



White Paper Evaluating COLI vs. Fixed Index Annuities for Credit Unions

Discover portfolio optimization and financial growth through our latest expert guide.

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CONTACT

Tony Streeter | SVP Growth

(210) 317-9060

Tony.Streeter@totalbenefitprefunding.com





Executive Summary

This white paper compares Corporate-Owned Life Insurance (COLI) and Fixed Index Annuities (FIA) as investment options for credit unions. It aims to educate credit union leaders on the fundamentals of COLI and FIA, including regulatory considerations under NCUA § 701.19. The paper outlines the financial advantages, regulatory implications, and strategic potential of transitioning from COLI to Fixed Index strategies to enhance long-term investment outcomes. It provides actionable insights for credit union executives to improve their investment strategies, with an emphasis on maximizing returns while safeguarding capital.

Introduction

Credit unions are tasked with balancing the improvement of investment returns while adhering to strict regulatory guidelines. Under NCUA Regulation § 701.19, credit unions may use investments such as COLI and Fixed Index Annuities to offset employee benefits. However, choosing the most suitable vehicle requires understanding their regulatory, financial, and operational implications. Traditionally, COLI has been a reliable choice for steady returns, but advancements in financial products, such as Fixed Index Annuities, offer a compelling alternative with higher growth potential and flexibility. This paper provides an educational framework and actionable guidance to help credit union executives navigate these investment strategies by comparing their structure, risk profiles, and return potential.

What Is Corporate-Owned Life Insurance (COLI)?

Corporate-Owned Life Insurance (COLI) is a life insurance policy purchased by a credit union on the lives of key employees. It is primarily used to offset employee benefit costs by leveraging tax-free death benefits and cash value growth.

Key Features

- **Principal Protection:** The initial investment is protected.
- **Cash Value Growth:** Earns interest at a rate determined by the insurer.
- **Death Benefits:** Provides a tax-free payout upon the insured's death.

Pros of COLI (under NCUA Regulation § 701.19)

- **Regulatory Alignment:** The NCUA allows COLI to be used as an employee benefit funding mechanism.
- **Tax Advantages:** Both the cash value accumulation and death benefit payouts are tax advantaged.
- **Low Volatility:** Provides steady, predictable growth with no market exposure risks.

Cons of COLI (under NCUA Regulation § 701.19)

- **Long-Term Lock-In:** Policies require holding periods of 30–50 years to maximize death benefit ROI.
- **Cost of Insurance:** Premiums and other insurance-related costs reduce returns over time.
- **Discretionary Interest Rates:** Growth is limited by insurer-determined rates, currently averaging around 2.8%.
- **Limited Growth Potential:** COLI lags in returns compared to other investment options.

What Are Fixed Index Annuities (FIA)?

A Fixed Index Annuity is an insurance product that combines guaranteed principal protection with growth tied to a market index (e.g., S&P 500). Unlike direct equity investments, FIAs are not exposed to downside market risks.

Key Features:

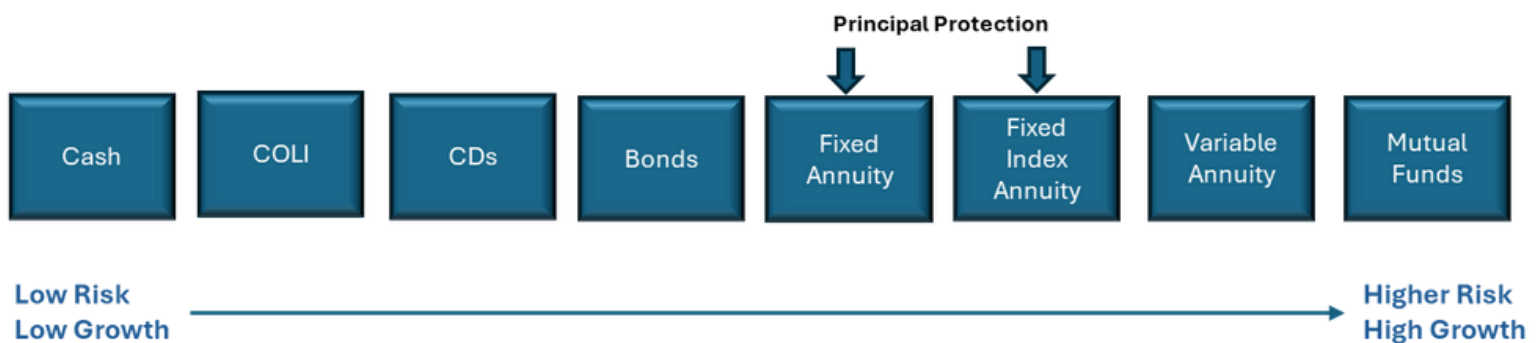
- **Index-Linked Growth:** Earns interest based on index performance, capped at a predetermined rate.
- **Principal Protection:** Ensures no loss of the original investment.
- **No Insurance Costs:** Unlike COLI, FIAs do not carry additional costs such as mortality charges.

