FROM THE AUTHOR OF
THE DEFINITIVE BOOK ON PREMIUM FINANCING

PREMIUM FINANCED LIFE INSURANCE

THE KEY TO EFFECTIVE ESTATE TAX PLANNING

DARREN SUGIYAMA

www.DarrenSugiyama.com

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Disclaimer:

The author of this book is not a CPA or tax attorney. Nothing in this book shall be misconstrued as tax advice or legal advice. For any tax-related or legal-related questions or concerns, it is highly recommended that you consult your CPA, tax professional, or tax attorney regarding these specific topics.

Chapter 1
The History Of The Author

If you are reading this book, my guess is that you are either a financial professional that is considering introducing the concept of *Premium Financed Life Insurance* to your clients, or you are an individual who is considering using *Premium Financed Life Insurance* as a wealth preservation strategy for yourself and your family.

My name is Darren Sugiyama and I am a *Premium Financing Intermediary*, which means I specialize in working with financial professionals all over the country that rely on me to do one thing and one thing only: To design the most mathematically prudent method of financing their clients' life insurance premiums.

When an individual's net worth reaches a certain level, it often times makes sense for them to purchase their life insurance policy using a lender's capital instead of their own capital.

Although premium financing may seem like a foreign concept, you have probably already purchased some of your other valuable assets using *leverage*. Perhaps you purchased your home using a mortgage loan, or financed your college tuition with student loans, or expanded your business with a line of credit. When it comes to purchasing life insurance, the concept of using *leverage* is not so different.

So why should you listen to me?

A wise man once said, "If you don't know the history of the author, then you don't know what you're reading."

That being said, I will begin this book by sharing with you my background, how I got into this highly specialized line of work, and the current scope of my business.

When most people hear that I finance $50 million to $100 million life insurance policies for uber-wealthy clients, they often think I grew up around extremely wealthy people. Perhaps they think I spend my time at private country clubs sipping on overpriced

cocktails holding my martini glass with my little pinky finger up in the air, hobnobbing with the likes of *Thurston Howell, III*.

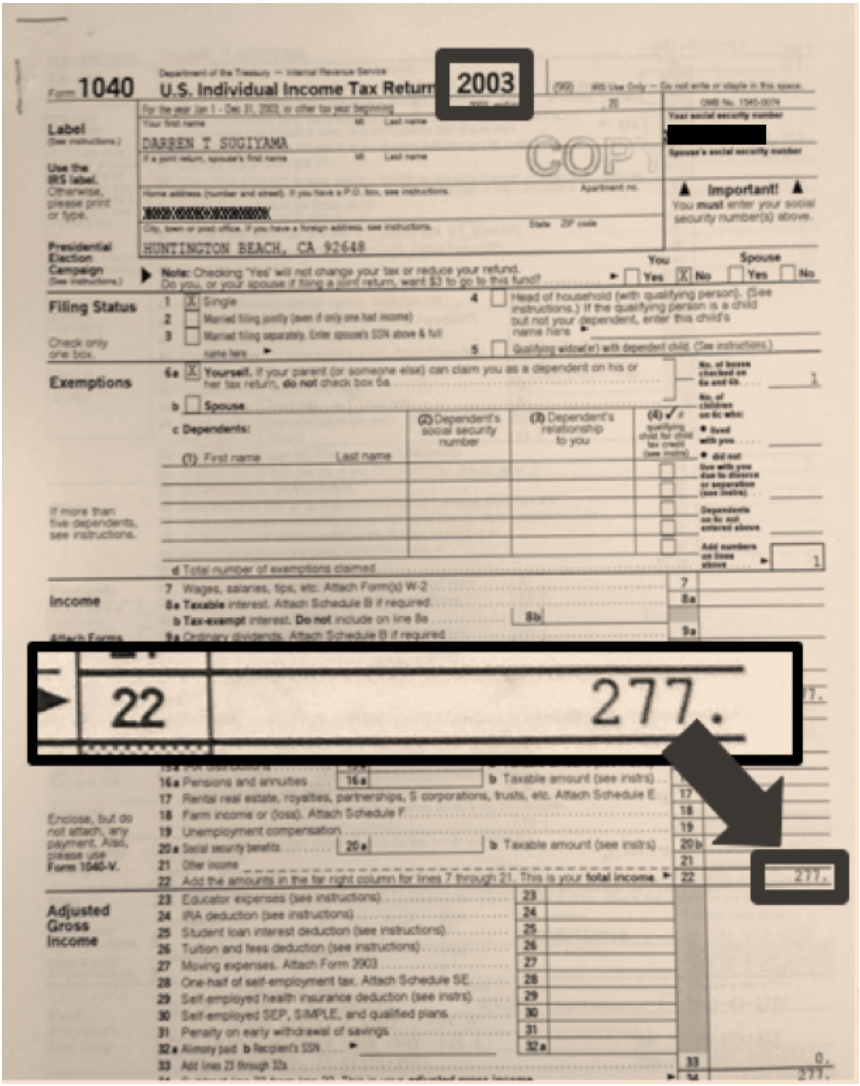
Nothing could be further from the truth. I started my career in the insurance industry in 2003 after I decided to end my career as high school teacher in Hawaii. I moved back to Long Beach, California where I was born and raised and entered the industry at age thirty-one. I got my start in the employee benefits arena, selling health insurance programs to small companies, and let me tell you, it was not as easy as I thought it was going to be.

The *California State Department of Insurance* issued my insurance license on January 3, 2003, and to say that 2003 was a rough year for me would be the understatement of a lifetime. I first solicited people I knew – my friends and family – and tried to get them to buy insurance from me. To my chagrin, most of them declined my offers. So I started cold calling businesses, and as you can probably imagine, my results were even more dismal. Nobody wanted to talk to me, and perhaps I couldn't blame them, for I was a brand new agent with no experience.

My 2003 personal tax return showed a total income of $277 for the entire year. I actually have a copy of it framed on the wall of my office. I think it's important for all of us to remember where we came from. It keeps us humble and grounded, regardless of how much success we may have achieved in our lives. Looking at my 2003 tax return on my wall every day is a great reminder that I didn't always work with the caliber of clients and advisors that I work with today.

After spending my first year in the insurance industry trying to emulate what other successful insurance agents have done (and failing miserably at it), I decided to do something extremely unconventional.

I took a step back – taking an outsider's view of the industry – and started designing an entirely different client proposition. I took a strategy that large corporations were using in their employee benefit packages, scaled it down, and re-engineered it into a new platform for small businesses that didn't have access to big company benefits.


Form 1040 U.S. Individual Income Tax Return 2003

Label (See instructions.) Use the IRS label. Otherwise, please print or type.

DARREN T SUGIYAMA

[redacted]

HUNTINGTON BEACH, CA 92648

Presidential Election Campaign (See instructions.)

Filing Status

Exemptions

Income

22 277.

Adjusted Gross Income

Darren Sugiyama's 2003 Personal Tax Return showing an income of $277 for the year.

Everyone in the insurance industry told me that my vision of reinventing the wheel was a bad idea, but after two years of recalibrating my platform based on what I *thought* small company employee benefits *could* be, my unconventional methodology began to get traction. I took my idea to two different *TPAs (Third-Party Administrators)* and built a white-labeled semi-self-funded

strategy using supplemental insurance products from specialty carriers in conjunction with the major medical carriers.

Five years into my insurance career, I had built one of the fastest growing employee benefits firms in the industry. My firm, *Apex Outsourcing* was the #1 producing firm in the country for *Kaiser Permanente*, *HealthNet* and *Colonial Life* concurrently; the #2 firm in the State of California for *Aetna*; top 30 in California for *Blue Cross*; and by my seventh year in the business, my firm had topped over $37 million in annual sales.

I actually wrote a book about it called ***How I Built A $37 Million Insurance Agency In Less Than 7 Years***, and it has become one of the insurance industry's most notorious books ever published. In fact, if you search the term *Insurance Agency* on *Amazon*, the first edition of my book pops up on the first page and has more reviews than any other book in its category. I have since written a *Second Edition* version of this book as well.

When I originally wrote that book, I was in my mid 30's at the time, and I met a so-called financial advisor that implemented a very elaborate life insurance-based financial strategy within my company. To make a very long story short, his recommendations ended up losing me $930,000 in a very short period of time.

This experience absolutely enraged me, but as angry as I was, I was far more embarrassed. I thought I was a reasonably smart person, but that financial loss I took made me feel naïve. It made me feel violated. It made me feel stupid. I spent the next year obsessively studying every life insurance product in the market, learning about how each product chassis was built, how the crediting methods work, how the underlying investments work, and how the policy charges work. I took those lemons I was dealt and decided to make a lemonade factory.

I ended up writing another book called ***Ouch: How My Financial Advisor Lost Me $930,000 In Three Years***. The concepts I wrote about in that book served as the foundation of building my second insurance agency – *DaVinci Financial* – this time specializing in life insurance for business owners. We used that book to teach our clients how to avoid what happened to me.

I built *DaVinci* into a sizable firm in Orange County, California that at one point housed over 40 life insurance agents and financial advisors, plus I also built additional satellite offices in Las Vegas, Nevada; Hartford, Connecticut; Seattle, Washington; Dallas, Texas; and Manhattan, New York. Eventually, we became responsible for over 25% of all the life insurance policies sold in Orange County, California for *Pacific Life* in 2017, and over 38% for Penn Mutual in 2019.

But all the while, I was also in the process of building *Lionsmark Capital*, my premium financing intermediary firm. I started *Lionsmark* in 2016, and we quickly became known as the most mathematically-sound premium financing intermediary in the insurance industry. At that time, I had a business partner, and though he eventually decided to move in a different direction with his life, we still remain good friends to this day.

Entering the niche space of premium financing – especially as an intermediary – was a counter-intuitive thing for me to do by most people's standards. I already had two successful multi-agent insurance agencies – one employee benefits firm and one life insurance firm – and so doubling down on building a premium financing intermediary firm was a big decision for me. But I identified two glaring deficiencies in the premium financing industry – two vitally important things that every client and advisor was silently begging for: Transparency and client education.

I felt it was time for me to innovate again – to reinvent another *new wheel*. Most people thought I was crazy for making this shift, but similar to my two previous insurance ventures, I was confident that my unorthodox approach and fresh perspective could disrupt the entire industry. I didn't want to merely build a *better* version of a premium financing intermediary firm. I wanted to create an entirely different client experience, as well as give advisors a completely new intermediary experience. As I said, I wanted to reinvent a *new wheel*.

Back in 2014, I had started building an algorithmically-based software solution that could backtest and stress-test *Indexed Universal Life (IUL)* insurance policies' crediting methods. I started out by using these backtesting models in *DaVinci*, but I

wanted to be able to expand my software solution into modeling premium financing arrangements, especially during times of volatility. No one in the life insurance industry was doing anything like this, and even to this day, no one has been able to replicate it.

I went to all the *advanced markets* attorneys at the major insurance carriers and explained what I was doing because I wanted to make sure I wasn't violating any compliance regulations. I emphatically clarified that my models were not recreations of *insurance policy illustrations*, rather they were hypothetical synthetic models that would help educate clients on how different elements of these products actually work; things like floors, caps, charges, and multiplier bonuses.

The spirit of my work has always been rooted in *client education* – probably a subconscious effort to continue my teaching career in a reimagined way.

When I first started implementing these mathematically-based models in premium financing back in 2017, *Lionsmark* was primarily a direct-to-consumer business model whose clientele was mostly small business owners. I felt that this was a great way for us to launch our company because we could control 100% of the point-of-sale process, refining our reimagined way of positioning premium financing. But once word started getting out that we had a superior technology-based backtesting and stress-testing method – as well as a proprietary way to mitigate client risk – other advisors began to inquire. My *ex-competitors* became my *referral sources,* and I am now one of their most trusted resources when it comes to interfacing with their most valuable clients.

By 2018, my reputation in the industry began to evolve from being *a guy that builds large insurance agencies*, to *THE guy that does premium financing the right way*.

I started receiving requests to speak at industry events as a premium financing expert. The first major speaking engagement happened on November 7, 2018 where I was asked to speak at *Simplicity Life's Premium Financing Symposium* in Houston, Texas.

I still remember hearing the *Senior Vice-President of Premium Financing* from a large bank explain that they only lend annual premiums of $1,000,000 or greater. Again, that's $1,000,000 in ANNUAL premiums, not the *total loan amount*.

I remember thinking to myself, "Whoa, those are some big policies." Back then, our average-sized policies were about a third of that. Fast forward three years later to 2021, and a $1,000,000 annual premium is now our *new normal*. Today, we do a sizable amount of premium financed cases using that bank as one of several different lenders we place our loans with.

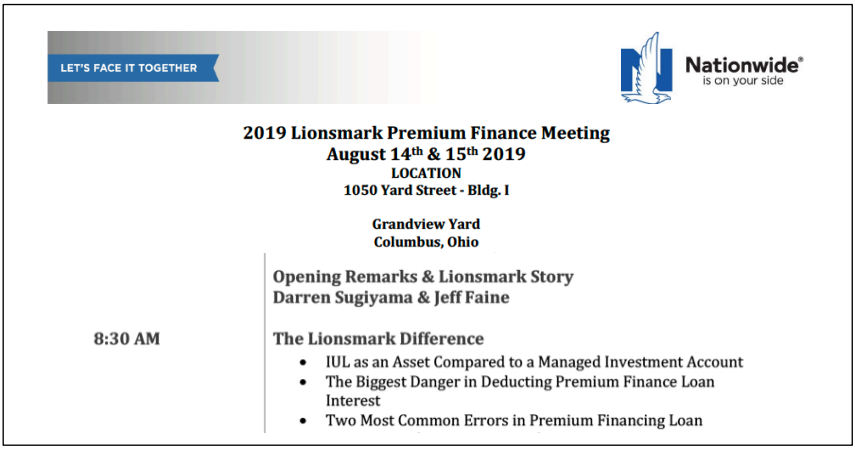
By 2019, things really started to ramp up. On March 19, 2019, I spoke from stage at *FFR's Spring Symposium* at *The Montage Resort* in Laguna Beach, California on how we approach premium financing in a completely different and reimagined way.

Darren Sugiyama speaking at FFR's 2019 Spring Symposium.

That *FFR* speaking engagement was a major pivotal moment for me because of the exposure it gave me to a larger audience: Advisors, Carrier Executives, Wholesalers and Distribution Partners. It really cemented my reputation as being an expert in the premium financing arena. It sent a message to the entire industry that I was now a force to be reckoned with.

Later that month, I was invited to speak at *Penn Mutual's Advance Planning Council* in Irvine, California as the subject expert on premium financing, and the very next month in April, I spoke at another event at their regional office in Chicago, Illinois.

