Premium finance

Common exit strategies

for premium finance strategies

Having an exit strategy is crucial to a successful premium finance plan – which is why it is important to consider at the beginning how it should end.

Typically, the primary goal of the exit strategy when funding a life insurance policy is to provide sufficient liquidity to repay the outstanding debt at a specific time in the future.

THERE ARE MULTIPLE WAYS THIS DEBT (LOAN) CAN BE REPAID:

1. Using the policy's available cash value
2. Using the policy's death benefit
3. Grantor Retained Annuity Trust (GRAT)
4. Charitable Lead Trust (CLT)
5. Lifetime Gift

Because fixed index universal life (FIUL) insurance policies are designed to build accumulation value, accessing the policy's available cash value accumulation through policy loans or withdrawals[1] is a common strategy seen at Allianz Life Insurance Company of North America (Allianz).

A few items to consider if your clients are considering this design:

- Does any available cash value need to be used for other goals or needs?
- The timing of the debt payoff needs to be aligned with the goals of the strategy
- Opportunity for accumulation value to build is not guaranteed
- Accessing available cash value via indexed loans, fixed loans, or withdrawals will impact how the policy will continue to build value over time
- The death benefit will decrease due to outstanding policy loans

When accessing policy loans and withdrawals, your clients should consider that the available cash value and death benefit will be reduced accordingly and that the loans may be taxable if the policy lapses or is surrendered. Your clients should consider the potential tax implications of taking policy loans and withdrawals and discuss them with their tax professional.

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[1]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.

ASI-469 (11/2020)

Using the policy to repay the bank loan

FACTORS THAT YOUR CLIENTS SHOULD CONSIDER WHEN DECIDING TO REPAY THE BANK LOAN INCLUDE:

1. Client's death benefit need
2. Client's life expectancy
3. Estimated number of years for which retirement income will be needed
4. Ratio of the bank loan to policy cash value (see below)
5. Client's other liquid assets

WHAT IS THE LIKELIHOOD OF SUCCESS FOR THE POLICY WHEN THE LOAN IS PAID OFF?

One factor that can be implemented in the design is the ratio of bank loan to policy cash value (loan to value ratio: LTV). You can design a policy with a "target" ratio to help increase the likelihood of the client being able to use any available cash value to pay off the bank loan.

Based on our analysis below, typically, the lower the ratio of bank loan to policy cash value, the more efficient and likely it is that the policy will be able to support paying off the bank loan and staying in force until age 95, without adding additional premium into the policy.

It pays to be conservative with the loan exit strategy as that will help set the client up for the greatest chance of success.

Ratio of bank loan to policy's cash value (LTV)	70% and below	70%-75%	75%-80%	80%-85%	85%-90%	90%-95%
Probability of paying off loan and keeping policy in force to age 95	98%	91%	86%	80%	75%	28%

This analysis uses 1,000 hypothetical economic scenarios based on the return profile of the Bloomberg US Dynamic Balance II ER Index using current caps on Allianz Life Pro+ Advantage℠ Fixed Index Universal Life Insurance Policy. In practice, actual returns are nonguaranteed and index credits could be higher or lower than those indicated in these statistics as a result of a change in caps and different equity performance.

Assumptions: Monte Carlo scenario, Allianz Life Pro+ Advantage Fixed Index Universal Life Insurance Policy, male, age 55, standard nontobacco, 10-pay, 30% Supplemental Term Rider, Loan year 16. Rider is available at an additional cost and is based on the amount of the additional term coverage.

A low LTV does not guarantee success. Two hypothetical examples. As shown in the following examples, results can vary based on the policy's sequence of returns.

Scenario 1

Hypothetical client has a 94.3% LTV which, per the chart above, correlates with 47% confidence in repaying the loan. Typically, this would mean low confidence in repaying the loan and the policy being able to persist until age 95 (without additional premiums).

Bank loan balance at end of year 15 = $1,560,388 / Cash value at end of year 15 = $1,653,921

However, in this case, the design would work out for the client; the policy would not lapse prior to age 95.