Pros of FIAs (under NCUA Regulation § 701.19):

- **Regulatory Compliance:** NCUA permits FIAs as permissible investments to fund employee benefits.
- **Higher Growth Potential:** Offers an average annualized return of up to 10.6% in favorable markets.
- **Shorter Contract Terms:** Typical 10-year contracts allow greater flexibility.
- **No Insurance Costs:** Maximizes returns without reductions for premiums.
- **Deposit Bonuses:** Immediate bonuses, such as Athene's \$1.95M bonus, further enhance income.

Cons of FIAs (under NCUA Regulation § 701.19):

- **Cap on Growth:** Interest is subject to a cap, limiting upside potential.
- **Complexity in Index Tracking:** Requires a thorough understanding of how index-linked returns are calculated.
- **Dependence on Index Performance:** Returns vary depending on market conditions.



Problem Statement

Credit unions face challenges when relying on COLI for long-term investments.

Low Return Rates

- COLI's returns, currently projected at 2.8%, are modest compared to emerging options.
- COLI's growth fails to keep pace with inflation or competing products.

High Holding Periods:

- Policies must be held for decades to realize benefits.
- Policies require 30-50 years to access death benefits fully.

Cost of Insurance: These reduce ROI over time, limiting overall gains.

In contrast, Fixed Index Annuities offer a compelling alternative by providing principal protection, zero downside risk, and an average annualized return of up to 10.6% depending on the market scenario. FIAs offer higher returns, shorter terms, and lower cost structures while staying compliant with NCUA §701.19.

Solution Overview

Transitioning from COLI to Fixed Index Annuities with reputable A or A+ rated insurance providers enables credit unions to achieve the following:

Unlock Growth

- Index-linked performance with no downside risk.
- Realize immediate deposit bonuses, such as \$2M, to boost annual income.

Realize Immediate Deposit Bonuses

- Achieve greater returns. For example, worst-case FIA scenarios generate over \$50M versus \$13M from COLI over 10 years.

Shorter Commitments

- 10-year FIA contracts versus 30-50 years for COLI high-cost insurance policies.

Regulatory Alignment

- Both options meet the NCUA § 701.19 guideline with FIAs providing better financial flexibility.

By transitioning from COLI to Fixed Index Annuities, credit unions can:

- **Enhance Returns:** Realize significantly higher income over shorter periods.
- **Reduce Costs:** Eliminate insurance-related charges that erode returns.
- **Stay Compliant:** Ensure adherence to NCUA § 701.19 guidelines while maximizing investment efficiency.

Conclusion

The comparison clearly establishes Fixed Index Annuities as a superior investment vehicle for credit unions seeking higher returns without compromising principal protection. CU Benefit can assist credit unions in evaluating their current portfolios and implementing this transition seamlessly, ensuring compliance with NCUA § 701.19 while reducing costs and improving returns.

CASE STUDY

Credit Union Investments Transitioning From COLI to Fix Index Annuities



Background

A credit union with sizeable assets worth \$1.43B sought to elevate the performance of its investment portfolio, all while ensuring unwavering compliance with NCUA Regulation §701.19. With a substantial \$39.2M invested in Corporate-Owned Life Insurance (COLI) across multiple providers, the client organization had been settling for modest annual returns of a mere 2.8%, amounting to a projected income of \$12.8M over the course of a decade. Recognizing the pressing need for superior growth opportunities, the forward-thinking credit union meticulously evaluated Fixed Index Annuities (FIAs) as a promising alternative poised to outshine their current financial instruments.

