Allianz Life Insurance Company of North America

PREMIUM FINANCE

# Additional considerations when using a premium finance strategy

Premium finance is a strategy used by high-net-worth individuals and/or business owners to pay for (or finance) the premium for large life insurance policies using bank loans.

This strategy offers several potential benefits. However, it also carries associated challenges (and mitigation strategies) you should understand. These challenges could include:

## CHANGES TO LOAN INTEREST RATES:

**The rate on bank loans has the potential to increase**

**Situation:** The initial plan assumes a future set of bank loan interest rates, which are usually not guaranteed. The actual rates experienced will likely be higher or lower than the initially assumed rate, which could result in the strategy not performing to expectations.

**Mitigation:**

- Increase in required collateral
- Increase in client contribution
- Longer time before bank loan payoff
- Lower income expectations
- Lower net income expectations
- Revised policy benefits
- Consider using a fixed rate bank loan

**Must be accompanied by the Understanding IUL brochure (M-3959) or appropriate indexed universal life insurance consumer brochure.**

Product and feature availability may vary by state and broker/dealer.

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## LOAN NONRENEWAL:

### The lender may not renew the annual loan

**Situation:** Most bank loans supporting the purchase of life insurance policies are renewable annually. However, failure to provide adequate documentation or collateral could jeopardize the loan renewal as well as the ability to make the premium payments on the policy. Banks can also change priorities, especially during economic crises, which could also cause them to “call” (demand repayment of) the loan.

**Mitigation:**

Work with an experienced finance vendor who:

- Is familiar with bank renewal procedures
- Has a process to help ensure loan renewals
- Can work with multiple banks in the event that one lender does not renew the loan

## POLICY UNDERPERFORMANCE:

### The policy may not perform to expectations

**Situation:** Policy performance assumes forward-looking index/interest credit rates, which are not guaranteed. The actual rates experienced will likely be higher or lower than initially assumed, which could result in the policy not performing to expectations and possibly lapsing.

**Mitigation:**

- Set realistic assumptions and use stress tests and diversification strategies
- Work with premium finance vendors that understand the need to properly design policies and conduct annual policy maintenance reviews to help keep the policy on track. Remember, taking early action when a policy deviates from expected performance can help avoid future problems

## COLLATERAL SHORTFALL:

### Can the client afford the policy beyond the projected collateral?

**Situation:** Due to the previous issues listed regarding bank loans and policy performance, the amount of client collateral or premium contribution could be greater than expected. You may need to pay additional premium or provide additional collateral to keep the policy in force.

**Mitigation:**

- Maintain liquidity to mitigate adverse financial scenarios
- Have reasonable design assumptions with realistic collateral requirements
- Bank loan refinancing

## POLICY TAXATION:

### The potential tax implications of loans from policies that lapse

**Situation:** Policy loans may be taxable in the event that a life insurance policy lapses, which may result in the need to pay a large lump sum of money to address any tax situations.

**Mitigation:**

- Reasonable initial designs
- Annual policy maintenance, taking into account the amount of the loans taken from the policy
- Adding a loan protection rider (if available and for an additional cost), which may provide protection from lapse due to an outstanding policy loan


Indexed universal life insurance involves qualification through health and financial underwriting.

Policy loans and withdrawals will reduce the available cash value and death benefit and may cause the policy to lapse, or affect guarantees against lapse. Withdrawals in excess of premiums paid will be subject to ordinary income tax. Additional premium payments may be required to keep the policy in force. In the event of a lapse, outstanding policy loans in excess of unrecovered cost basis will be subject to ordinary income tax. If a policy is a modified endowment contract (MEC), policy loans and withdrawals will be taxable as ordinary income to the extent there are earnings in the policy. If any of these features are exercised prior to age 59½ on a MEC, a 10% federal additional tax may be imposed. Tax laws are subject to change and you should consult a tax professional.

Allianz has not given any legal or tax advice related to the premium financing arrangement. Allianz assumes no responsibility for the obligations, demands, losses, or liabilities, including attorney fees, resulting from the premium financing arrangement.

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Through a line of innovative products and a network of trusted financial professionals, and with 3.9 million contracts issued, Allianz helps people as they seek to achieve their financial and retirement goals. Founded in 1896, Allianz is proud to play a vital role in the success of our global parent, Allianz SE, one of the world's largest financial services companies.

While we are proud of our financial strength, we are made of much more than our balance sheet. By being true to our commitments and keeping our promises, we believe we make a real difference for our clients. It's why so many people rely on Allianz today and count on us for tomorrow – when they need us most.

Products are issued by:

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Product and feature availability may vary by state and broker/dealer.