Later that year in August 2019, *Nationwide* hosted a premium financing symposium at their corporate office in Columbus, Ohio, and *Lionsmark Capital* was the only *non-Nationwide* presenter at their entire symposium.



In the midst of the COVID-19 pandemic, *Pacific Life* held their *2020 National Symposium* virtually, and I was a featured speaker as the subject expert on *IUL* multipliers.

I was chosen to speak about the charges and crediting methodologies used in their *PDX2* and *PIA6 IULs* alongside Stephan Mitchell – *Assistant Vice President of Product Marketing at Pacific Life* – who is someone that I have always had an immense amount of respect for as an *IUL* expert and product technician.

I believe *Pacific Life's* decision to select me as a speaker for this nationally broadcasted event was largely due to the sophistication of my backtesting modeling capabilities.

Darren Sugiyama was a featured speaker at Pacific Life's 2020 National Symposium.

I have been the featured speaker on premium financing at seminar and webinar events sponsored by other carriers including *John Hancock* and *Ohio National*, as well as other BGAs and producer groups like *AEG*, *BGA Insurance*, *CPS*, *The Producers Group*, and *Pelaton* (an IMO that supports over 20 different BGAs).

Lionsmark Capital is currently one of only eight nationally approved premium financing intermediaries endorsed by *National Life Group*, and one of only seven approved premium financing intermediaries endorsed by *Penn Mutual*.

Now, I know the last few pages of this book probably sounded like shameless self-promotion and braggadocio (and perhaps it was), however I felt it was important to establish my background and credibility on this topic. As I said at the beginning of this book, a wise man once said, "If you don't know the history of the author, then you don't know what you're reading."

As my reputation in the life insurance industry grew, financial professionals began to receive strong endorsements from insurance carriers, investment broker-dealers, IMOs, and BGAs that *Lionsmark Capital* should be their *Hired Gun Of Choice* when it came to premium financing. This level of endorsement gave me the credibility I needed to grow my firm exponentially.

The financial professionals that we do business with today come from a variety of different disciplines, including financial advisors, CPAs, estate planning attorneys, family offices, and of course, life insurance agents. These professionals rely on my firm to not only secure the lender capital for their high-end clients, but also to articulate how our algorithmically-designed platforms mitigate risk in a way that no other premium financing intermediary can.

In 2019, I wrote a book called *The Definitive Book On Premium Financing* that quickly became, well, the definitive book on premium financing. I knew that book would have a short shelf life because the life insurance industry is an ever-evolving landscape.

Over time, life insurance products change, tax laws change, the cost of lender capital changes, plus the regulatory agencies constantly change their stance on what they deem as being *reasonable and allowable depictions of potential outcomes* in life insurance illustrations.

With so many changes occurring in the industry right now, financial advisors and life insurance agents must now be fluent in:

1. How AG-49A completely changed allowable index crediting assumptions depicted in carrier illustrations, along with how participating loans are depicted.

2. How the updated 7702 guidelines have completely changed how *IULs* can be designed and funded, drastically improving cash value accumulation efficiencies.

3. How premium financing borrowing interest rates are at an all-time low, while the S&P 500 returns continue their bull run.

4. How new estate tax initiatives have radically increased the population looking to increase their life insurance coverage.

As these changes began to create a radical shift in the areas of estate planning and life insurance, I felt the need to write yet another book – this book – to address these changes and explain how *Premium Financed Life Insurance* can be integrated into an overall estate plan.

This is the eighth book I have authored in my career, and several of my books are currently being distributed in multiple countries including Australia, Brasil, Canada, Croatia, Czechoslovakia, Denmark, India, Italy, Japan, Mexico, New Zealand, Norway, Singapore, Sweden, the United Kingdom, and of course, the United States of America.

In this book, I will discuss *Premium Financed Life Insurance* both at the conceptual level AND at the granular level and explain how it can be the key to effective estate tax planning.

Chapter 2
The Tax-Free Benefits Of Life Insurance

The three most common uses of life insurance in estate planning are to:

1. Accumulate a low-risk tax-fee asset.
2. Generate a tax-free supplemental retirement income.
3. Pay the estate taxes due at death with tax-free dollars.

The tax-advantaged treatment of the cash value accumulation inside a life insurance policy is very appealing for those who want a conservative alternative to a *taxable stocks and bonds portfolio*. This benefit can also be enjoyed when taking retirement income drawdowns from the policy because if done properly, the income stream is tax-free as well. I have devoted an entire chapter in this book to explaining the different ways to take tax-free income drawdowns from a life insurance policy (Chapter 5).

In addition, when a wealthy individual passes away, their assets can be passed on to their surviving spouse without tax consequence, however once their surviving spouse passes away and their wealth is transferred to the next generation, their heirs can incur a substantial tax liability in the form of *estate taxes*.

The IRS allows a certain amount of their net worth to be transferred to the next generation tax-free up until a certain dollar amount known as the *Estate Tax Exemption Limit*.

In 2017, the *Trump Tax Act* was enacted, giving individuals an $11,180,000 estate tax exemption starting in 2018 (up from $5,490,000 in 2017). This exemption increased to $11,700,000 in 2021.

Upon death, they could also pass their exemption on to their surviving spouse. This meant that if a married person passed away in 2021, their $11,700,000 exemption could be passed to their surviving spouse, giving their estate a $23,400,000 total *Estate Tax Exemption* ($11,700,000 x 2 = $23,400,000).

However this exemption was always scheduled to revert back to the $5,000,000 range per individual on January 1, 2026 unless Congress decided to take early action.

What many feared regarding the Biden Administration's tax agenda came to pass on September 13, 2021 when the *House Ways and Means Committee* released a tax change proposal in favor of reducing the estate tax exemption limit back down to the $5,000,000 range per individual as of January 1, 2022.

However, one thing that has remained constant is the favorable tax treatment of life insurance, which is why it continues to be an incredibly valuable estate planning tool.

Due to Section 101a of the IRS tax code, the death benefit of a life insurance policy is tax-free, giving policy owners a huge advantage when it comes to using life insurance in estate planning. I will discuss comparing life insurance strategies to non-insurance-based alternatives later in this book (Chapter 9), however it is important to understand that when a person dies, any excess net worth above the estate tax exemption is currently taxed at a rate of 40.00% when it is transferred to the next generation.

To clarify how this works, when one spouse passes away, the surviving spouse does not incur any estate tax liability. However when the second spouse dies and the estate is transferred to the next generation, estate taxes are due, payable by this next inheriting generation.

As an example, if the surviving spouse is worth $100,000,000 above the exemption limit, the inheriting generation will owe $40,000,000 in estate taxes (40.00% of the $100,000,000). This inheriting generation is only given nine months from the time of the surviving spouse's death to file and pay the estate taxes due, which is not much lead time by any means.

Even if the estate value is comprised of illiquid assets (e.g., real estate, a company, jewelry, art, automobile collection, etc.), the estate tax is still due on the value of these assets nonetheless, which often results in a necessary fire sale of such assets to come up with the funds required to pay the estate taxes. This can be both financially draining and emotionally taxing for all parties involved.

Life insurance is an extremely efficient tool in planning for the estate tax liability that the next generation will incur because it removes the need to liquidate the estate's illiquid assets within this nine-month period. If the policy is owned by an *Irrevocable Life Insurance Trust (ILIT)* – which is outside the estate – the death benefit will pay out tax-free to the *ILIT* and not subject to estate taxes, and the *ILIT* can then pay the taxes as soon as the death benefit is issued. This is a much easier process to manage than a fire sale to desperately come up with the cash needed to pay the estate taxes.

There are many benefits of using life insurance as both an estate tax planning tool, as well as a tax-advantaged asset for wealth accumulation and supplemental retirement income. But this is an industry wherein the explanations of how these insurance-based instruments actually work is *opaque* at best. One of the biggest criticisms of the life insurance industry is that many of the products lack transparency, and quite frankly, I would have to agree with that accusation… sort of.

The reality is that these life insurance products do not lack transparency in their *construction*. The lack of transparency is in how their construction is *communicated* to the client – both from the carriers and the agents. It is a problem I have experienced as a life insurance client back before I got into this line of work, and it is a problem that still exists today. To make things even worse, when the concept of premium financing is introduced into an already-opaque equation, the complexities, perceived risk, confusion, and skepticism grow exponentially.

That being said, I have the solution to these seemingly daunting issues and accusations which I will articulate in this book.

The key is to understand how different types of life insurance policies are built and how they work mechanically. This is the foundation that I have built my practice on. Everything I do is rooted in education and granular understanding.

In this book, I will open up the *black box* for you so you can see what's actually inside the box, which will change your perspective from looking through opaque lenses to looking through a high-powered microscope. The strong stance I have taken on

opening up the *black box* has at times felt like I was opening *Pandora's Box*, but as I stated earlier, I am an industry disruptor – a beacon of transparency – and my goal is to teach you the truth about these products, where the risks are, how to mitigate these risks, and to show you the best way to utilize these products in the most effective way possible.

If you are not familiar with the details of the Greek mythological story of *Pandora's Box*, indulge me for just a moment to share with you how analogous this story is to *Premium Financed Life Insurance*.

In Greek mythology, Pandora was the first woman on Earth. She was given a box that the gods told her contained special gifts, but she was also told that she was not allowed to open it and see what was inside. Sounds like life insurance already, doesn't it?

Eventually, Pandora could not contain her curiosity and she opened the box. When she did, all the illnesses and hardships that the gods had hidden in the box started coming out. She tried to quickly close the box once she saw the evil coming out of it, but in doing so, *hope* got trapped inside the box.

Many people feel the same way about certain life insurance products. They are told that the *black box* contains all kinds of special gifts (e.g., tax-free benefits, 0% floor, etc.), but they are told not to open the box and dissect its components at the granular level. In fact, I've even heard advisors say, "My clients don't want to know all the details."

Personally, I think that statement greatly underestimates the curiosity of high-net worth clients. To say that a person worth $100 million doesn't want to understand how an *IUL* works is a condescending thing to say, and from my own personal experience, a very inaccurate thing to say.

When I started teaching advisors and their clients how *Premium Financed IULs* work at the granular level, my result was much different than Pandora's because when I opened up the *black box* of *IULs*, not only did the evils of the life insurance industry come out, but so did *hope*. Sure, I exposed certain products and their design flaws (especially in premium financing), but I have also

been able to uncover the truth about how a well-designed *Premium Financed IUL* can be one of the most valuable assets in estate planning that exists – assuming it is used properly, and assuming it is used with the right client.

As I mentioned in the first chapter of this book, before I knew anything about life insurance, my financial advisor lost me $930,000 in three years due to a poorly designed life insurance strategy. I'm still not certain if he even knew what he was doing when he designed that strategy.

If he did, he was commission-greedy and unethical.

If he didn't, then he was irresponsible and incompetent.

Either way, I was the one got hurt financially.

The purpose of this book is to teach you how these products actually work – specifically the *Indexed Universal Life Insurance (IUL)* product – so that you fully understand not only the general concept, but the granular details as well.

I will also teach you several different ways to finance life insurance premiums because each specific financing arrangement should be custom designed for each specific client.

In Chapter 9, I will dive into a thorough explanation of how life insurance can be utilized in effective estate tax planning, but before I delve into its application, I will first explain how the *IUL* product is constructed, beginning with what most believe to be a black box – *policy charges*.

Chapter 3
How IUL Policy Charges Actually Work

When most financial professionals measure risk, they will typically have conversations about *Standard Deviation*, *Sharpe Ratios*, and *Monte Carlo* simulations.

These risk-measuring techniques are certainly important topics of discussion because they address the *Probability Of Risk*, however they all fail to articulate the most important element of risk: *The Consequence Of Risk*.

To give you a non-insurance-related analogy, I am a very skilled driver by most people's standards. My track record behind the wheel is very good, and so the *Probability Of Risk* when I'm driving to the grocery store is very low. That being said, I still wear my seatbelt. Why? Because the *Consequence Of Risk* (getting into a fatal car accident) is too high to not wear a seatbelt. My seatbelt mitigates the risk of dying in the event of a serious car accident – it doesn't guarantee survival, but statistically speaking, it drastically reduces the likelihood of fatality.

My perspective on premium financing is very similar. The *Consequence Of Risk* in premium financing is severe – a lapsing policy – which can happen if the compounding debt of interest accrual outpaces the policy value growth. However the risk of interest accrual is not limited to its use solely in the third-party loan debt. It also includes the accrual that occurs in a *Participating Loan* with the carrier, which I will discuss in great detail in both Chapter 5 and in Chapter 7, pages 54-56. If the combination of the policy charges and the internal accrued interest debt erodes the cash value greater than the index credit grows the cash value, it may result in an early policy lapse. The probability of this happening drastically increases when a premium financing arrangement is too aggressively designed wherein the client does not have enough *skin-in-the-game*.

The *Probability Of Risk* in an over-leveraged, overly-aggressive premium financing arrangement is too high for most

clients' financial strength and risk tolerance levels. At *Lionsmark Capital*, we provide the *premium financing seatbelt (*reducing the *Probability Of Risk*), as well as the simulated crash test results (modeling the *Consequence Of Risk)* in order to evaluate whether or not premium financing is appropriate for the client.

Sure, there are extremely rare exceptions where high-risk tolerant minded clients choose to employ hyper-aggressive leverage-on-leverage tactics, but for the most part, life insurance should be a conservative piece of a client's overall financial portfolio, especially when it comes to estate tax planning. I specialize in the conservative approach to premium financing.

Although I am not a CPA or tax attorney (which means that I cannot give tax advice or legal advice), I can mathematically model different premium financing strategies, compare them to non-insurance-based solutions, and showcase different financial outcomes using certain tax assumptions. I can also model certain unfavorable assumptions that put extra strains on the premium financed solutions, which I think is vitally important to model for clients in the spirit of full transparency.

This industry lacks full client disclosure, so being the *beacon of transparency* – albeit a self-proclaimed title – is the main reason I am the trusted source of premium financing for top advisors, producer groups, and carriers in the life insurance industry.

If the spirit of advisor/client conversations is rooted in education, consumer protection, and risk mitigation, then the foundation of these conversations will be client-centric, which is what it should be. My goal in all communication efforts is to transparently articulate how the math works, and if the indisputable math tells us that one particular method of premium financing is the most advantageous to the client above all other options, the decision to move forward with that particular design is a simple one.

