetical example makes a number of simplifying assumptions to demonstrate a concept. It is important to note that the rate of return is not guaranteed in either an IUL or a 401(k). While an IUL will never lose money because the market goes down or the underlying crediting index goes down, it is dependent upon increases over time for interest to be credited to the account and substantial value to build. There is also no way of knowing with certainty what future tax rates will be. This case is being generous to the 401(k) and doesn't show them increasing. Also, don't forget that any and all guarantees in IUL products are dependent solely on the financial strength and claims-paying ability of the issuing insurance company.

Case Study #2: Janet & Jill

Janet and Jill are Bob and Bill's 40-year-old twin sisters. Janet also takes the widely travelled path and participates in a 401(k) thru her employer. Jill takes the IUL route…

Janet

$17,500/yr before tax for 25 years

401(k)

$75K/yr after tax until age 81

Jill

$11,375/yr after tax for 25 years

IUL

$75K/yr after tax for life + $487K death benefit

Case Study #2: Janet & Jill

Janet

- $17,500/yr into the plan for 25 years
- Assume an avg. annual return of 7.5% reduced by 1% for fees and expenses
- 25 years later, she has account value of $1,098,000
- Starting at 66, she can take $116,000/yr (taxed at 35%), giving her $75,000/yr
- The problem is, she runs out of money at **age 81**

Jill

- $11,375/yr into IUL ($17,500 minus $6,125 in taxes she pays yearly at 35% tax rate) for 25 years
- Assume yearly credited interest at 7.5%
- 25 years later, she has $692,000
- Starting at 66, she can take $75,000/yr **tax-free for life** as policy loans
- Jill's family *also* has a death benefit of $487,000 (assuming she dies at age 90)

It is worth noting that if Jill thought she needed more than $75,000/year tax-free she could simply get a bigger plan. *Here her premiums are modeled to be the after-tax equivalent of Janet's, who is "maxing out" her 401(k). Remember, there are no such limits on IULs.*

This hypothetical example makes a number of simplifying assumptions to demonstrate a concept. It is important to note that the rate of return is not guaranteed in either an IUL or a 401(k). While an IUL will never lose money because the market goes down or the underlying crediting index goes down, it is dependent upon increases over time for interest to be credited to the account and substantial value to build. There is also no way of knowing with certainty what future tax rates will be. This case is being generous to the 401(k) and doesn't show them increasing. Also, don't forget that any and all guarantees in IUL products are dependent solely on the financial strength and claims-paying ability of the issuing insurance company.

IUL: Is it right for you?

Everyone's situation, needs and goals are different. The only way to know if this may be right for you is to talk to a licensed, qualified agent and advisor.

For more information, contact:

[AGENT NAME]
[PHONE]
[EMAIL]
[WEBSITE]

AGENT PHOTO

This presentation is intended to be accompanied by the white paper "*Qualified Insanity*™*: Is there a better way to save for retirement?*" ©2014 Arlinghaus Strategic Advantage Partners, LLC, which includes citations & source information. Agent will be pleased to provide a copy upon request.

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