Interest Rate Arbitrage

Interest rate arbitrage occurs with Indexed Universal Life ("IUL") when:

- The loan interest rate is fixed (typically 4% to 5%);
- There are outstanding policy loans and the selected index yields more than the loan interest rate;
- The cash values securing the loan balances are credited with the yield produced by the selected index as if there were no loans.

Interest rate arbitrage with IUL is a powerful force when coupled with max-funded IUL policies with serious participating loans scheduled for retirement years.

There is a way to accelerate the arbitrage further (Accelerated Arbitrage™). This can be done by coupling it with higher policy premiums and greater policy loans. In this case, the policy owner funds the increase in premiums from another source – like bank loans, with the expectation that the policy yield will also <u>outperform</u> the loan interest being charged by the bank.

Safety Valve

With IUL/premium financing coupled together and assuming a policy with high early cash values is used, plans can be designed in which termination of the plan mid-stream will likely result in the policy having significant residual value after repayment of the bank loan. This is further enhanced by the guarantee that negative arbitrage cannot occur on the IUL due the carrier guarantee that the yield credited to cash values can never go negative regardless of the performance of the selected index.

Suitability

Accelerated arbitrage produces an extraordinary increase, but it is not a plan for the faint-hearted. Suitability of the two arbitrage variations is an important consideration:

- A very conservative client may not be willing to acquire IUL let alone couple it with a premium financing arrangement.
- A moderate client may welcome IUL for its arbitrage potential but be unwilling to include it in a premium financing arrangement.
- A moderately aggressive or aggressive client may be willing to couple both concepts in search of accelerated arbitrage provided the safety valve discussed below is present.

Important Note: The information in this Blog is for educational purposes only. In all cases, the approval of a client's legal and tax advisers must be secured regarding the implementation or modification of any planning technique as well as the applicability and consequences of new cases, rulings, or legislation upon existing or impending plans.

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