inclined Case Study

The True Cost of Direct Recognition Policy Loans

Guardian Life Insurance Example

Summary

Under direct recognition, taking a policy loan will affect the annual dividend paid on a Whole Life Insurance policy. Therefore the true cost of borrowing against the policy can be significantly different than the listed loan rate, and often much higher when accounting for tax implications, especially in scenarios where interest is accrued.

Borrowing from a third party using the cash value as collateral instead of taking a policy loan can be a less expensive, more flexible option.

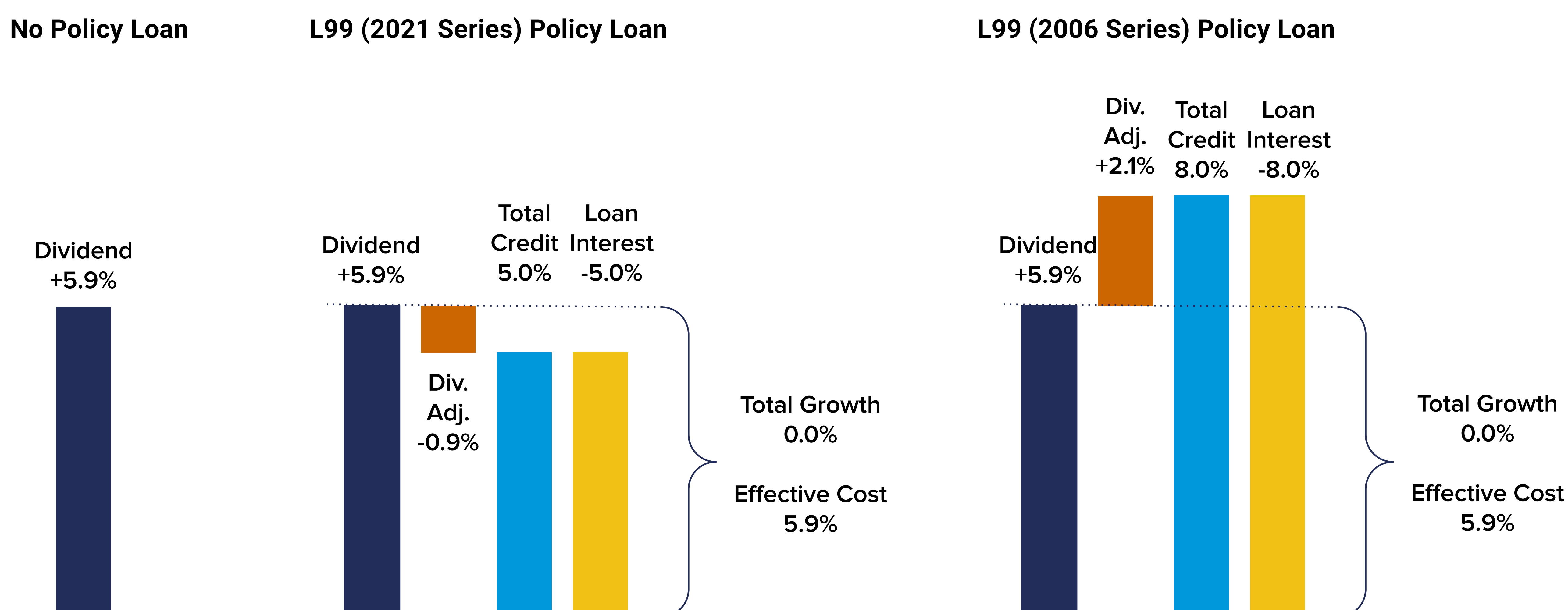
What is Guardian's Policy Loan Fixed Rate?

The answer is not as straightforward as you may think. Guardian applies an adjustment to the standard dividend earned on borrowed funds *"to align the policyowner's net cost of borrowing with the investment return Guardian would have made had the funds not been borrowed."*

To achieve this, Guardian sets target Loan Spreads each year, which in 2024 were 1.00% in the first 20 policy years, 0.50% in years 21+ if the policyholder is under age 60, and 0.10% in years 21+ if the policyholder is older than 60. Then, dividend adjustments are calculated based on the policy's interest rate to achieve the target cost of borrowing.