Client Profile

- \$1.43B asset size credit union
- HQ in Houston, TX
- 268 Full Time Employees

Current Pain Points

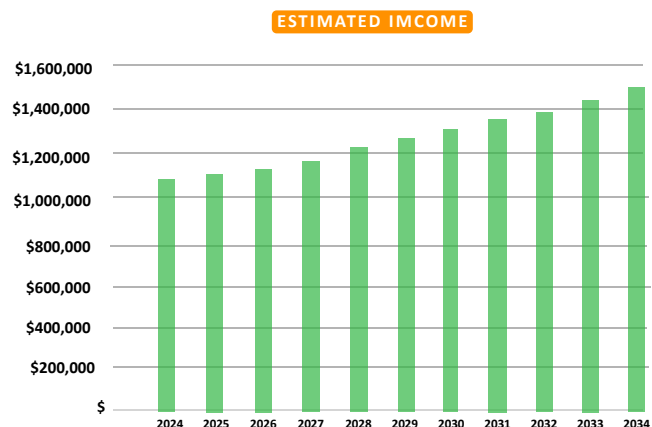
- A COLI executive benefit plan only earning 2.8% after investment agency fees.
- Interest rate based on insurer's discretion.
- The credit union may have to hold the policy for 30-50 years to receive the death benefit.

The Challenges Credit Unions Face When Relying on COLI for Long-term Investments:

- COLI returns, currently projected at 2.8%, are modest compared to emerging options.
- COLI growth fails to keep pace with inflation or competing products.
- Policies must be held for decades to realize benefits.
- Policies require 30-50 years to access death benefits fully.
- Cost of Insurance reduce ROI over time, limiting overall gains.

CURRENT COLI INVESTMENTS

- **Provider A:** \$19,628,983
- **Provider B:** \$19,613,793
- **2023 Income:** \$1,049,152
- **2024 Income as of 9/30:** \$824,339
- **Interest Rate:** 2.8%
- **Income Next 10 Years:** \$12,834,296



Credit Union Key Objectives:

- **Maximizing Investment Returns:** Achieving higher growth rates than the current COLI investments.
- **Preserving Capital:** Ensuring principal protection while mitigating risk exposure.
- **Enhancing Short-Term Income:** Leveraging deposit bonuses to increase income for upcoming fiscal years.
- **Maintaining Regulatory Compliance:** Ensuring adherence to NCUA Regulation §701.19 for employee benefit funding mechanisms.

Solution

The transition plan involved reallocating the \$39.2M COLI investment into FIAs with three highly rated providers—known for their robust historical performance and competitive deposit bonuses.

- Rollover COLI to Fixed Index Annuity with A or A+ rated insurance companies
- Interest rate based upon investment performance
- No investment agency fees

The 10-year FIA contracts were tailored to the credit union's needs, offering higher returns and shorter holding periods compared to COLI.

Anticipated Results

- Credit Union receives a \$1.9M deposit bonus from Fixed Index Annuity company that can count as revenue
- Worst 10-year FIA performance to deliver in \$51.5M of income vs \$12.8M via COLI
- Best 10-year FIA performance to deliver in \$104.5M of income vs. \$12.8M via COLI

Results

In contrast, Fixed Index Annuities offer a compelling alternative providing principal protection, zero downside risk, and an average annualized return of up to 10.6% depending on the market scenario. FIAs offer higher returns, shorter terms, and lower cost structures while staying compliant with NCUA §701.19.

The transition yielded significant improvements in both projected income and return rates:

- **Worst-Case Scenario:** Total income of \$51.5M, outperforming COLI by nearly four times.
- **Best-Case Scenario:** Total income of \$104.5M, a return nearly eight times higher than COLI projections.
- **10-Year Rate of Return:**
 - **Provider A:** 7.41% (worst) to 13.50% (best)
 - **Provider B:** 8.99% (worst) to 14.60% (best)
 - **Provider C:** 8.47% (worst) to 10.60% (best)