Conversely, there have even been scenarios where my mathematical modeling process proved that it was NOT in the client's best interest to finance their life insurance premiums, and in such scenarios, I am the first one to discourage them from using

premium financing as a strategy. Some advisors don't like that I'm so blunt with my recommendations against premium financing in these scenarios, and some of them will even try to get me to rework the numbers to favor the premium financing proposition. In these rare instances, my answer is always the same: *The math either works, or it doesn't work. The math doesn't lie.*

Your journey to understanding the true *Consequence Of Risk* in poorly designed *Premium Financed IUL* policies starts with understanding how policy charges and credits actually work.

When a carrier receives the policy premium for an *IUL* product, the first charge that is deducted is the *premium load*. *Premium loads* are comprised of the state and local taxes that are deducted from the premium payment before the net premium is applied to the policy value. Assuming the premium is paid annually at the *Beginning Of The Year (BOY)*, the premium loads are also deducted at *BOY*. The remaining policy charges (e.g., Cost of Insurance, Administration Fees, Mortality Expenses, etc.) are then deducted monthly.

Assuming the client selected a *1-Year Annual Point-To-Point* index option, the *segment* begins in the month the premium is swept into the index account (e.g., the 15th day of the month), and ends twelve months later. At the end of this 12-month segment – the *End Of The Year (EOY)* – the index credit is then determined based on the underlying index's performance during that 1-year segment wherein the *IUL's* cap and floor would be applied to the gross accumulated value of the policy (not the net cash surrender value, but the gross accumulated value). Some carriers apply this index credit to the *EOY Accumulated Value (EOYAV)*, whereas other carriers apply the index return to the *Average Monthly Accumulated Value (AMAV)*.

Mathematically speaking, the *AMAV* is a higher number than the *EOYAV* because it does not account for 100% of the monthly charges. In other words, in the second month of the segment, only 2/12 of the monthly charges have been deducted, hence the accumulated value in that month would be higher than the accumulated value in the eleventh month wherein 11/12 of the monthly charges were deducted.

For the sake of this discussion, we will assume that the *Indexed Universal Life (IUL)* insurance product applies the index credit to the *EOY Accumulated Value*. We will also assume that the product's underlying index tracks the S&P 500's performance, with a 0.00% floor and a 9.00% cap. In the event that the S&P 500 produced a positive return of 15.00% in a given year, the policy index credit would credit 9.00%, not exceeding the maximum allowable return (the cap).

	$1,000,000	Previous Year's EOY Accumulated Value
+	$0	New Policy Premium
	$1,000,000	**Current Year's BOY Accumulated Value**
-	$50,000	Current Year's Policy Charges
	$950,000	**Current Year's EOY Accumulated Value (Before Index Credit)**
x	9.00%	Index Credit (assuming a +15.00% S&P 500 Return & 9.00% cap)
	$85,000	**Accumulated Index Credit (Accumulated Value Gain)**
+	$950,000	Current Year's EOY Accumulated Value (Before Index Credit)
	$1,035,500	**Current Year's EOY Accumulated Value (After Index Credit)**

However if the S&P 500 produced a negative return in a given year, the index credit would be 0.00% (the floor). This stop-loss feature of this particular crediting method acts as a risk-mitigation tool, which is certainly one of the most valuable elements of the *IUL* product chassis.

However, one of the most inaccurate statements I've heard some life insurance agents say is, *"With the IUL's 0.00% floor, you can never lose money."* Mathematically speaking, this is not a true statement. It is true that you would not receive a negative index return (an index return less than the 0.00% floor), however that is only true AFTER the policy charges have been deducted from the policy value. If the policy charges were $50,000 in a given year, and the *BOY* cash surrender value was $1,000,000 (assuming a 0.00% index credit in such year), the *EOY* cash surrender value would be $950,000.

	$1,000,000	Previous Year's EOY Accumulated Value
+	$0	New Policy Premium
	$1,000,000	**Current Year's BOY Accumulated Value**
-	$50,000	Current Year's Policy Charges
	$950,000	**Current Year's EOY Accumulated Value (Before Index Credit)**
x	0.00%	Index Credit (assuming a -15.00% S&P 500 Return & 0.00% floor)
	$0	**Accumulated Index Credit (Accumulated Value Gain)**
+	$950,000	Current Year's EOY Accumulated Value (Before Index Credit)
	$950,000	**Current Year's EOY Accumulated Value (After Index Credit)**

In this example, the policy's *Accumulated Value* would have actually decreased by $50,000 despite the 0.00% floor.

Aside from premium financing, the first risk factor to understand in an *IUL* is the relationship between policy index credits and policy charges.

One of the problems I have with clients making buying decisions solely based on standard carrier illustrations is that they depict a positive static index return every year with no simulations of volatility wherein 0.00% index returns are modeled (as they were in the example I just depicted).

What this means is that the discussion (and mathematical modeling) of negative arbitrage during 0.00% return years is never properly articulated (and certainly never mathematically stress-tested) in most advisor/client discussions.

As I mentioned earlier in this book, one of the main things that makes *Lionsmark Capital* stand apart from other premium financing intermediaries is our ability to mathematically model scenarios wherein these design elements (e.g., floors, caps, charges, etc.) can be modeled during times of volatility so you can actually see the potential effects of these different variables.

I will discuss how we do this later in this book, but first, let's discuss how the floors and caps are created by the carriers, as well as the long-term sustainability of such product features.

Chapter 4
How IUL Floors & Caps Work

The 0.00% floor sounds too good to be true, doesn't it?

Years ago when I first heard about this *IUL* feature, I thought the same thing. Most people do not truly understand how this feature actually works, and this seemingly mysterious *black box* makes intelligent people skeptical. I am still shocked that the life insurance industry does not do a better job of explaining how the *floor & cap proposition* mechanically works in practice, because once you understand it, you will appreciate just how well thought out (and how sustainable) this design element truly is.

To understand how an *IUL*'s crediting method works, we must first discuss the origin of permanent life insurance policies in general. We will start with one type of permanent life insurance policy: *Whole Life*.

Whole Life is not synonymous with the category of ALL permanent life insurance policies. *Whole Life* is one of several different types of permanent life insurance. Compared to *Term* life insurance (which expires after the term period), *Whole Life* was originally designed to give a person life insurance coverage that would last for their whole/entire life, hence the name *Whole Life*.

The general concept was that the premiums (approximately four times greater than *Term* insurance premiums) would not only pay for the cost of insurance, but the excess premiums would be *invested* in the life insurance company itself (somewhat similar to buying stock in the insurance company, not exactly, but similar). These excess premiums invested in the life insurance company would yield a *dividend* based on how well the life insurance company's overall investment portfolio did in the previous year.

A dividend would be declared, then it would be credited to the policy's cash value the following year. It would then be used to pay for the ongoing *Cost Of Insurance* (long after the insured person stopped paying premiums) which enabled the policy to last

until the end of the insured person's life – insuring them for their *whole* life. To give you an idea of how stable these *Whole Life* dividends have been over time, below is the historical dividend scale over the last forty years of four major *Whole Life* carriers.

CALENDAR YEAR	GUARDIAN DIVIDENDS	MASS MUTUAL DIVIDENDS	NORTHWESTERN DIVIDENDS	PENN MUTUAL DIVIDENDS
1981	7.20%	8.27%	7.25%	6.25%
1982	7.50%	8.27%	9.00%	6.25%
1983	7.65%	8.27%	9.75%	6.58%
1984	12.25%	11.60%	10.75%	7.15%
1985	13.25%	12.20%	11.00%	11.20%
1986	13.25%	12.20%	11.25%	11.20%
1987	12.50%	12.20%	11.00%	8.20%
1988	12.00%	11.35%	10.25%	8.20%
1989	11.50%	11.15%	10.00%	9.93%
1990	11.00%	10.50%	10.00%	9.93%
1991	10.50%	10.50%	10.00%	9.93%
1992	10.25%	9.95%	9.25%	9.93%
1993	9.75%	9.45%	9.25%	9.70%
1994	9.00%	9.30%	8.50%	9.20%
1995	8.50%	9.00%	8.50%	8.50%
1996	8.00%	8.40%	8.50%	8.50%
1997	8.50%	8.40%	8.50%	8.00%
1998	8.75%	8.40%	8.80%	8.00%
1999	8.75%	8.40%	8.80%	7.40%
2000	8.50%	8.30%	8.80%	7.40%
2001	8.50%	8.30%	8.80%	7.40%
2002	8.00%	8.10%	8.60%	7.40%
2003	7.00%	7.90%	8.20%	6.48%
2004	6.60%	7.50%	7.70%	5.74%
2005	6.75%	7.00%	7.50%	5.74%
2006	6.50%	7.55%	7.50%	6.30%
2007	6.75%	7.55%	7.50%	6.30%
2008	7.25%	7.90%	7.50%	6.34%
2009	7.30%	7.45%	6.50%	6.34%
2010	7.00%	6.85%	6.15%	6.34%
2011	6.85%	6.80%	6.00%	6.34%
2012	6.95%	7.00%	5.85%	6.34%
2013	6.65%	7.00%	5.60%	6.34%
2014	6.25%	7.10%	5.60%	6.34%
2015	6.05%	7.10%	5.60%	6.34%
2016	6.05%	7.10%	5.45%	6.34%
2017	5.85%	6.70%	5.00%	6.34%
2018	5.85%	6.70%	5.00%	6.34%
2019	5.85%	6.40%	5.00%	6.10%
2020	5.56%	6.00%	5.00%	5.75%
Average Returns:	**8.30%**	**8.50%**	**7.98%**	**7.46%**

In addition, most *Whole Life* products also guarantee a minimum annual return (typically around 4.00%).

One of the main benefits of the cash value accumulation inside a life insurance policy is that the gains are tax-free due to IRS tax code 7702. This favorable tax treatment eventually led to the category of *permanent life insurance* expanding into several additional products with more aggressive underlying investments.

When *Variable Universal Life (VUL)* insurance products hit the market, the idea was to use mutual funds as the underlying investments instead of the life insurance carrier's guaranteed return and dividend crediting method. In concept, the client could use the same mutual funds they were already investing in, but by housing them inside a life insurance construct, the gains on these mutual funds would be tax-free.

It was a great concept in theory, especially when the mutual fund returns were sky-high like they were in the mid-80's and 90's. But when the tech bubble burst in the early 2000's, it was rude awakening for *VULs* because in order to offset the high policy expenses that were built into the policy, the underlying mutual fund returns needed to continue to perform as they did in the previous two decades. When this did not happen in *The Lost Decade* (2000-2009 wherein the S&P 500 produced four negative returns during this ten-year run), these expense charges began to outpace the *VUL*s' credits. Today, many advisors and consumers have shifted their interest away from *VUL* policies towards *IUL* policies.

Unlike a *VUL* policy that can experience negative returns, *IULs* have a *floor* – a minimum index credit – which is typically 0.00%. The question is, *"How is this possible and how is this sustainable?"*

If you recall, the *Whole Life* product crediting method included a guaranteed return plus a dividend based on how profitable the life insurance company was in the previous year. In an *IUL* product, the carrier essentially takes the guaranteed return they were going to automatically credit in the *Whole Life* policy and uses that amount as the budget to purchase *options contracts*.

I am going to attempt to explain the general mechanics of how this works without getting too overly detailed, for the full explanation would require a 1,000+ page book. In my attempt to

teach you the basics, I will articulate this as succinctly as possible. Additionally, in the spirit of full disclosure, there are details that vary from carrier to carrier, product to product.

For example, *Allianz* does not currently use investment banking firms to purchase their options contracts. They do it in-house due to the massive amount of options purchasing they do to not only support their *IUL* products, but also their international distribution of *Indexed Annuities*, so their method of utilizing S&P 500-correlated options contracts is different. I am not saying the *Allianz's IUL* products are necessarily better or worse than other carriers' *IULs*. I am just mentioning their unique way of buying options.

As another example of differentiation, *Pacific Life* applies their index credit to the *Average Monthly Accumulated Value*, whereas most other carriers apply their index credit to the *EOY Accumulated Value*, which is a lower value. Again, I am not saying that *Pacific Life's IUL* products are necessarily better or worse than other carriers' *IULs*. I am just mentioning their unique way calculating their index crediting method.

These are just two of many examples of how each product from each carrier is built slightly differently, however learning about *IULs* in general is best done by using one hypothetical example, which I will do below.

In this hypothetical example, the carrier purchases *options* from an investment banking firm – S&P 500-correlated options with a 0.00% floor. The budget for this type of arrangement is approximately 4.00% of the life insurance premium ($4,000 per $100,000 in insurance premium). But remember, that was the amount the carrier was going to automatically credit the *Whole Life* policy's cash value anyway, so in this scenario, the carrier has zero exposure because that allocation was already built into the pricing.

The investment banking firm takes the $4,000 as the *options premium*, and if the S&P 500 produces a negative return, they absorb the losses and pass the benefit of the 0.00% floor on to the carrier, who then passes the benefit on to the policy. The investment banking firm does however get to keep the $4,000.

If the S&P 500 produces a positive return, they pass that return through to the carrier, who then passes the return through to the policy, up to a maximum allowable return (the cap), and any return above the cap is then retained by the investment banking firm in addition to the $4,000 options premium per $100,000 in insurance premium.

The carrier does not incur any risk in a negative S&P 500 return scenario, and they do not participate in any of the upside above the cap either. Remember, the $4,000 options premium they paid the investment banking firm was already budgeted into the contract pricing, so for the policy owner, the decision to buy an *IUL* instead of a *Whole Life* policy is based on the belief that over time, the returns of the S&P 500-correlated index fund with a floor and cap with outpace the dividend returns of a *Whole Life* product.

This decision could be based on the client analyzing historical S&P 500 performance using the floor and cap assumptions, and comparing them to historical *Whole Life* dividend returns.

This decision could also be influenced by the conservative nature of the *Whole Life* dividend crediting history which has never produced a 0.00% return, let alone a negative return.

However, there are several elements in addition to the dividend or index return that also determine the actual cash value yield over time.

For example, policy charges need to be factored into the equation. The actual sequence of returns that a policy experiences also plays a major role in accumulation.

Another variable that affects cash value accumulation is the method in which drawdowns are taken from the policy values – not just retirement income drawdowns, but drawdowns to pay off the third-party lender in a premium financing arrangement. I will be discussing this element in great depth in the upcoming chapter (Chapter 5).

The following chart shows historical S&P 500 returns and different floors and caps. Again, merely comparing average *Whole Life* dividends to average S&P 500-correlated *after-floor/after-cap* returns does not tell the entire story.

