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No. 363: Scott Witt's Views on Indexed Universal Life

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Background

In **No. 314** (May 29, 2019), I presented the views of two prominent professionals on indexed universal life (IUL) policies: Lawrence J. Rybka, JD, CFP; and Richard Weber, MBA, CLU, AEP. In that post I said I have never written about IUL and explained why. I do not understand IUL policies well enough to feel comfortable writing about them, and I have always avoided writing about topics I do not understand.

Scott Witt

Scott Witt, FSA, MAAA, is a fee-only insurance advisor and a Financial Services Affiliate member of the National Association of Personal Financial Advisors. He was born and raised in Montana and graduated from Montana Tech in 1993 with a dual major in Mathematics and Computer Science. He received a Master's degree in Statistics from Oregon State University in 1994. He started his career at Northwestern Mutual, where he worked in various actuarial roles for more than ten years. Areas of expertise and responsibility included life insurance pricing, risk management, valuation, mortality studies, and marketing. Before he founded his firm, he worked for Katt & Company, one of the nation's first fee-only insurance advisors. Additional biographical information is on his firm's website at **wittactuarialservices.com/scott-witt**.

I have known Witt for many years, and hold him in very high regard. Some time back we discussed the idea of his expressing his views on IUL. He agreed, and the result is "A Critical Review of Indexed Universal Life." It is in the complimentary package offered at the end of this post.

Witt's Views on IUL

Witt's seven-page, single-spaced review of IUL begins with an introductory paragraph. It reads:

Indexed Universal Life (IUL) has long been touted as a product that provides upside potential with downside protection. With the precipitous market decline in the first quarter of 2020 caused by COVID-19, this is no doubt a great opportunity for those who sold or purchased IUL products to take a victory lap. But should they be celebrating? And more broadly, are IUL products everything they are cracked up to be?

The next section of Witt's review consists of four paragraphs entitled "Understanding IUL Policy Mechanics." The section also includes four "critical observations to understand about the IUL policy mechanics."

The third section, a long one, is entitled "Do IUL Policies Provide an Upgrade Over a Good Whole Life Policy?" The first paragraph reads:

In my opinion, no. They certainly look good on paper, and you can contrive situations where an IUL policy can perform well for short (or even relatively long) periods of time, but over the long haul I do not believe a compelling case can be made for an IUL policy outperforming a whole life policy from a good carrier (say a highly rated mutual insurance company)—particularly if the whole life policy were optimized to reduce agent compensation and maximize policy efficiency.

The third section includes ten numbered and detailed discussions of "issues with many IUL illustrations." The fourth section is entitled "Do IUL Policies Have an Investment Advantage Over Whole Life Policies?" The fifth section is entitled "Premium Financing—Even More Leveraging."

The "Conclusion" has three paragraphs. The first paragraph reads:

When you put it all together, many IUL illustrations resemble a house of cards. When you inject heavy internal borrowing into the illustration (using a favorable and potentially unsustainable arbitrage assumption), you now have another house of cards put on top of the first house of cards. (And for those that are so inclined, you can add another house of cards by introducing premium financing into the mix.)

General Observations

I am impressed by Witt's views on IUL. One point I found especially interesting, discussed in the third paragraph of the fourth section of his review, is how the current illustration rules favor IUL policies over whole life policies.

In my opinion, IUL is a product that is sold by agents who do not fully understand it to clients who do not fully understand it. It will be interesting to see what IUL promoters—insurance companies, marketing organizations, and agents—have to say about Witt's views. I would welcome thoughtful comments from them and others.