Year	Age	Annual return	Accumulation value (before credit)	Policy loan balance	Cash value (before credit)	Net death benefit
16	70	10.28%	$1,651,049	$1,638,408	$12,641	$485,021
17	71	5.58%	$1,843,339	$1,720,328	$123,011	$496,307
18	72	0.00%	$1,958,462	$1,806,344	$152,118	$367,548
19	73	5.77%	$1,955,540	$1,896,662	$58,879	$376,355
20	74	12.29%	$2,082,593	$1,991,495	$91,098	$552,130
21	75	11.04%	$2,374,680	$2,091,070	$283,610	$719,190
22	76	1.18%	$2,673,184	$2,195,623	$477,561	$649,200
23	77	0.00%	$2,705,606	$2,305,404	$400,202	$535,482
24	78	6.80%	$2,701,343	$2,420,674	$280,669	$637,559
25	79	18.61%	$2,907,381	$2,541,708	$365,673	$1,164,833
26	80	27.58%	$3,522,802	$2,668,793	$854,009	$2,204,342
27	81	14.12%	$4,630,433	$2,802,233	$1,828,200	$2,849,963
28	82	6.32%	$5,369,242	$2,942,345	$2,426,897	$3,105,357
29	83	0.00%	$5,743,233	$3,089,462	$2,653,771	$2,940,932
30	84	16.24%	$5,724,813	$3,243,935	$2,480,878	$3,891,325
31	85	10.08%	$6,770,918	$3,406,132	$3,364,786	$4,528,766
32	86	0.00%	$7,526,302	$3,576,439	$3,949,864	$4,326,179
33	87	6.44%	$7,491,803	$3,755,260	$3,736,542	$4,694,514
34	88	0.00%	$8,005,706	$3,943,023	$4,062,683	$4,462,968
35	89	3.48%	$7,958,897	$4,140,175	$3,818,722	$4,551,749
36	90	7.03%	$8,223,422	$4,347,183	$3,876,239	$4,987,362
37	91	12.26%	$8,837,158	$4,564,543	$4,272,616	$5,925,732
38	92	5.46%	$10,036,360	$4,792,770	$5,243,591	$6,195,171
39	93	25.55%	$10,628,404	$5,032,408	$5,595,996	$8,999,658
40	94	13.20%	$13,729,092	$5,284,028	$8,445,064	$10,689,453
41	95	6.48%	$15,815,318	$5,548,230	$10,267,088	$11,444,868
	Return after loan payback	**8.68%**				

Assumptions: Male, 55 years old, Standard nontobacco, $100,000 for 10 year, 1.66MM initial death benefit, fully financed PF repaying loan at beginning of year 16, targeting loan protection rider at age 95, using the Bloomberg US Dynamic Balance II ER Index with a 145% participation rate. Current participation rates are not guaranteed. Assuming the guaranteed minimum interest rate of 0.10% and maximum charges, there would be insufficient cash value to support the strategy and the policy would have lapsed in year 17. If the policy was projected at guaranteed charges and crediting, it would have insufficient cash value to repay the bank loan.

Scenario 2

Scenario 2: Hypothetical client has an 82.6% LTV with 87% confidence in repaying the loan and the policy being able to persist until age 95 (without additional premiums).

Bank loan balance at end of year 15 = $1,560,388 / Cash value at end of year 15 = $1,889,648

Here, even with the lower LTV and higher confidence, this hypothetical client's policy would not perform to expectations. The policy **would not** be able to pay off the bank loan and stay in force until age 95. The policy would lapse in policy year 24.