CALENDAR YEAR	S&P 500 RETURNS	FLOOR: 0.00% CAP: 8.50%	FLOOR: 0.00% CAP: 10.00%	FLOOR: 0.00% CAP: 12.00%
1981	-9.73%	0.00%	0.00%	0.00%
1982	14.77%	8.50%	10.00%	12.00%
1983	17.26%	8.50%	10.00%	12.00%
1984	1.38%	1.38%	1.38%	1.38%
1985	26.36%	8.50%	10.00%	12.00%
1986	14.62%	8.50%	10.00%	12.00%
1987	2.04%	2.04%	2.04%	2.04%
1988	12.39%	8.50%	10.00%	12.00%
1989	27.25%	8.50%	10.00%	12.00%
1990	-6.56%	0.00%	0.00%	0.00%
1991	26.30%	8.50%	10.00%	12.00%
1992	4.48%	4.48%	4.48%	4.48%
1993	7.07%	7.07%	7.07%	7.07%
1994	-1.56%	0.00%	0.00%	0.00%
1995	34.13%	8.50%	10.00%	12.00%
1996	20.26%	8.50%	10.00%	12.00%
1997	31.01%	8.50%	10.00%	12.00%
1998	26.67%	8.50%	10.00%	12.00%
1999	19.53%	8.50%	10.00%	12.00%
2000	-10.14%	0.00%	0.00%	0.00%
2001	-13.04%	0.00%	0.00%	0.00%
2002	-23.37%	0.00%	0.00%	0.00%
2003	26.38%	8.50%	10.00%	12.00%
2004	8.99%	8.50%	8.99%	8.99%
2005	3.00%	3.00%	3.00%	3.00%
2006	13.60%	8.50%	10.00%	12.00%
2007	3.52%	3.52%	3.52%	3.52%
2008	-38.49%	0.00%	0.00%	0.00%
2009	23.65%	8.50%	10.00%	12.00%
2010	12.63%	8.50%	10.00%	12.00%
2011	0.10%	0.10%	0.10%	0.10%
2012	13.29%	8.50%	10.00%	12.00%
2013	29.43%	8.50%	10.00%	12.00%
2014	11.54%	8.50%	10.00%	11.54%
2015	-0.73%	0.00%	0.00%	0.00%
2016	9.54%	8.50%	9.54%	9.54%
2017	19.42%	8.50%	10.00%	12.00%
2018	-6.24%	0.00%	0.00%	0.00%
2019	28.88%	8.50%	10.00%	12.00%
2020	16.26%	8.50%	10.00%	12.00%
Average Returns:	**9.90%**	**5.64%**	**6.50%**	**7.59%**

What I find mildly fascinating is that when merely comparing the average returns seen above (during this particular historical 40-year period) to average *Whole Life* dividend returns

shown during the same historical 40-year period (as depicted a few pages ago), it seems that the *Whole Life* dividend returns are better than the *IUL's* S&P 500-correlated *after-floor/after-cap* returns, even with a 12.00% cap (which is on the higher end of available *IUL* caps at the time this book was written).

But merely comparing the average historical *Whole Life* dividend credits to the historical *IUL* index credits does not give you a complete picture of which is *better*, especially when financing the premiums.

The reason I say this is that when the third-party lender is paid off by taking a lump sum drawdown from the policy value, it can be done in three different ways in an *IUL*.

1. Withdrawals.
2. Fixed Loans.
3. Participating Loans.

Some *Whole Life* products will not allow the policy owner to drawdown policy values as efficiently as *IUL* products, and in premium financing, this is an extremely important attribute to consider for the long-term sustainability of the policy.

Yes, some *Non-Direct Recognition Whole Life* carriers allow drawdowns to be taken in a similar fashion to the way *Participating Loans* are treated in an *IUL* (currently *New York Life* and *Mass Mutual* allow this), while other *Direct-Recognition Whole Life* carriers limit the drawdowns to be treated similarly to *Fixed Loans* in an *IUL*.

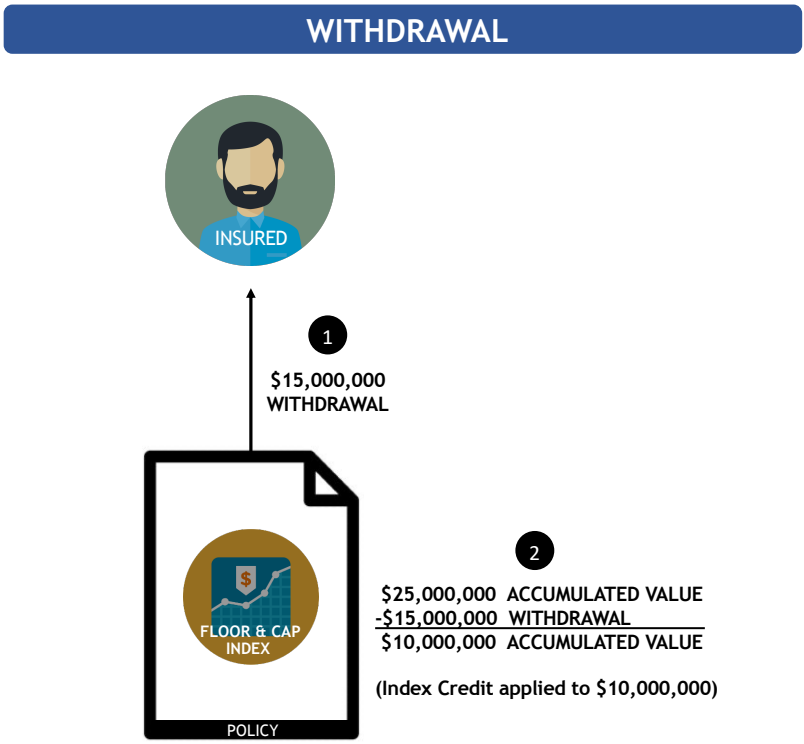
In the next chapter, I will explain the difference between *Withdrawals*, *Fixed Loans*, and *Participating Loans* in an *IUL*.

Chapter 5
How Policy Drawdowns Work

There are three ways to take drawdowns from an *IUL*, whether it be for supplemental retirement income or to pay off a third-party premium financing lender. You can take *Withdrawals*, *Fixed Policy Loans*, or *Participating Policy Loans*.

1. Withdrawal.

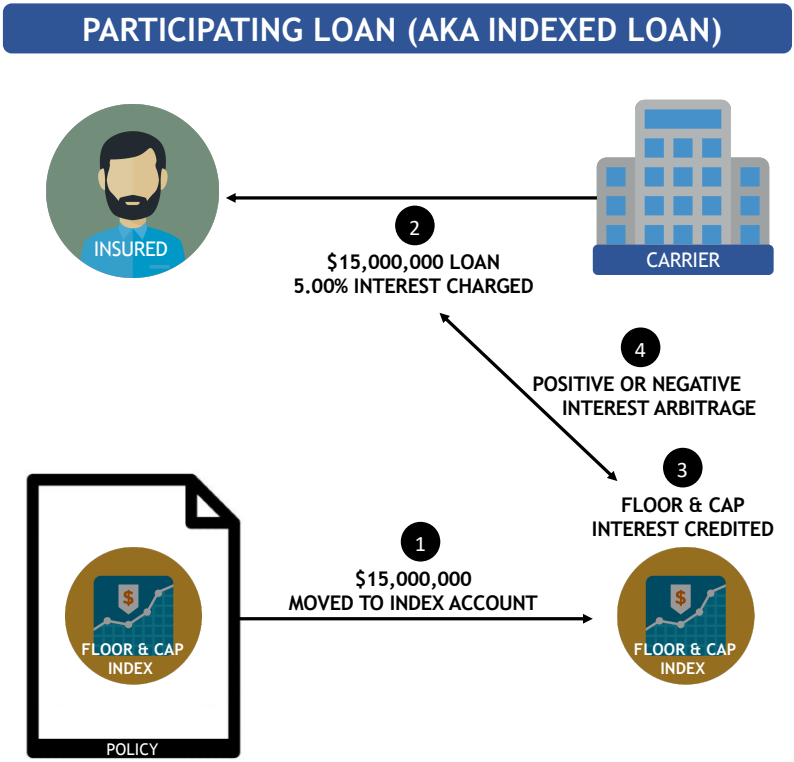
In a *withdrawal* scenario, the drawdown amount is literally withdrawn from the index account to payoff the third-party lender. From that moment forward, the remaining net accumulated value of the policy receives the annual *after-floor/after-cap* index credit each year.



2. Fixed Loan (AKA "Wash Loan").

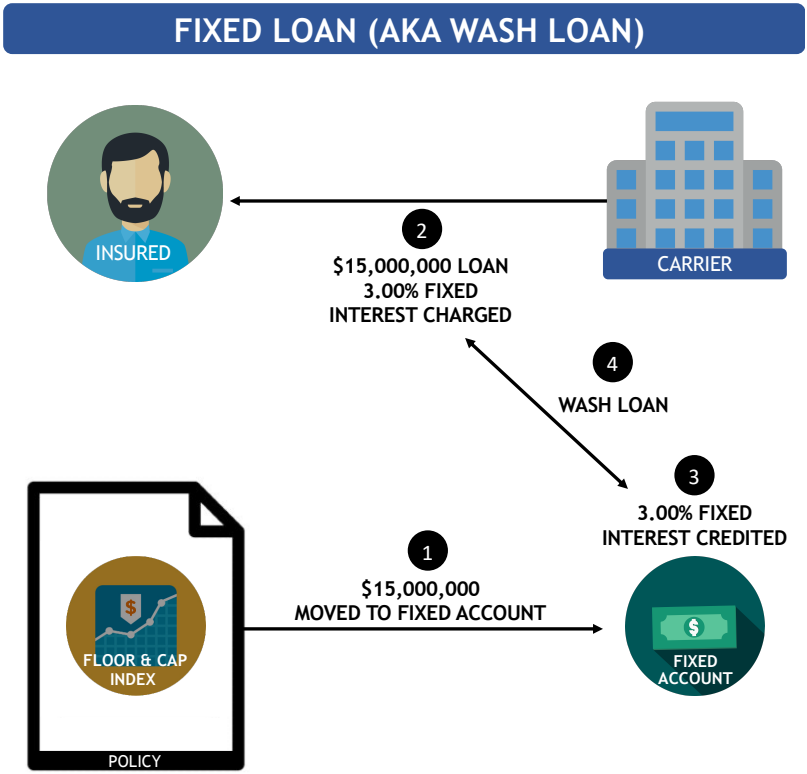
When taking a *Fixed Policy Loan*, the drawdown amount is removed from the index account and placed into a separate account that receives a fixed return (3.00% as a hypothetical example) instead of the annual after-floor/after-cap index credit each year. The carrier then "loans" the policy owner the same drawdown amount and "charges" interest on the policy loan at the same interest rate the fixed account receives (3.00% in this example), making it a "wash loan."

Similar to the *Withdrawal* scenario, from that moment forward, only the remaining net accumulated value of the policy receives the annual *after-floor/after-cap* index credit each year.



3. Participating Loan (AKA "Indexed Loan").

When taking a *Participating Policy Loan*, the drawdown amount is removed from the index account and placed into a separate account that receives the same (or similar) annual *after-floor/after-cap* index credit as the indexed account inside the *IUL*. The carrier then "loans" the policy owner the same drawdown amount and "charges" interest on this policy loan. Sometimes the interest rate charged is a fixed amount (5.00% for example), and sometimes that interest rate is a variable floating rate. In this policy loan strategy, the policy owner is hoping the *S&P 500-correlated floor & cap* index crediting method will outpace the interest charged.



The anticipated benefit of the *Participating Loan* is that from the moment the *Participating Loan* is taken, the annual *after-*

floor/after-cap index credit is applied to both the *Gross Accumulated Value* in the policy, as well as the index account the funds were moved into.

The accounting of this is all done on a ledger with the carrier, making it easy for the policy owner. In other words, the policy owner does not need to do any accounting independently to manage the interest charged and credited

To see how *Participating Loans* work in a case study during the 40-year period with the *Worst Compounded Annual Growth Rate*, refer to pages 54-56.

My backtesting model evaluates each of these three methods of drawdowns, backtesting 121 different historical 40-year periods of S&P 500 performance, and builds a *proxy* for the premium financed *IUL*.

To be clear, this evaluation model is not a modified version of an *IUL* illustration. That would violate AG-49A guidelines and several other compliance regulations. I created a *Hypothetical Synthetic Asset* – a fictitious index account – that behaves very similar to an *IUL* in regards to charges, crediting methodology, and participating loan methodology.

The goal was to see how these factors could potentially affect short-term and long-term outcomes during times of volatility. For example, in certain sequences of returns we analyze, there are as many as four 0.00% index credits within the first ten years of the 40-year sequence.

In other scenarios we model, the consecutive 0.00% index returns happen in the middle of the 40-year sequence during the beginning years of income drawdowns (or right before or after the lender payoff, similar to a premium financed life insurance scenario), both of which put excessive stress on cash value accumulation which is needed to keep the policy in force.

Before we delve into my backtesting methodology, in this next chapter, I will address one of the most controversial topics of discussion when it comes to *IULs*: Multiplier Bonuses & Asset-Based Charges.

Chapter 6
Are IUL Multiplier Bonuses Too Risky?

One of the most controversial design elements in modern-day *IULs* is the *Multiplier Bonus*. At the moment, the majority of *IUL* multiplier propositions allow a client to accept an asset-based charge in exchange for a multiplier bonus that enhances the index return.

In this arrangement, the client *doubles down* on the carrier's ability to buy more options contracts from the investment bankers. Often times, *IUL* critics attempt to make multipliers appear opaque and mysterious, however the multiplier proposition is actually quite simple.

As an example, if the multiplier bonus factor is 1.45x, this means that the *after-floor/after-cap* index return would be multiplied by 1.45, giving the pre-multiplier return a 45.00% boost.

	15.00%	End-Of-Segment S&P 500 Return
>	10.00%	IUL Cap
	10.00%	**End-Of-Segment After-Floor/After-Cap Return**
x	1.45	Multiplier Bonus
	14.50%	**EOY Index Credit After Multiplier Bonus**

If the client likes this proposition, they can elect to purchase this feature each year at policy renewal for an asset-based charge. For example, if the asset-based multiplier charge is 1.00%, that means the policy receives an additional charge on top of the standard policy charges, calculated by multiplying 1.00% by the *Accumulated Value* and deducted from the *Accumulated Value* in the current year (1/12 of 1.00%, monthly).

Pre-AG-49A, one of the biggest criticisms of these multiplier features was that the carrier illustration depicted a static positive index credit each year, which illustrated a multiplier advantage each year. In other words, if the carrier illustration showed a static 5.50% index return every year, and the multiplier bonus factor was 1.45x, the illustration's cash value growth in the

illustration was actually calculated based on a 7.98% index credit (5.50% x 1.45 = 7.98%), not the stated 5.50%.

