BONDED LIFE CAPITAL

A High Value Life Insurance Program

A new approach. Financial institutions have for years provided a strategy called "premium financing". A new group of financial institutions like Wells Fargo, Citibank and many others are now providing a new approach, Bonded Life Capital. This program allows clients to purchase life insurance fully funded by participating banks through a bond procedure. Simply put, clients can benefit from the following concepts that are all financed and paid for through the special bond premium financing structure typically with no out of pocket cost:

- Estate and Charitable planning
- Corporate Owned Life Insurance programs (COLI)
- Raise capital—Hospitals, Universities/Colleges can leverage endowment/foundation funds to raise needed capital by sharing the beneficial interest in its employees insurance plans

"There is no free lunch", as the saying goes. Clients are asked to post a Letter of Credit (LOC) or cash collateral, which is the short term difference between what the bank is funding versus the growth of the insurance policy values in the early years. This Letter of Credit/cash collateral is minimal and is usually released back to client around the sixth to twelfth year depending on the client's age. The banks recover all of the funding amount that they paid over the years from the cash surrender value of the policy down the road usually 20 to 30 years or from death proceeds—which ever happens first.

HERE ARE THE STEPS:

1. The client submits a credit application and a personal financial statement to the banking team. This allows the bank to review the financial strength of the client and to evaluate how much funding can be provided to the client's insurance program.

2. Credit Application is approved by banking team—usually in five business days.

3. Once funding is pre-approved, the client will submit a life insurance application—the insurance company will order from client personal doctor medical records for review and order a basic medical exam, which will be scheduled at a location of choice by the client.

The exam will include the client giving blood and urine samples. This will be all that is asked of the client from a medical standpoint.

If the case is a Corporate Owned Life Insurance (COLI) plan, there will be no medical exam needed. COLI programs are based on a guaranteed issue basis, which means that all employees under the COLI program qualify for coverage regardless of medical health.

4. The client advisory team will work with the legal team to set up an Insurance Trust which will be the owner and beneficiary of the insurance policy. This keeps the insurance values protected from potential lawsuits, creditors and federal estate taxes.
The bank will be lending to the Trust and not to the individual—this is a very important part of the structure—by having the trust enter into this agreement with the bank, the client individually is not borrowing the funds. There is no personal guarantee by the client with this structure. The client is not liable to pay back the premium financed amount provided by the bank. The client's only risk in the transaction is the short term collateral posted by the client.

5. At this point in the process, the client will coordinate with the banking team to secure a "letter of Credit" against client assets or post liquid collateral. Basically, the bank is on the hook for the funding until the policy values increase. This takes about 6 to 12 years depending on the age of the client and the performance of the insurance policy. Once there is enough cash value in the insurance policy, the bank releases the Letter of Credit/cash collateral back to the client.

SPECIAL NOTE: WHAT IS A "LETTER OF CREDIT" AND ITS PURPOSE?

When a client needs collateral for a loan, like the bond premium financing concept outlined above, banks will evaluate the financial strength of a client and provide a Letter of Credit in place of the client actually putting up cash or other liquid assets. The Letter of Credit is a promise by the bank that it is backing the client's collateral need because it knows the client has the financial strength to pay off the Letter of Credit if needed. This allows the client to keep their assets in place without any disruption to their investment accounts or other financial planning programs they have in place. The majority of clients provide cash collateral in these programs since there is an annual fee for a Letter of Credit.

6. The money for the premium finance strategy is raised in the bond market by our bond team (www.frazerlanier.com) to be used to fund the client's insurance program. This takes about 30 days. All monies needed for the financing structure are raised and placed in the corresponding bank in a lump sum. The bank will set up a client trust brokerage account and wire monies into this trust for all insurance premium payments to be made on behalf of the client over a ten year period. All aspects of this structure are fully managed by the banking team with frequent reporting to the client.

7. Once the client posts short term collateral and the insurance company has approved the policy, the bank will wire the first payment for the insurance program to the insurance

company. Each yearly anniversary, the bank will automatically wire the needed payment to the insurance company from the client Trust account.

8. Now that the program is active, the values in the policy will grow substantially over time. The bank will allow the client to borrow funds from the program after year ten. Its takes time for the cash values in the insurance policy to grow, and remember, the bank is funding the full cost of the program, so it's really the bank's money in the early years. Once the cash values grow, the bank will retire the note usually around twenty years, at which time all of the cash value belongs to the client/trust.

Bottom-line:

1. You received substantial life insurance with no premium or interest cost to you
2. No personal guarantee—no liability other than the short term collateral you posted
3. Individuals can now cover their estate planning needs without the burden of expensive insurance premium costs
4. Universities/Colleges and hospitals can now leverage endowment/foundation assets to meet the collateral needs of the program, while receiving tens or even hundreds of millions of additional capital from sharing in beneficial interest of insurance policies

Additional important points regarding the premium financing structure:

Utilizing the bond market to raise the money for a premium financing structure has many advantages over a traditional premium financing program:

1. The bond market offers extremely low interest rates to finance the insurance. The current interest rate in the 7 day floating market is approximately 1.25%, which covers floating rate and banking fees and has been in this range for the last ten years. Other premium financing programs use a LIBOR spread loan that is typically at 2.75%-3.25% interest cost on the loan.

2. This unique structure provides an interest rate hedge which can cap the interest rate at 4% fixed any time in the program. The program starts at a variable rate to take advantage of the low interest environment at this time, but can switch to a fixed rate at any point in the program. Once the rate is moved to a fixed rate, we cannot go back to a variable rate.

3. Due to the bond market the loan term is twenty years, but can go longer, based on the growth of cash surrender values of the insurance policy. The client is approved for the loan and will never have to reapply. Traditional LIBOR spread premium financing loans typically have term of 1 to 5 years based on the banking loan provisions making the client go through approval process each year.

4. All the money needed for the 10 year premium finance loan is raised at the beginning of the process and directed to the clients trust.

5. There are two interest rate arbitrages created with this structure:

A) By raising all the money needed for the premium financing loan in a lump sum, a side fund is created which earns interest that is credited to the trust. The interest earned offsets the interest due on the loan in the earlier years. This allows the cash surrender value to grow rapidly in the early years. The side fund is a decreasing value as it is used to pay interest and premiums until exhausted over the first ten years of the program, at which time the interest payments will start being deducted from cash surrender values.

B). The second arbitrage created by the structure is the premium financing loan interest rate versus the crediting rate of the insurance policy. The type of insurance used for the structure is an Indexed Universal Life policy (whole life or universal life can be used as well). The cash value's crediting interest rate is based on S&P 500, which allows for market gains when the S&P 500 is positive capped up to 13% annually, but never allows for market loss. PLEASE SEE ATTACHED S&P 75 YEAR HISTORICAL RETURNS TO ILLUSTRATE THE RATIONALE OF SHOWING "HIGHER" RETURNS IN THE INDEXED UL INSURANCE POLICY. With this historical return, the policy returns should exceed the loan interest rate even at the maximum fixed loan rate of 4%.

6. The client is required to post a Letter of Credit or liquid collateral to the corresponding bank. This Letter of Credit/cash collateral is based on the differential of the premiums paid versus the growth of cash surrender value of the insurance policy. As the cash value builds the letter of credit/collateral is released back to the client. This is the client's only obligation to the structure and the only asset at risk.

In summary: the only risk to the client is the collateral posted by the client. When evaluating the merits/risk of this financed program, one needs to look at the relationship between costs of interest on loan versus insurance cash surrender growth. If one believes that the index universal life insurance will continue to perform at historical returns, the structure will provide as outlined above.

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