Guardian adjusts dividends to "align the policyowner's net cost of borrowing with the investment return Guardian would have made." In other words, the cost of a policy loan is similar to the dividend, regardless of the face value rate listed on the policy.

Since the dividend is adjusted to align net borrowing cost with returns, the loan interest rate is immaterial to the actual cost of borrowing. Two policies with different loan rates will have an identical net cost of borrowing:



Example Policy in policy year 21 with a borrower under the age of 60. Assumes 2024 dividend rate of 5.90% and Loan Spread of 0.5% for policies in year 21+ but before age 60.

This adjustment also aligns structures across policy series. Borrowing in the first 20 policy years has the same net cost. After year 20, borrowing is either 0.5% or 0.9% less expensive based on age, as shown in the example on the following page.

10 Pay Whole Life (2021 Series)

Policy Year	Age	Interest Rate	Dividend Adjustment	Cost of Borrowing
1 - 10	All Ages	5.0%	-1.4%	6.4%
11 - 20	Prior to 60	5.0%	-1.4%	6.4%
	60 and older	3.0%	-3.4%	6.4%
21+	Prior to 60	5.0%	-0.9%	5.9%
	60 and older	3.0%	-2.5%	5.5%

Guardian has a variety of loan rates and structures based on policy tenure and attained age, however the effective cost to borrow is adjusted to always be 5.50-6.40% to align with expected investment returns (the dividend).

What is the Impact of Borrowing at the Dividend Rate?

One key benefit of Whole Life Insurance is that it can provide the same after-tax return of an investment with a higher pre-tax return, but without the higher investment risk and volatility associated with other asset classes.

That attractive after-tax return is achieved through the dividend, which is reduced when funds are accessed via policy loan. In 2024 for policies in their first 20 years, that means forgoing a post-tax return of 6.40% (5.90% after year 20 if younger than 60 years old, 5.50% if older than 60).

For high income earners anywhere, but especially in states with high state income taxes, this effect can be quite meaningful:

State	Forgone Post-Tax Gains Policy < year 20, Age < 60	Income Tax Highest Combined State/Federal	Third-Party Loan Equivalent Pre-Tax Impact on Net Returns
CA	6.40%	49.3%	12.62%
NY	6.40%	47.9%	12.28%
TX	6.40%	37.0%	10.16%

Due to the loss of the dividend, high earning clients would need to earn 10.16% to 12.62% pre-tax to offset the impact of the policy loan on post-tax returns. Therefore, the comparable third-party loan rate to a policy loan rate is over 10%.

The lost returns are realized when interest is accrued, as is often the case when using funds for real estate or in retirement. A client paying the interest in cash every year can minimize the taxable difference. However, few clients make regular cash payments on policy loans.

Borrowing from a third party lender, such as Inclined, instead of a policy loan allows policyowners to continue to earn the attractive post-tax return offered by the dividend.