Using the static positive index credits in a carrier's illustration was misleading because in a real-world scenario, the S&P 500 is going to experience some negative return years wherein the policy's index credit would be 0.00%. In these years, not only would the policy's cash value decrease due to the standard policy charges, but the additional 1.00% multiplier asset-based charge would create an additional reduction in cash value.

The *IUL* multiplier critics and die-hard *Whole Life* fans accused *IUL* illustrations of being misleading because the illustrations assumed a positive multiplier bonus each year, not taking into consideration the substantial reduction in cash value the additional asset-based charges could cause during 0.00% index crediting years, and they were right… sort of.

The problem was that no one did the math.

The critics were making broad conceptual assertions that the multiplier propositions were too risky, but they had no mathematically-proven analytics to back up their claims.

On the other side of the fence were the over-zealous *IUL* fanatics that reveled in showing the massively bolstered returns and claimed that *IUL*s with multiplier bonuses were the best thing since sliced bread, but they had no mathematically-proven analytics to back up their claims either.

So who was right?

Neither of them.

As a result, the regulators passed a new actuarial guideline – AG-49A – that restricted carrier illustrations from illustrating multiplier bonuses. The illustrations could now only show multiplier asset-based charges, but no multiplier bonuses. The non-sensical nature of this restriction didn't solve the problem they were trying to solve.

I would agree that an illustration that depicts a positive static return every year wherein a multiplier bonus enhances the index return EVERY YEAR tells a very incomplete and inaccurate story

of how multiplier *IULs* actually work, but I would also say that showing a carrier illustration with multiplier asset-based charges with no multiplier bonus credits also tells a very inaccurate story.

As a result of the illogical way this restriction was implemented, most agents started running illustrations WITHOUT any multiplier features. The problem with this decision was that if the client intended to buy an *IUL* with a multiplier feature, the agent was showing the client something they were not actually going to buy. This is perhaps the most inaccurate scenario of all scenarios an agent could present to a client.

To complicate things even further, if the client was actually going to buy an *IUL* with a multiplier feature, and they were originally shown an illustration without the multiplier feature, just prior to policy delivery, the client had to sign a version of the illustration that included all the product features they were actually buying, which included the multiplier feature. This meant that the agent had to re-run the illustration and include the multiplier asset-based charges, which then depicted a much worse cash value accumulation outcome because the additional charges eroded the as-illustrated returns with no multiplier bonus enhancement taken into consideration. This version of the illustration looked substantially worse than the first version the client saw when they initially made their decision to buy, which made the agent look like they had *bait-and-switched* the offering.

As an alternative, the agent could have just started off showing the client a version of the illustration that included all of the multiplier charges (but did not include any of the multiplier benefits), and say, "Trust me, there are multiplier bonuses included, but I can't show them in the carrier illustration."

That's a tough thing to say, and an impossible thing to prove. It would be like trying to sell a $550,000 *Lamborghini Aventador* that actually puts out 770 horsepower, despite the brochure stating that it only puts out 570 horsepower, and telling the client, "Trust me, not the brochure."

The third option the agent had was to not sell any *IULs* with multiplier bonus features whatsoever, restricting the client from

buying something that might be tremendously beneficial to their overall estate plan, retirement plan, and overall financial plan. Clearly, this was not a good option either.

I am a big supporter of compliance and industry regulation in general, for I believe the spirit of compliance is rooted in consumer protection, and consumer protection is a good thing.

But AG-49A did not solve the problem of lack of transparency in carrier illustrations. It just exchanged one problem for another – exchanging one inaccurate depiction for another inaccurate depiction. The illustrative limitations and inaccuracies that AG-49A created didn't stop there either.

AG-49A also required the carrier illustration to depict a static *Participating Loan Rate* equal to 0.50% less than the index crediting rate illustrated, despite what the actual *Participating Loan Rate* was. In other words, if the carrier illustration assumed a 5.75% index crediting rate, the *Participating Loan Rate* had to be illustrated at 5.25%, even if the actual *Participating Loan Rate* was only 5.00%.

This problem was two-fold.

First, this depiction showed a *Participating Loan Rate* that was not accurate. And second, because the illustration depicted a positive static index credit every year, there was always a positive arbitrage between the index credit and the *Participating Loan Rate*, which will not happen in years when the actual *Index Credit* is lower than the actual *Participating Loan Rate*.

In a year wherein the *Participating Loan Rate* was 5.00%, and the index credit was 2.00%, the client would actually lose 3.00% in that negative arbitrage year (2.00% - 5.00% = -3.00%). However if the *Participating Loan Rate* was 5.00%, and the index credit was 9.00%, the client would actually gain 4.00% in that positive arbitrage year (9.00% - 5.00% = 4.00%).

This is why my backtesting capabilities are so valuable, because they can mathematically articulate both types of scenarios in each given year so the client can actually see how the math works during times of volatility. I will begin explaining these capabilities in the next chapter.

Chapter 7
Why Backtesting Is So Important

So far, I have discussed the problems I see with the assumptions and limitations depicted in carrier illustrations, as well as how *IUL* crediting and charges methods actually work in real-world scenarios. In this chapter, I will explore how floors, caps, multipliers and asset-based charges can impact financial outcomes. I will do so by reviewing a case study using data sourced directly from an actual premium financed *IUL* policy, but we will do so by analyzing the behavior of a *Leveraged Hypothetical Synthetic Asset* that will act as a proxy for a *Premium Financed IUL.*

As I stated earlier in this book, my process begins with analyzing 121 different historical 40-year periods. I use one-year annual point-to-point segments and track them over 40-year rolling periods.

The first 40-year period I analyzed started on January 1, 1970 and tracked historical S&P 500 performance for the next forty years (forty 12-month segments), ending on December 31, 2009. The second 40-year period I analyzed started one month later on February 1, 1970 and ended on January 31, 2010. The third one started one month after that on March 1, 1970 and ended on February 28, 2010. These 40-year sequences continued with the 121st one starting on January 1, 1980 and ending on December 31, 2019.

In the spirit of conservatism (and arguably pessimism), I will focus on the 40-year period that produced the *Worst Compounded Annual Growth Rate* of all the 121 different 40-year periods analyzed. To be clear, this particular 40-year period was only the "worst" one based on the *Compounded Annual Growth Rate* of the 121 different 40-year periods I analyzed, not the "worst possible case scenario that could ever exist in the future."

It is certainly possible that the next forty years could produce an even worse *Compounded Annual Growth Rate* than this one, and it is also possible that the next forty years could produce

HYPOTHETICAL SYNTHETIC ASSET — FIRST-DOLLAR FINANCING

WORST CAGR 40-YEAR PERIOD OUT OF 121 DIFFERENT INDEX PERIODS ANALYZED (STARTING 10/1/1971)

Current Cap: **9.00%** Floor Modeled: **0.00%**

Upside Design: **CAPPED** Cap Modeled: **8.00%** Participation Rate: **100.00%**

# YEAR	AGE	1 TOTAL INDEX CONTRIBUTION	2 CLIENT INDEX CONTRIBUTIONS	3 LENDER INDEX CONTRIBUTIONS	4 CUMULATIVE LOAN BALANCE	5 THIRD PARTY LOAN PAYOFF	6 FINANCING INTEREST RATE	7 INTEREST DUE	8 INTEREST ACCRUED	9 TOTAL CLIENT OUTLAY	10 ESTIMATED COLLATERAL	11 CALENDAR YEAR	12 INDEX RETURN (GROSS)	13 INDEX RETURN (FLOOR & CAP)	14 INDEX RETURN (EFFECTIVE)	15 ANNUAL INCOME DRAWDOWNS	16 EOY GROSS INDEX ACCOUNT VALUE	17 EOY NET INDEX ACCOUNT VALUE
1	55	$1,250,000	$0	$1,250,000	$1,250,000		1.67%	$20,875	$0	$20,875	$420,598	1971	12.42%	8.00%	8.00%	$0	$1,130,343	-$613,201
2	56	$1,250,000	$0	$1,250,000	$2,500,000		1.71%	$42,650	$0	$42,650	$420,598	1972	-1.92%	0.00%	0.00%	$0	$2,158,794	-$788,171
3	57	$1,250,000	$0	$1,250,000	$3,750,000		1.75%	$65,730	$0	$65,730	$693,571	1973	-41.40%	0.00%	0.00%	$0	$3,168,301	-$981,646
4	58	$1,250,000	$0	$1,250,000	$5,000,000		1.81%	$90,682	$0	$90,682	$930,997	1974	32.00%	8.00%	11.60%	$0	$4,641,444	-$710,900
5	59	$1,250,000	$0	$1,250,000	$6,250,000		1.89%	$118,296	$0	$118,296	$727,231	1975	25.48%	8.00%	11.60%	$0	$6,259,092	-$295,066
6	60	$1,250,000	$0	$1,250,000	$7,500,000		2.00%	$149,666	$0	$149,666	$381,500	1976	-8.28%	0.00%	0.00%	$0	$7,196,745	-$558,642
7	61	$1,250,000	$0	$1,250,000	$8,750,000		2.13%	$186,306	$0	$186,306	$683,456	1977	6.23%	6.23%	9.03%	$0	$8,846,827	-$109,060
8	62	$1,250,000	$0	$1,250,000	$10,000,000		2.30%	$230,298	$0	$230,298	$306,871	1978	6.61%	6.61%	9.59%	$0	$10,669,487	$513,831
9	63	$1,250,000	$0	$1,250,000	$11,250,000		2.53%	$284,499	$0	$284,499	$0	1979	14.76%	8.00%	11.60%	$0	$12,864,797	$1,510,101
10	64	$1,250,000	$0	$1,250,000	$12,500,000		2.82%	$352,817	$0	$352,817	$0	1980	-7.40%	0.00%	0.00%	$0	$13,686,939	**$1,134,080**
11	65	$0	$0	$0	$12,500,000		3.20%	$400,538	$0	$400,538	$0	1981	3.65%	3.65%	5.29%	$0	$14,122,262	$1,622,262
12	66	$0	$0	$0	$12,500,000		3.70%	$462,574	$0	$462,574	$0	1982	37.91%	8.00%	11.60%	$0	$15,443,786	$2,943,786
13	67	$0	$0	$0	$12,500,000		4.35%	$543,221	$0	$543,221	$0	1983	0.02%	0.02%	0.03%	$0	$15,146,129	$2,646,129
14	68	$0	$0	$0	$12,500,000		5.18%	$648,063	$0	$648,063	$0	1984	9.62%	8.00%	11.60%	$0	$16,565,127	$4,065,127
15	69	$0	$0	$0	$0	-$12,500,000	0.00%	$0	$0	$0	$0	1985	27.04%	8.00%	11.60%	$0	$18,128,863	$5,003,863
16	70	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1986	39.13%	8.00%	11.60%	$0	$19,853,046	$6,071,796
17	71	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1987	-15.51%	0.00%	0.00%	$0	$19,494,263	$5,023,951
18	72	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1988	28.41%	8.00%	11.60%	$0	$21,358,196	$6,164,368
19	73	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1989	-12.34%	0.00%	0.00%	$0	$20,984,487	$5,030,967
20	74	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1990	26.73%	8.00%	11.60%	$0	$23,010,149	**$6,258,953**
21	75	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1991	7.72%	7.72%	11.19%	$0	$25,165,909	$7,577,153
22	76	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1992	9.84%	8.00%	11.60%	$0	$27,655,621	$9,187,428
23	77	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1993	0.82%	0.82%	1.19%	$0	$27,591,616	$8,200,013
24	78	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1994	26.30%	8.00%	11.60%	$0	$30,359,960	$9,998,777
25	79	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1995	17.61%	8.00%	11.60%	$0	$33,411,483	$12,032,241
26	80	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1996	37.82%	8.00%	11.60%	$0	$36,861,094	$14,412,890
27	81	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1997	7.36%	7.36%	10.67%	$0	$40,324,586	$16,753,972
28	82	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1998	26.13%	8.00%	11.60%	$0	$44,476,687	$19,727,542
29	83	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1999	11.99%	8.00%	11.60%	$0	$49,049,902	$23,063,300
30	84	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2000	-27.54%	0.00%	0.00%	$0	$48,464,062	**$21,178,130**
31	85	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2001	-21.68%	0.00%	0.00%	$0	$47,865,319	$19,215,090
32	86	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2002	22.16%	8.00%	11.60%	$0	$52,733,009	$22,650,269
33	87	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2003	11.91%	8.00%	11.60%	$0	$58,083,677	$26,496,799
34	88	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2004	10.25%	8.00%	11.60%	$0	$63,962,559	$30,796,338
35	89	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2005	8.71%	8.00%	11.60%	$0	$70,418,928	$35,594,396
36	90	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2006	14.29%	8.00%	11.60%	$0	$77,509,914	$40,944,155
37	91	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2007	-23.61%	0.00%	0.00%	$0	$76,493,954	$38,099,907
38	92	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2008	-9.37%	0.00%	0.00%	$0	$75,518,096	$35,204,347
39	93	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2009	7.96%	7.96%	11.54%	$0	$83,208,802	$40,879,365
40	94	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2010	-0.86%	0.00%	0.00%	$0	$82,287,647	**$37,841,738**
			$0	**$12,500,000**				**$3,596,216**	$0	**$3,596,216**					*AVERAGE ANNUAL INCOME DRAWDOWN:*	**$0**		**WORST 40**

an even better *Compounded Annual Growth Rate* than the *Best 40-Year Period* of the 121 different 40-year periods I analyzed.

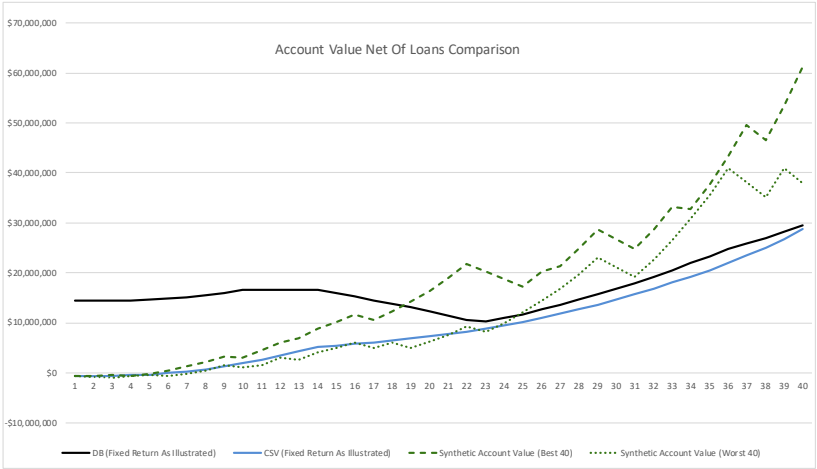
This particular 40-year historical period analyzed above started on October 1, 1971 (column 11). These historical S&P 500 returns do not include S&P 500 dividends (column 12), and we are modeling an 8.00% hypothetical pre-multiplier cap (column 13). We are also modeling a 1.45x multiplier bonus with a 1.00% asset-based multiplier charge (I will explain how this asset-based charge works later in this chapter).