PROJECTED RATE OF RETURN

Worst 10-year Performance			
Year	Provider A	Provider B	Provider C
	\$15,000,000	\$15,000,000	\$9,042,663
1	13.00%	0.00%	7.00%
2	6.49%	18.84%	0.00%
3	0.00%	0.00%	4.29%
4	23.54%	33.74%	29.24%
5	0.00%	0.00%	0.00%
6	11.90%	25.73%	14.07%
7	0.00%	0.00%	7.91%
8	38.90%	18.41%	13.68%
9	0.00%	0.00%	0.00%
10	0.00%	0.00%	11.72%

Worst 10-year Performance			
Year	Provider A	Provider B	Provider C
	\$15,000,000	\$15,000,000	\$9,042,663
1	13.00%	0.00%	7.68%
2	36.48%	53.39%	26.02%
3	0.00%	0.00%	7.00%
4	11.59%	27.52%	0.00%
5	0.00%	0.00%	4.29%
6	36.67%	18.84%	29.24%
0	0.00%	0.00%	0.00%
8	22.20%	33.71%	14.07%
9	0.00%	0.00%	7.91%
10	39.51%	25.73%	13.68%

PROJECTED INCOME

Worst 10-year Performance			
Year	Provider A	Provider B	Provider C
1	\$1,950,000	\$0	\$6,329,896
2	\$1,110,055	\$2,826,000	\$0
3	\$0	-	\$415,805
4	\$4,248,983	\$6,009,145	\$2,950,528
5	\$0	-	\$0
6	\$2,653,586	\$6,132,783	\$1,834,904
7	\$0	-	\$1,176,704
8	\$9,706,571	\$5,517,095	\$21,960,311
9	\$0	-	\$0
10	\$0	-	\$2,138,770
Total Income	\$19,669,195	\$20,485,023	\$36,806,918
	8.7% IRR	\$51,489,023	

Worst 10-year Performance			
Year	Provider A	Provider B	Provider C
1	\$1,950,000	\$0	\$694,745
2	\$6,183,630	\$8,008,500	\$2,533,601
3	\$0	-	\$858,951
4	\$2,681,156	\$6,331,939	\$0
5	\$0	-	\$563,263
6	\$9,466,183	\$5,527,793	\$4,003,817
7	\$0	-	\$0
8	\$7,832,315	\$11,754,063	\$2,489,934
9	\$0	-	\$1,596,768
10	\$170,300,952	\$11,995,903	\$2,979,978
Total Income	\$198,414,236	\$43,618,198	\$15,721,057
	10.35% IRR	\$104,495,898	

Solution Overview

Transitioning from COLI to Fixed Index Annuities with reputable A or A+ rated insurance providers enables credit unions to achieve the following:

- **Unlock Growth:** Index-linked performance with no downside risk.
- **Realize Immediate Deposit Bonuses:** Realize immediate deposit bonuses, such as \$2 million, to boost annual income.
- **Greater Returns:** Achieve greater returns. For example, worst-case FIA scenarios generate over \$50 million versus \$13 million from COLI over 10 years.
- **Shorter Commitments:** 10-year FIA contracts versus 30-50 years for COLI high-cost insurance policies.
- **Regulatory Alignment:** Both options meet NCUA § 701.19 guideline with FIAs providing better financial flexibility.

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Conclusion

Fixed Index Annuities offer a compelling combination of enhanced yields and principal protection that savvy financial institutions cannot afford to overlook. In today's competitive landscape, a thorough evaluation of your investment portfolio is not just good practice—it is essential for trimming unnecessary costs and maximizing returns that flow directly to your bottom line. By strategically incorporating these powerful financial instruments, your credit union can transform its investment approach and improve net income such that employee and executive benefit costs are covered.

Next Steps

Allow us to demonstrate how partnering with CU Benefit can significantly enhance your financial perspective and contribute to a more secure future for both your credit union and its employees.

- ✓ **Schedule a call with a CU Benefit Expert to discover more and obtain your complimentary CUB Evaluation.**

BOOK NOW ➔



About CUB

CUB, in partnership with Ten Talents Wealth Management, has been serving Credit Unions since 2013 with their retirement plans, executive benefits, and total benefit prefunding. In 2019, we created Total Benefit Prefunding, a program that allows credit unions to build an endowment-like strategy to help stem the tides of rising employee benefit costs. For more information, please visit www.totalbenefitprefunding.com.





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