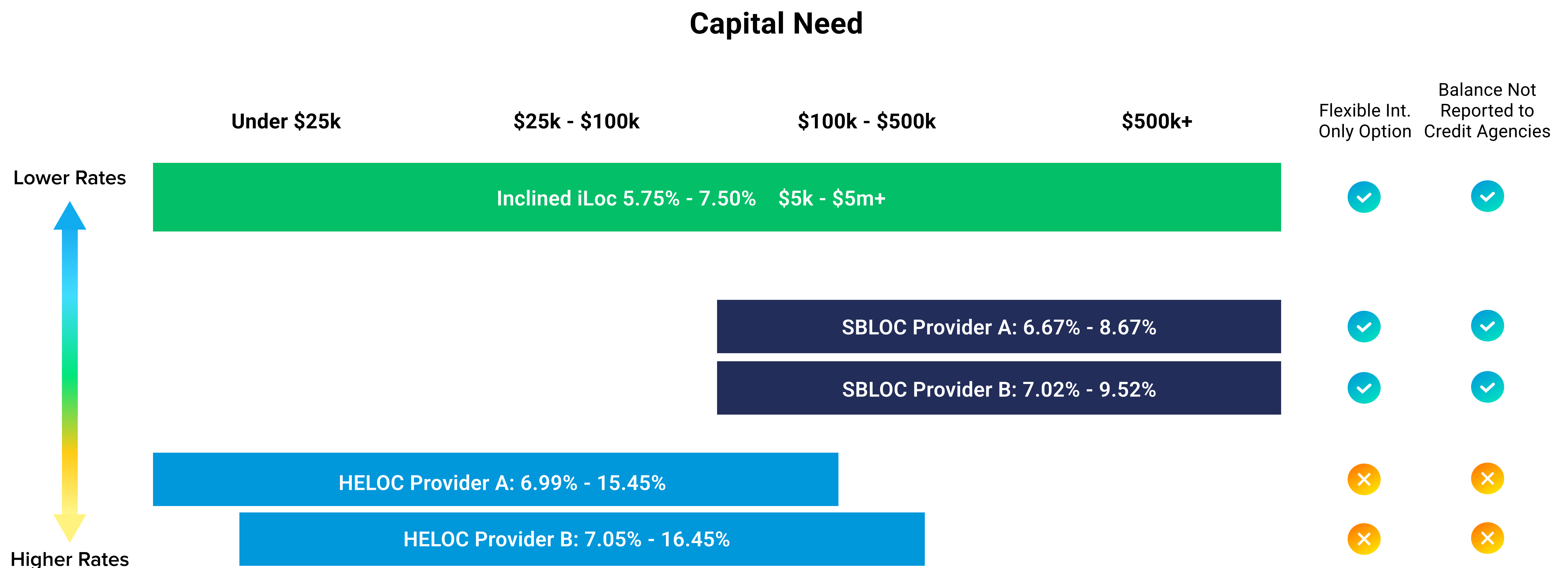
On average, 85% of iLOC clients make regular cash payments against their line of credit – 58% of them use monthly autopay from a connected checking or savings account. Additionally, interest paid on policy loans is clearly not deductible, however interest paid on loans made by a third party may be deductible if used for certain purposes[1].

1 Inclined does not offer tax advice. Please consult a tax advisor to determine deductibility in each case.

Third-Party Cash Value Loans vs. Other Borrowing Options

To protect the post-tax returns earned inside the dividend from the negative impact of a policy loan, clients likely want to consider borrowing outside of the policy. When considering where to borrow, policyowners have a number of options.

As of December 2024, few options offer better rates and flexibility, for both small and large line sizes, than borrowing against cash value via a third party.



SBLOC provider A is Charles Schwab PAL product as of Jan.22,2025 at SOFR + 2.40% to 4.40%, minimum of $100K. SBLOC provider B is Raymond James SBLOC product as of Jan.22,2025 at SOFR + 2.75% to 4.60%, minimum of $100K. HELOC Provider A is Aven's stated APR range as of Dec.4,2024 with $5k-250K line sizes. HELOC Provider A is Figure's stated APR range as of Dec.4,2024 with $15k-400K line sizes.

The Inclined Line of Credit (iLOC) is a revolving line of credit designed to give whole life policyowners the ultimate freedom and flexibility to access the cash value in their policies. We've innovated to offer features and benefits that include:

- **Apply online in 15 minutes or less[2]**
- **Next-day draws[4]**
- **Evergreen lines, no manual renewals**
- **Not reported to credit bureaus**
- **No fees, ever**
- **Access up to 95% of cash value[3]**
- **Minimum $5,000 credit limit[5]**
- **Automatic evaluations for credit limit increases[6]**
- **Competitive rates**

2 Typical application times are 15 minutes. Application review and approval times are typically 1 business day, and funds can be available as quickly as 10 business days from completing an application. However, time estimates are contingent upon insurance carrier response times and may be longer.

3 Credit limits can be up to 95% of the cash surrender value, not to exceed the maximum loan amount from your carrier, inclusive of existing balances. Inclined will also reevaluate your credit limit for you two times per year.

4 Once an Inclined Line of Credit is opened, policyowners can use our online portal to make draws that process overnight. Funds arrive at the receiving bank the next business day, fund availability subject to receiving bank's policies. In some cases, it may take 2 business days.

5 Final underwritten line must be at least $25,000 in Washington D.C., $10,000 in New Mexico and Arizona, and $5,000 everywhere else.

6 When an iLOC account is active and in good standing, Inclined evaluates the credit limit twice per policy, per year and generally increases it with the value of the policy. However, credit limit increases are discretionary and are not guaranteed.

Learn more about the Inclined Line of Credit (iLOC) and get started today by visiting inclined.com