The 1.45x multiplier bonus was then accounted for in the *Effective Index Return* (column 14) which is the *after-floor/after-cap/after-multiplier* return. In a year wherein the index return hits the 8.00% cap, the Effective Index Return is 11.60% (8.00% x 1.45 = 11.60%). It is important to note that in the first ten years of this 40-year sequence, the S&P 500 produced four negative returns, resulting in four 0.00% *Effective Index Returns*. Because the *Hypothetical Synthetic Asset* depicted above is not a life insurance illustration (it is just a proxy for a financed *IUL*), there is no death benefit shown in the model. However, because we are using

the same fee structure as the charges in an actual *IUL* policy, the behavior of this *Leveraged Hypothetical Synthetic Asset* gives us some perspective of how a *Premium Financed IUL's* cash value might behave during one of the 121 different 40-year sequences analyzed. This is a valuable depiction to consider because the charges and crediting methods used cause the account value to behave very similar to an actual *Premium Financed IUL*.

In a death benefit-focused case, it would be logical to question the relevance of this backtested modeling, however the reason this *Leveraged Hypothetical Synthetic Asset* modeling is so important is that in an actual *Premium Financed IUL*, its long-term sustainability is largely based on its cash value performance being able to pay the future insurance charges AND outpace the participating loan debt balance with the carrier. Modeling the behavior of the *Leveraged Hypothetical Synthetic Asset* is important to compare its performance during the *Worst 40* to the as-illustrated *Cash Surrender Value* and death benefit.

HYPOTHETICAL SYNTHETIC ASSET COMPARISON



SCENARIO MODELED	PAYOFF YEAR	TOTAL OUTLAY	TOTAL INCOME DRAWDOWN	NET ACCOUNT VALUE IN YEAR 40	RETURNS DEPICTED	VOLATILITY MODELED	CAGR	PAR LOAN RATE
Static:	15	-$3,596,216	$0	$28,779,800	hypothetical static	no	5.47%	4.97%
Best 40*:	15	-$3,596,216	$0	$61,198,548	actual historical	yes	9.02%	5.00%
Worst 40*:	15	-$3,596,216	$0	$37,841,738	actual historical	yes	6.30%	5.00%

*In modeling every 40-year annual point-to-point period between 1/1/1970 and 12/31/2019, there were 121 different 40-year periods. Each of these 121 different 40-year periods have been analyzed and ranked based on their Compounded Annual Growth Rate (CAGR). This report highlights the Best and Worst 40-year periods limited to this sampling of 121 different 40-year periods. In real-world scenarios, it is possible for a 40-year period to produce a worse CAGR than the Worst 40 in this report. In such case, outcomes could be significantly worse than as depicted in this hypothetical report.

LIONSMARK CAPITAL

At *Lionsmark Capital*, we include this graph in all of our client proposals because it compares the net *Cash Surrender Value*

as-illustrated in the carrier illustration (the solid grey line) to the simulated net account values in the *Hypothetical Synthetic Asset* during the 40-year period with the *Best Compounded Annual Growth Rate* (the heavily dashed line) and during the 40-year period with the *Worst Compounded Annual Growth Rate* (the dotted line).

Though this graph is merely a hypothetical simulation, it is interesting that even during the worst 40-year period of the 121 different 40-year periods analyzed, the simulated account value of the *Leveraged Hypothetical Synthetic Asset* (the dotted line) is similar to the as-illustrated *Cash Surrender Value* in the carrier illustration (the solid grey line) for the first twenty-four years. If the *Cash Surrender Value* in a real world *IUL* equaled the values depicted in the dotted line, it would be logical to assume that the *Death Benefit* would be as much (if not greater) than the as-illustrated *Death Benefit* in the carrier illustration for the first twenty-three years.

Furthermore, beyond the twenty-fourth year, the account value of the *Leveraged Hypothetical Synthetic Asset* not only pulls ahead of the as-illustrated *Cash Surrender Value*, but it also eclipses the carrier as-illustrated *Net Death Benefit* (the solid black line) in both the *Best 40* and the *Worst 40*, and if the *Net Cash Surrender Value* in a real world *IUL* equaled values depicted in the dotted line, the actual *Net Death Benefit* (the solid black line) would have to be greater than the dotted line because the *Net Death Benefit* in a real world *IUL* cannot be less than the policy's *Net Cash Surrender Value*.

This particular synthetic case study is quite encouraging because the backtesting graph on the previous page depicts the outcomes represented in the carrier illustration as being substantially worse than the synthetic account value during the 40-year period with the *Worst Compounded Annual Growth Rate* out of the 121 different 40-year periods analyzed. In addition, our *Leveraged Hypothetical Synthetic Asset* depiction also transparently shows both the standard charges (using the same charge amounts in the carrier illustration) as well as the additional asset-based multiplier charges and compares the total charges to the total index credits each year (depicted in the next two pages).

HYPOTHETICAL SYNTHETIC ASSET — CHARGES + CREDITS + BONUSES

WORST CAGR 40-YEAR PERIOD OUT OF 121 DIFFERENT INDEX PERIODS ANALYZED (STARTING 10/1/1971)

CHARGES & CREDITS

# YEAR	1 ASSET-BASED CHARGES (%)	2 ASSET-BASED CHARGES ($)	3 FIXED CHARGES ($)	4 BACKTESTED YEAR	5 INDEX GROSS RETURN	6 INDEX CREDIT	7 MULTIPLIER BONUS (x)	8 INDEX CREDIT w/ MULTIPLIER	9 PERSISTENCY BONUS (+)	10 TOTAL INDEX CREDIT (%)	11 TOTAL INDEX CREDITS ($)	12 TOTAL CHARGES ($)	13 YEAR-END GAIN/LOSS ($)	14 EOY VALUE AFTER CHARGES B4 CREDIT	15 EOY GROSS INDEX ACCOUNT VALUE	16 EOY NET INDEX ACCOUNT VALUE
1	1.00%	-$12,546	-$190,840	1971	12.42%	8.00%	1.00	8.00%	0.00%	8.00%	$83,729	-$203,386	**-$119,657**	$1,046,614	$1,130,343	-$613,201
2	1.00%	-$21,805	-$199,745	1972	-1.92%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$221,550	**-$221,550**	$2,158,794	$2,158,794	-$788,171
3	1.00%	-$32,046	-$208,447	1973	-41.40%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$240,493	**-$240,493**	$3,168,301	$3,168,301	-$981,646
4	1.00%	-$42,097	-$217,204	1974	32.00%	8.00%	1.45	11.60%	0.00%	11.60%	$482,444	-$259,301	**$223,143**	$4,159,000	$4,641,444	-$710,900
5	1.00%	-$56,784	-$226,155	1975	25.48%	8.00%	1.45	11.60%	0.00%	11.60%	$650,587	-$282,939	**$367,648**	$5,608,505	$6,259,092	-$295,066
6	1.00%	-$72,894	-$239,453	1976	-8.28%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$312,347	**-$312,347**	$7,196,745	$7,196,745	-$558,642
7	1.00%	-$82,216	-$250,241	1977	6.23%	6.23%	1.45	9.03%	0.00%	9.03%	$732,539	-$332,457	**$400,082**	$8,114,288	$8,846,827	-$109,060
8	1.00%	-$98,658	-$262,123	1978	6.61%	6.61%	1.45	9.59%	0.00%	9.59%	$933,441	-$360,781	**$572,661**	$9,736,046	$10,669,487	$513,831
9	1.00%	-$116,820	-$275,072	1979	14.76%	8.00%	1.45	11.60%	0.00%	11.60%	$1,337,201	-$391,892	**$945,310**	$11,527,596	$12,864,797	$1,510,101
10	1.00%	-$138,702	-$289,156	1980	-7.40%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$427,858	**-$427,858**	$13,686,939	$13,686,939	**$1,134,080**
11	1.00%	-$136,178	-$138,260	1981	3.65%	3.65%	1.45	5.29%	0.00%	5.29%	$709,761	-$274,438	**$435,323**	$13,412,501	$14,122,262	$1,622,262
12	1.00%	-$140,506	-$143,237	1982	37.91%	8.00%	1.45	11.60%	0.00%	11.60%	$1,605,268	-$283,743	**$1,321,525**	$13,838,518	$15,443,786	$2,943,786
13	1.00%	-$153,698	-$147,925	1983	0.02%	0.02%	1.45	0.03%	0.00%	0.03%	$3,966	-$301,623	**-$297,657**	$15,142,163	$15,146,129	$2,646,129
14	1.00%	-$150,701	-$152,125	1984	9.62%	8.00%	1.45	11.60%	0.00%	11.60%	$1,721,823	-$302,826	**$1,418,998**	$14,843,304	$16,565,127	$4,065,127
15	1.00%	-$164,873	-$155,753	1985	27.04%	8.00%	1.45	11.60%	0.00%	11.60%	$1,884,362	-$320,626	**$1,563,737**	$16,244,501	$18,128,863	$5,003,863
16	1.00%	-$180,494	-$158,902	1986	39.13%	8.00%	1.45	11.60%	0.00%	11.60%	$2,063,578	-$339,396	**$1,724,182**	$17,789,467	$19,853,046	$6,071,796
17	1.00%	-$197,725	-$161,057	1987	-15.51%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$358,782	**-$358,782**	$19,494,263	$19,494,263	$5,023,951
18	1.00%	-$194,133	-$161,962	1988	28.41%	8.00%	1.45	11.60%	0.00%	11.60%	$2,220,028	-$356,095	**$1,863,933**	$19,138,169	$21,358,196	$6,164,368
19	1.00%	-$212,777	-$160,932	1989	-12.34%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$373,709	**-$373,709**	$20,984,487	$20,984,487	$5,030,967
20	1.00%	-$209,060	-$157,014	1990	26.73%	8.00%	1.45	11.60%	0.00%	11.60%	$2,391,736	-$366,074	**$2,025,662**	$20,618,413	$23,010,149	**$6,258,953**
21	1.00%	-$229,361	-$148,142	1991	7.72%	7.72%	1.45	11.19%	0.00%	11.19%	$2,533,263	-$377,503	**$2,155,760**	$22,632,646	$25,165,909	$7,577,153
22	1.00%	-$250,990	-$133,897	1992	9.84%	8.00%	1.45	11.60%	0.00%	11.60%	$2,874,599	-$384,887	**$2,489,712**	$24,781,022	$27,655,621	$9,187,428
23	1.00%	-$275,988	-$113,654	1993	0.82%	0.82%	1.45	1.19%	0.00%	1.19%	$325,637	-$389,642	**-$64,005**	$27,265,979	$27,591,616	$8,200,013
24	1.00%	-$275,356	-$111,995	1994	26.30%	8.00%	1.45	11.60%	0.00%	11.60%	$3,155,695	-$387,351	**$2,768,344**	$27,204,265	$30,359,960	$9,998,777
25	1.00%	-$303,008	-$118,347	1995	17.61%	8.00%	1.45	11.60%	0.00%	11.60%	$3,472,878	-$421,355	**$3,051,523**	$29,938,605	$33,411,483	$12,032,241
26	1.00%	-$333,875	-$47,954	1996	37.82%	8.00%	1.45	11.60%	0.00%	11.60%	$3,831,440	-$381,829	**$3,449,611**	$33,029,654	$36,861,094	$14,412,890
27	1.00%	-$368,325	-$57,158	1997	7.36%	7.36%	1.45	10.67%	0.00%	10.67%	$3,888,976	-$425,483	**$3,463,492**	$36,435,610	$40,324,586	$16,753,972
28	1.00%	-$402,906	-$68,018	1998	26.13%	8.00%	1.45	11.60%	0.00%	11.60%	$4,623,025	-$470,924	**$4,152,101**	$39,853,662	$44,476,687	$19,727,542
29	1.00%	-$444,363	-$80,799	1999	11.99%	8.00%	1.45	11.60%	0.00%	11.60%	$5,098,377	-$525,162	**$4,573,215**	$43,951,525	$49,049,902	$23,063,300
30	1.00%	-$490,020	-$95,820	2000	-27.54%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$585,840	**-$585,840**	$48,464,062	$48,464,062	**$21,178,130**
31	1.00%	-$484,067	-$114,676	2001	-21.68%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$598,743	**-$598,743**	$47,865,319	$47,865,319	$19,215,090
32	1.00%	-$477,975	-$135,543	2002	22.16%	8.00%	1.45	11.60%	0.00%	11.60%	$5,481,209	-$613,518	**$4,867,690**	$47,251,801	$52,733,009	$22,650,269
33	1.00%	-$526,529	-$160,175	2003	11.91%	8.00%	1.45	11.60%	0.00%	11.60%	$6,037,371	-$686,704	**$5,350,667**	$52,046,305	$58,083,677	$26,496,799
34	1.00%	-$579,888	-$189,667	2004	10.25%	8.00%	1.45	11.60%	0.00%	11.60%	$6,648,438	-$769,555	**$5,878,883**	$57,314,121	$63,962,559	$30,796,338
35	1.00%	-$638,502	-$224,659	2005	8.71%	8.00%	1.45	11.60%	0.00%	11.60%	$7,319,530	-$863,161	**$6,456,369**	$63,099,398	$70,418,928	$35,594,396
36	1.00%	-$702,876	-$262,724	2006	14.29%	8.00%	1.45	11.60%	0.00%	11.60%	$8,056,586	-$965,600	**$7,090,986**	$69,453,328	$77,509,914	$40,944,155
37	1.00%	-$773,889	-$242,072	2007	-23.61%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$1,015,961	**-$1,015,961**	$76,493,954	$76,493,954	$38,099,907
38	1.00%	-$763,880	-$211,978	2008	-9.37%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$975,858	**-$975,858**	$75,518,096	$75,518,096	$35,204,347
39	1.00%	-$754,366	-$162,939	2009	7.96%	7.96%	1.45	11.54%	0.00%	11.54%	$8,608,011	-$917,305	**$7,690,706**	$74,600,791	$83,208,802	$40,879,365
40	1.00%	-$831,640	-$89,515	2010	-0.86%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$921,155	**-$921,155**	$82,287,647	$82,287,647	**$37,841,738**

In the years wherein the S&P 500 produced a negative return and the *Effective Index Credit* was 0.00%, this *Charges+Credits+Bonuses Report* also shows the reduction in account value during these years. In addition, it transparently shows the relationship between the annual charges and the annual multiplier-enhanced credits during positive S&P 500 return years, as well as how the net credits (and net losses) affect the account value over time. This *Charges+Credits+Bonuses Report* of the *Hypothetical Synthetic Asset* uncovers a vitally important truth about the multiplier proposition in this particular case study, especially during this extremely adverse 40-year period.