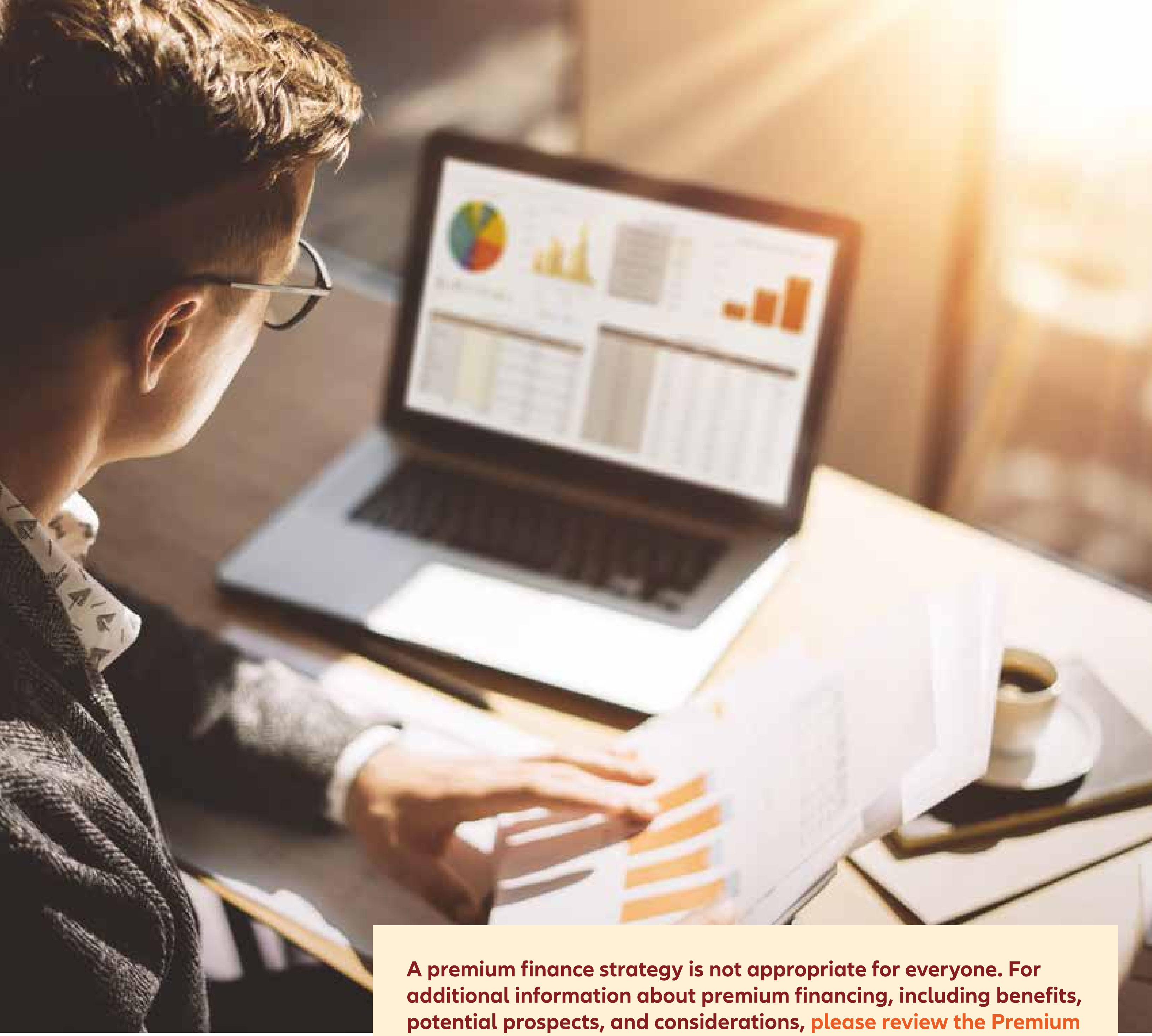
Year	Age	Annual return	Accumulation value (before credit)	Policy loan balance	Cash value (before credit)	Net death benefit
16	70	6.12%	$1,886,368	$1,638,408	$247,960	$683,599
17	71	0.00%	$2,015,724	$1,720,328	$295,396	$557,440
18	72	0.00%	$2,012,475	$1,806,344	$206,131	$427,503
19	73	9.38%	$2,009,474	$1,896,662	$112,812	$530,070
20	74	5.10%	$2,223,430	$1,991,495	$231,935	$527,142
21	75	0.00%	$2,351,351	$2,091,070	$260,281	$377,849
22	76	0.00%	$2,348,491	$2,195,623	$152,868	$270,292
23	77	0.00%	$2,345,240	$2,305,404	$39,835	$157,097
24	78	18.11%	$2,341,543	$2,420,674	($79,131)	$0
	Return after loan payback	**2.58%**				

Assumptions: Male, 55 years old, Standard nontobacco, $100,000 for 10 year, 1.66MM initial death benefit, fully financed PF repaying loan at beginning of year 16, targeting loan protection rider at age 95, using the Bloomberg US Dynamic II ER Index with a 145% participation rate. Current participation rates are not guaranteed. Assuming the guaranteed minimum interest rate of 0.10% and maximum charges, there would be insufficient cash value to support the strategy and the policy would have lapsed in year 17. If the policy was projected at guaranteed charges and crediting, it would have insufficient cash value to repay the bank loan.

As you can see, the ratio of bank loan to policy value is one element that clients can take into account that may help increase the likelihood of the premium finance strategy meeting expectations.

Call your divisional vice president to learn more about a premium finance strategy.

FIUL is not a retirement vehicle and does not provide a guaranteed income stream in retirement.



A premium finance strategy is not appropriate for everyone. For additional information about premium financing, including benefits, potential prospects, and considerations, please review the Premium Financing agent guide (ASI-457).

Clients should consult with their tax advisor and attorney before entering into this or any other arrangement involving tax, legal, and economic considerations.

The Bloomberg US Dynamic Balance II ER Index is comprised of the Bloomberg Barclays US Aggregate Custom RBI Unfunded Index and the Bloomberg US Equity Custom Futures ER Index and shifts weighting daily between them based on realized market volatility. The Bloomberg Barclays US Aggregate Custom RBI Unfunded Index is comprised of a portfolio of derivative instruments that are designed to provide exposure to U.S. Investment-grade and Treasury bond markets in excess of a benchmark rate. The Bloomberg US Equity Custom Futures ER Index is designed to provide exposure to large-cap U.S. stocks in excess of a benchmark rate.

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