The *Asset-Based Charge* is 1.00% (column 1) for the 1.45x *Multiplier Bonus* (column 7). In this *Hypothetical Synthetic Asset* depiction, the previous year's *EOY Gross Index Account Value* (column 15 of the previous year) minus 50% of the *Fixed Charges* (column 3) is calculated (since the asset-based charge is a monthly charge applied to the monthly *Accumulated Value*), then the 1.00% asset-based multiplier charge is applied to this value, equaling the *Asset-Based Charges ($)* int that given year. As you can see, these asset-based multiplier charges can be substantial. The question is however, *"Are they worth it?"*

To make it easier for you to reference my commentary, this same ledger will continuously reappear in the two pages to follow.

HYPOTHETICAL SYNTHETIC ASSET

CHARGES + CREDITS + BONUSES

WORST CAGR 40-YEAR PERIOD OUT OF 121 DIFFERENT INDEX PERIODS ANALYZED (STARTING 10/1/1971)

CHARGES & CREDITS

# YEAR	1 ASSET-BASED CHARGES (%)	2 ASSET-BASED CHARGES ($)	3 FIXED CHARGES ($)	4 BACKTESTED YEAR	5 INDEX GROSS RETURN	6 INDEX CREDIT	7 MULTIPLIER BONUS (x)	8 INDEX CREDIT w/ MULTIPLIER	9 PERSISTENCY BONUS (+)	10 TOTAL INDEX CREDIT (%)	11 TOTAL INDEX CREDITS ($)	12 TOTAL CHARGES ($)	13 YEAR-END GAIN/LOSS ($)	14 EOY VALUE AFTER CHARGES B4 CREDIT	15 EOY GROSS INDEX ACCOUNT VALUE	16 EOY NET INDEX ACCOUNT VALUE
1	1.00%	-$12,546	-$190,840	1971	12.42%	8.00%	1.00	8.00%	0.00%	8.00%	$83,729	-$203,386	**-$119,657**	$1,046,614	$1,130,343	-$613,201
2	1.00%	-$21,805	-$199,745	1972	-1.92%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$221,550	**-$221,550**	$2,158,794	$2,158,794	-$788,171
3	1.00%	-$32,046	-$208,447	1973	-41.40%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$240,493	**-$240,493**	$3,168,301	$3,168,301	-$981,646
4	1.00%	-$42,097	-$217,204	1974	32.00%	8.00%	1.45	11.60%	0.00%	11.60%	$482,444	-$259,301	**$223,143**	$4,159,000	$4,641,444	-$710,900
5	1.00%	-$56,784	-$226,155	1975	25.48%	8.00%	1.45	11.60%	0.00%	11.60%	$650,587	-$282,939	**$367,648**	$5,608,505	$6,259,092	-$295,066
6	1.00%	-$72,894	-$239,453	1976	-8.28%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$312,347	**-$312,347**	$7,196,745	$7,196,745	-$558,642
7	1.00%	-$82,216	-$250,241	1977	6.23%	6.23%	1.45	9.03%	0.00%	9.03%	$732,539	-$332,457	**$400,082**	$8,114,288	$8,846,827	-$109,060
8	1.00%	-$98,658	-$262,123	1978	6.61%	6.61%	1.45	9.59%	0.00%	9.59%	$933,441	-$360,781	**$572,661**	$9,736,046	$10,669,487	$513,831
9	1.00%	-$116,820	-$275,072	1979	14.76%	8.00%	1.45	11.60%	0.00%	11.60%	$1,337,201	-$391,892	**$945,310**	$11,527,596	$12,864,797	$1,510,101
10	1.00%	-$138,702	-$289,156	1980	-7.40%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$427,858	**-$427,858**	$13,686,939	$13,686,939	**$1,134,080**
11	1.00%	-$136,178	-$138,260	1981	3.65%	3.65%	1.45	5.29%	0.00%	5.29%	$709,761	-$274,438	**$435,323**	$13,412,501	$14,122,262	$1,622,262
12	1.00%	-$140,506	-$143,237	1982	37.91%	8.00%	1.45	11.60%	0.00%	11.60%	$1,605,268	-$283,743	**$1,321,525**	$13,838,518	$15,443,786	$2,943,786
13	1.00%	-$153,698	-$147,925	1983	0.02%	0.02%	1.45	0.03%	0.00%	0.03%	$3,966	-$301,623	**-$297,657**	$15,142,163	$15,146,129	$2,646,129
14	1.00%	-$150,701	-$152,125	1984	9.62%	8.00%	1.45	11.60%	0.00%	11.60%	$1,721,823	-$302,826	**$1,418,998**	$14,843,304	$16,565,127	$4,065,127
15	1.00%	-$164,873	-$155,753	1985	27.04%	8.00%	1.45	11.60%	0.00%	11.60%	$1,884,362	-$320,626	**$1,563,737**	$16,244,501	$18,128,863	$5,003,863
16	1.00%	-$180,494	-$158,902	1986	39.13%	8.00%	1.45	11.60%	0.00%	11.60%	$2,063,578	-$339,396	**$1,724,182**	$17,789,467	$19,853,046	$6,071,796
17	1.00%	-$197,725	-$161,057	1987	-15.51%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$358,782	**-$358,782**	$19,494,263	$19,494,263	$5,023,951
18	1.00%	-$194,133	-$161,962	1988	28.41%	8.00%	1.45	11.60%	0.00%	11.60%	$2,220,028	-$356,095	**$1,863,933**	$19,138,169	$21,358,196	$6,164,368
19	1.00%	-$212,777	-$160,932	1989	-12.34%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$373,709	**-$373,709**	$20,984,487	$20,984,487	$5,030,967
20	1.00%	-$209,060	-$157,014	1990	26.73%	8.00%	1.45	11.60%	0.00%	11.60%	$2,391,736	-$366,074	**$2,025,662**	$20,618,413	$23,010,149	**$6,258,953**
21	1.00%	-$229,361	-$148,142	1991	7.72%	7.72%	1.45	11.19%	0.00%	11.19%	$2,533,263	-$377,503	**$2,155,760**	$22,632,646	$25,165,909	$7,577,153
22	1.00%	-$250,990	-$133,897	1992	9.84%	8.00%	1.45	11.60%	0.00%	11.60%	$2,874,599	-$384,887	**$2,489,712**	$24,781,022	$27,655,621	$9,187,428
23	1.00%	-$275,988	-$113,654	1993	0.82%	0.82%	1.45	1.19%	0.00%	1.19%	$325,637	-$389,642	**-$64,005**	$27,265,979	$27,591,616	$8,200,013
24	1.00%	-$275,356	-$111,995	1994	26.30%	8.00%	1.45	11.60%	0.00%	11.60%	$3,155,695	-$387,351	**$2,768,344**	$27,204,265	$30,359,960	$9,998,777
25	1.00%	-$303,008	-$118,347	1995	17.61%	8.00%	1.45	11.60%	0.00%	11.60%	$3,472,878	-$421,355	**$3,051,523**	$29,938,605	$33,411,483	$12,032,241
26	1.00%	-$333,875	-$47,954	1996	37.82%	8.00%	1.45	11.60%	0.00%	11.60%	$3,831,440	-$381,829	**$3,449,611**	$33,029,654	$36,861,094	$14,412,890
27	1.00%	-$368,325	-$57,158	1997	7.36%	7.36%	1.45	10.67%	0.00%	10.67%	$3,888,976	-$425,483	**$3,463,492**	$36,435,610	$40,324,586	$16,753,972
28	1.00%	-$402,906	-$68,018	1998	26.13%	8.00%	1.45	11.60%	0.00%	11.60%	$4,623,025	-$470,924	**$4,152,101**	$39,853,662	$44,476,687	$19,727,542
29	1.00%	-$444,363	-$80,799	1999	11.99%	8.00%	1.45	11.60%	0.00%	11.60%	$5,098,377	-$525,162	**$4,573,215**	$43,951,525	$49,049,902	$23,063,300
30	1.00%	-$490,020	-$95,820	2000	-27.54%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$585,840	**-$585,840**	$48,464,062	$48,464,062	**$21,178,130**
31	1.00%	-$484,067	-$114,676	2001	-21.68%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$598,743	**-$598,743**	$47,865,319	$47,865,319	$19,215,090
32	1.00%	-$477,975	-$135,543	2002	22.16%	8.00%	1.45	11.60%	0.00%	11.60%	$5,481,209	-$613,518	**$4,867,690**	$47,251,801	$52,733,009	$22,650,269
33	1.00%	-$526,529	-$160,175	2003	11.91%	8.00%	1.45	11.60%	0.00%	11.60%	$6,037,371	-$686,704	**$5,350,667**	$52,046,305	$58,083,677	$26,496,799
34	1.00%	-$579,888	-$189,667	2004	10.25%	8.00%	1.45	11.60%	0.00%	11.60%	$6,648,438	-$769,555	**$5,878,883**	$57,314,121	$63,962,559	$30,796,338
35	1.00%	-$638,502	-$224,659	2005	8.71%	8.00%	1.45	11.60%	0.00%	11.60%	$7,319,530	-$863,161	**$6,456,369**	$63,099,398	$70,418,928	$35,594,396
36	1.00%	-$702,876	-$262,724	2006	14.29%	8.00%	1.45	11.60%	0.00%	11.60%	$8,056,586	-$965,600	**$7,090,986**	$69,453,328	$77,509,914	$40,944,155
37	1.00%	-$773,889	-$242,072	2007	-23.61%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$1,015,961	**-$1,015,961**	$76,493,954	$76,493,954	$38,099,907
38	1.00%	-$763,880	-$211,978	2008	-9.37%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$975,858	**-$975,858**	$75,518,096	$75,518,096	$35,204,347
39	1.00%	-$754,366	-$162,939	2009	7.96%	7.96%	1.45	11.54%	0.00%	11.54%	$8,608,011	-$917,305	**$7,690,706**	$74,600,791	$83,208,802	$40,879,365
40	1.00%	-$831,640	-$89,515	2010	-0.86%	0.00%	1.45	0.00%	0.00%	0.00%	$0	-$921,155	**-$921,155**	$82,287,647	$82,287,647	**$37,841,738**

Column 5 shows the historical S&P 500 returns each year. The floor and cap are applied, creating the *Pre-Multiplier Index Credit* (column 6), which is then multiplied by the *Multiplier Bonus* (column 7) totaling the *Index Credit w/ Multiplier* (column 8). In some real world *IUL*s, there is an additional persistency bonus (not modeled in this example). The *Total Index Credit (%)* is depicted in column 10. Depending on the *Total Index Credit (%)* each year, the *Total Index Credits ($)* are determined by multiplying column 10 by the *End-Of-Year Value After Charges Before Credit* (column 14).

You will notice that in years wherein the index credit was 0.00%, the *Total Index Credits ($)* column shows a $0 index credit (column 11). You will also notice that in some years, the values in the *Total Index Credits ($)* column (column 11) are greater than the *Total Charges ($)* in column 12, resulting in a *Year-End Gain* (column 13), and in other years, the charges were greater than the credits, resulting in a *Year-End Loss*. These gains/losses are reflected in the *End-Of-Year Gross Index Account Value* (column 15). The total cumulative third-party lender debt (if any exist in that year) is then backed out of column 15, and any internal carrier debt balance incurred by any participating loans is also backed out, creating an *End-Of-Year Net Index Account Value* (column 16).

(Pages 52-53)

HYPOTHETICAL SYNTHETIC ASSET

PARTICIPATING

WORST CAGR 40-YEAR PERIOD OUT OF 121 DIFFERENT INDEX PERIODS ANALYZED (STARTING 10/1/1971)

INTERNAL ACCOUNT LOANS: PARTICIPATING PLR: 5.00%

YEAR	1 3RD PARTY PAYOFF USING PARTICIPATING LOAN	2 INCOME DRAWDOWNS PARTICIPATING LOANS	3 CUMULATIVE ACCRUED INTERNAL LOAN PRINCIPAL	4 ACCRUED INTERNAL LOAN INTEREST	5 INDEX CREDIT AFTER CHARGES	6 CUMULATIVE INTERNAL DEBT BALANCE	7 CUMULATIVE INDEX BALANCE ON PAR LOANS	8 CUMULATIVE LOAN GAIN/LOSS	9 EOY GROSS INDEX ACCOUNT VALUE	10 EOY NET INDEX ACCOUNT VALUE
1	$0	$0	$0	$0	$0	$0	$0	$0	$1,130,343	-$613,201
2	$0	$0	$0	$0	$0	$0	$0	$0	$2,158,794	-$788,171
3	$0	$0	$0	$0	$0	$0	$0	$0	$3,168,301	-$981,646
4	$0	$0	$0	$0	$0	$0	$0	$0	$4,641,444	-$710,900
5	$0	$0	$0	$0	$0	$0	$0	$0	$6,259,092	-$295,066
6	$0	$0	$0	$0	$0	$0	$0	$0	$7,196,745	-$558,642
7	$0	$0	$0	$0	$0	$0	$0	$0	$8,846,827	-$109,060
8	$0	$0	$0	$0	$0	$0	$0	$0	$10,669,487	$513,831
9	$0	$0	$0	$0	$0	$0	$0	$0	$12,864,797	$1,510,101
10	$0	$0	$0	$0	$0	$0	$0	$0	$13,686,939	**$1,134,080**
11	$0	$0	$0	$0	$0	$0	$0	$0	$14,122,262	$1,622,262
12	$0	$0	$0	$0	$0	$0	$0	$0	$15,443,786	$2,943,786
13	$0	$0	$0	$0	$0	$0	$0	$0	$15,146,129	$2,646,129
14	$0	$0	$0	$0	$0	$0	$0	$0	$16,565,127	$4,065,127
15	-$12,500,000	$0	-$12,500,000	-$625,000	$1,421,935	-$13,125,000	$13,679,991	$554,991	$18,128,863	$5,003,863
16	$0	$0	-$13,125,000	-$656,250	$1,557,171	-$13,781,250	$14,981,055	$1,199,805	$19,853,046	$6,071,796
17	$0	$0	-$13,781,250	-$689,063	$0	-$14,470,313	$14,710,319	$240,006	$19,494,263	$5,023,951
18	$0	$0	-$14,470,313	-$723,516	$1,675,227	-$15,193,828	$16,116,837	$923,009	$21,358,196	$6,164,368
19	$0	$0	-$15,193,828	-$759,691	$0	-$15,953,520	$15,834,837	-$118,682	$20,984,487	$5,030,967
20	$0	$0	-$15,953,520	-$797,676	$1,804,797	-$16,751,196	$17,363,396	$612,201	$23,010,149	**$6,258,953**
21	$0	$0	-$16,751,196	-$837,560	$1,911,593	-$17,588,755	$18,990,127	$1,401,371	$25,165,909	$7,577,153
22	$0	$0	-$17,588,755	-$879,438	$2,169,164	-$18,468,193	$20,868,857	$2,400,664	$27,655,621	$9,187,428
23	$0	$0	-$18,468,193	-$923,410	$245,725	-$19,391,603	$20,820,559	$1,428,956	$27,591,616	$8,200,013
24	$0	$0	-$19,391,603	-$969,580	$2,381,279	-$20,361,183	$22,909,544	$2,548,361	$30,359,960	$9,998,777
25	$0	$0	-$20,361,183	-$1,018,059	$2,620,624	-$21,379,242	$25,212,215	$3,832,973	$33,411,483	$12,032,241
26	$0	$0	-$21,379,242	-$1,068,962	$2,891,194	-$22,448,204	$27,815,282	$5,367,078	$36,861,094	$14,412,890
27	$0	$0	-$22,448,204	-$1,122,410	$2,934,610	-$23,570,614	$30,428,824	$6,858,210	$40,324,586	$16,753,972
28	$0	$0	-$23,570,614	-$1,178,531	$3,488,522	-$24,749,145	$33,561,988	$8,812,843	$44,476,687	$19,727,542
29	$0	$0	-$24,749,145	-$1,237,457	$3,847,221	-$25,986,602	$37,012,924	$11,026,322	$49,049,902	$23,063,300
30	$0	$0	-$25,986,602	-$1,299,330	$0	-$27,285,932	$36,570,851	$9,284,918	$48,464,062	**$21,178,130**
31	$0	$0	-$27,285,932	-$1,364,297	$0	-$28,650,229	$36,119,041	$7,468,812	$47,865,319	$19,215,090
32	$0	$0	-$28,650,229	-$1,432,511	$4,136,105	-$30,082,740	$39,792,187	$9,709,446	$52,733,009	$22,650,269
33	$0	$0	-$30,082,740	-$1,504,137	$4,555,784	-$31,586,877	$43,829,786	$12,242,908	$58,083,677	$26,496,799
34	$0	$0	-$31,586,877	-$1,579,344	$5,016,893	-$33,166,221	$48,265,975	$15,099,753	$63,962,559	$30,796,338
35	$0	$0	-$33,166,221	-$1,658,311	$5,523,298	-$34,824,532	$53,137,933	$18,313,401	$70,418,928	$35,594,396
36	$0	$0	-$34,824,532	-$1,741,227	$6,079,478	-$36,565,759	$58,488,772	$21,923,013	$77,509,914	$40,944,155
37	$0	$0	-$36,565,759	-$1,828,288	$0	-$38,394,047	$57,722,131	$19,328,084	$76,493,954	$38,099,907
38	$0	$0	-$38,394,047	-$1,919,702	$0	-$40,313,749	$56,985,752	$16,672,002	$75,518,096	$35,204,347
39	$0	$0	-$40,313,749	-$2,015,687	$6,495,582	-$42,329,437	$62,789,138	$20,459,701	$83,208,802	$40,879,365
40	$0	$0	-$42,329,437	-$2,116,472	$0	-$44,445,909	$62,094,036	$17,648,128	$82,287,647	**$37,841,738**

The above ledger is different than the one on the previous pages. This one depicts the correlation between the *Participating Loan* debt and the *Index Credits* received in the *Index Account* when opting to pay off the third-party lender with a *Participating Loan*. Personally, I think it is important to transparently show clients examples wherein their net account value may decrease in a given year due to policy charges and internal interest charged on participating loans, despite the 0.00% floor. This ledger above shows the $12,500,000 third-party loan being paid off using a *Participating Loan* in year 15 (column 1) during the 40-year period that produced the *Worst Compounded Annual Growth Rate* out of 121 different 40-year periods analyzed. The interest charged using a *Participating Loan Rate (PLR) of* 5.00% is accrued (column 4) and rolled into the *Cumulative Accrued Internal Loan Principal* (column 3).

However that $12,500,000 is moved into a separate index account and is credited using the same S&P 500-correlated floor/cap index crediting method as the primary index account. This separate account receives a positive index credit during years wherein the S&P 500 generates a positive return , and credits $0

during years wherein the S&P 500 produces a negative return (column 5).

The *Cumulative Internal Debt Balance* is depicted in column 6, and the *Cumulative Index Balance On Participating Loans* is depicted in column 7, producing a *Cumulative Loan Gain/Loss* in column 8.

Due to using a participating loan to payoff the third-party lender in year 15, the cumulative internal debt totals -$44,445,909 by year 40 (bottom of column 6).

However, the cumulative gains in the separate index account total $62,094,036 (bottom of column 7), resulting in a net gain of $17,648,128 in year 40 (bottom of column 8) due to the participating loan arrangement during the 40-Year period with the *Worst Compounded Annual Growth Rate* out of 121 different 40-year periods analyzed.

Being able to show a client this type of modeling is invaluable because it shows that a tremendous effort was made in the areas of:

1. Full Transparency.
2. Client Education.
3. Consumer Protection.
4. Explaining How Volatility Can Produce a Range of Different Potential Outcomes.
5. Explaining The Relationship Between Credits and Charges.

Chapter 8
Case Study: First-Dollar Financing

Despite the limitations and inaccuracies of carrier illustrations, the client must be shown the carrier illustration for compliance purposes. Contractually speaking, this is what they are accepting when they purchase the policy – not the outcome, but the depiction of the outcome that represents one of many possible outcomes.

In this chapter, we will evaluate the carrier as-illustrated outcomes using a real-world *Premium Financed IUL,* illustrated using a static index credit of 5.50%. We will also assume a third-party lender payoff in year 15 using a *Participating Loan* with a carrier *Participating Loan Rate* of 5.00%.

At the time this book was written, we actually had access to borrowing rates much lower than what is being illustrated in this case study, but we will use a higher borrowing rate, just to be more conservative.

The third-party lender rate we will use in this case study is based on 3-month Libor + a 1.55% lender spread. At the time this book was written, 3-month Libor was 0.12%, hence the Year-1 borrowing rate is illustrated at 1.67% (0.12%+1.55%=1.67%). The borrowing rate depicted assumes a 30% compounded annual increase on 3-month Libor, resulting in a total borrowing rate of 5.18% by year 14. This is a hypothetical rate increase. Future borrowing rates could be greater or less than what is depicted in this case study.

It is also important to note that the client's age and health rating are significant factors that determine the efficiency of premium financing, for they dictate certain charges within the policy (e.g., mortality cost, cost of insurance, etc). The older and unhealthier the client, the less favorable the economics of premium financing become, and if too unfavorable, I am the first one to recommend that the client should NOT enter a premium financing arrangement.

ALGORITHMICALLY-BASED LIFE INSURANCE SOLUTION

version 426813.98 IUL

FIRST-DOLLAR FINANCING

Health Rating: **PREFERRED**

Initial Gross Policy Face Amount: **$14,601,915**

YEAR	AGE	1 TOTAL POLICY PREMIUMS	2 PREMIUMS PAID BY CLIENT	3 PREMIUMS PAID BY LENDER	4 CUMULATIVE PF LOAN BALANCE	5 FINANCING INTEREST RATE	6 INTEREST DUE	7 INTEREST ACCRUED	8 CLIENT CONTRIBUTION	9 ESTIMATED COLLATERAL	10 HYPOTHETICAL INDEX CREDIT	11 POLICY DRAWDOWNS	12 GROSS ACCUMULATED VALUE	13 POLICY CSV NET OF LOANS	14 DEATH BENEFIT NET OF LOANS	15 DEATH BENEFIT IRR INCLUDING DRAWDOWNS	YEAR	AGE
1	55	$1,250,000	$0	$1,250,000	$1,250,000	1.67%	$20,875	$0	$20,875	$954,642	5.50%	$0	$1,117,457	-$626,087	$14,469,372	69214.36%	1	55
2	56	$1,250,000	$0	$1,250,000	$2,500,000	1.71%	$42,650	$0	$42,650	$954,642	5.50%	$0	$2,302,901	-$644,064	$14,404,816	2426.71%	2	56
3	57	$1,250,000	$0	$1,250,000	$3,750,000	1.75%	$65,730	$0	$65,730	$981,285	5.50%	$0	$3,553,201	-$596,745	$14,405,116	709.60%	3	57
4	58	$1,250,000	$0	$1,250,000	$5,000,000	1.81%	$90,682	$0	$90,682	$945,291	5.50%	$0	$4,872,368	-$479,976	$14,474,283	352.63%	4	58
5	59	$1,250,000	$0	$1,250,000	$6,250,000	1.89%	$118,296	$0	$118,296	$842,580	5.50%	$0	$6,264,505	**-$289,653**	**$14,616,420**	**218.32%**	5	59
6	60	$1,250,000	$0	$1,250,000	$7,500,000	2.00%	$149,666	$0	$149,666	$665,308	5.50%	$0	$7,729,542	-$25,846	$14,831,457	151.72%	6	60
7	61	$1,250,000	$0	$1,250,000	$8,750,000	2.13%	$186,306	$0	$186,306	$419,917	5.50%	$0	$9,274,718	$318,831	$15,126,633	113.06%	7	61
8	62	$1,250,000	$0	$1,250,000	$10,000,000	2.30%	$230,298	$0	$230,298	$95,967	5.50%	$0	$10,903,880	$748,224	$15,505,795	88.24%	8	62
9	63	$1,250,000	$0	$1,250,000	$11,250,000	2.53%	$284,499	$0	$284,499	$0	5.50%	$0	$12,621,144	$1,266,448	$15,973,059	71.11%	9	63
10	64	$1,250,000	$0	$1,250,000	$12,500,000	2.82%	$352,817	$0	$352,817	$0	5.50%	$0	$14,430,812	**$1,877,954**	**$16,532,727**	**58.66%**	10	64
11	65	$0	$0	$0	$12,500,000	3.20%	$400,538	$0	$400,538	$0	5.50%	$0	$15,185,954	$2,685,954	$16,532,727	48.47%	11	65
12	66	$0	$0	$0	$12,500,000	3.70%	$462,574	$0	$462,574	$0	5.50%	$0	$15,983,011	$3,483,011	$16,532,727	40.45%	12	66
13	67	$0	$0	$0	$12,500,000	4.35%	$543,221	$0	$543,221	$0	5.50%	$0	$16,824,914	$4,324,914	$16,532,727	33.95%	13	67
14	68	$0	$0	$0	$12,500,000	5.18%	$648,063	$0	$648,063	$0	5.50%	$0	$17,714,986	$5,214,986	$16,532,727	28.54%	14	68
15	69	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$12,500,000	$18,627,608	**$5,502,608**	**$15,907,727**	**24.24%**	15	69
16	70	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$19,592,173	$5,810,923	$15,251,477	20.74%	16	70
17	71	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$20,612,881	$6,142,569	$14,562,415	17.86%	17	71
18	72	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$21,694,458	$6,500,630	$13,838,899	15.44%	18	72
19	73	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$22,842,646	$6,889,126	$13,079,208	13.39%	19	73
20	74	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$24,064,556	**$7,313,360**	**$12,281,532**	**11.61%**	20	74
21	75	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$25,369,941	$7,781,185	$11,443,972	10.04%	21	75
22	76	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$26,769,596	$8,301,403	$10,564,534	8.63%	22	76
23	77	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$28,275,722	$8,884,119	$10,297,905	7.82%	23	77
24	78	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$29,875,533	$9,514,350	$11,008,126	7.76%	24	78
25	79	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$31,565,667	**$10,186,425**	**$11,764,709**	**7.70%**	25	79
26	80	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$33,433,505	$10,985,301	$12,656,976	7.70%	26	80
27	81	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$35,405,021	$11,834,407	$13,604,658	7.68%	27	81
28	82	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$37,484,733	$12,735,588	$14,609,825	7.67%	28	82
29	83	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$39,677,149	$13,690,547	$15,674,404	7.65%	29	83
30	84	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$41,986,703	**$14,700,771**	**$16,800,106**	**7.63%**	30	84
31	85	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$44,416,394	$15,766,165	$17,986,985	7.60%	31	85
32	86	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$46,971,339	$16,888,599	$19,237,166	7.58%	32	86
33	87	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$49,655,089	$18,068,211	$20,550,966	7.54%	33	87
34	88	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$52,470,234	$19,304,012	$21,927,524	7.51%	34	88
35	89	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$55,418,828	**$20,594,296**	**$23,365,237**	**7.47%**	35	89
36	90	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$58,505,624	$21,939,865	$24,865,146	7.44%	36	90
37	91	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$61,801,515	$23,407,468	$25,879,529	7.32%	37	91
38	92	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$65,329,290	$25,015,540	$26,975,419	7.21%	38	92
39	93	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$69,123,270	$26,793,833	$28,176,298	7.12%	39	93
40	94	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$73,225,709	**$28,779,800**	**$29,512,058**	**7.04%**	40	94

I will be repeating this same ledger over the next several pages with my commentary at the bottom of each page to make it easier for you to reference the numbers in the ledger.

In this case study, the goal is to insure a 55-year old male with a low point death benefit of $10,000,000. In other words, in premium financing, we will typically need to start with a higher face amount because after the third-party lender payoff, the net death benefit will decrease, therefore we will design the premium financing strategy so that the low point net death benefit is equal to or greater than the requested death benefit (in this case, $10,000,000).

(Pages 58-59)

The $1,250,000 annual premiums in this 10-pay design (column 1) are 100% funded by the third-party lender (column 3). The total cumulative borrowed premium from the lender over the 10-year period is $12,500,000 (column 4).

The client is then charged the *Financing Interest Rate* (column 5) on the *Cumulative Premium Financed Loan Balance* (column 4), and pays the lender the *Interest Due* each year (column 6).

In this *First Dollar Financing* design (one of several different financing methods I often use), there is no *Interest Accrued* (column 7), so the total *Client Contribution* each year is solely comprised of the interest payment to the lender (column 8).

ALGORITHMICALLY-BASED LIFE INSURANCE SOLUTION

version 426813.98 IUL

FIRST-DOLLAR FINANCING

Health Rating: **PREFERRED**

Initial Gross Policy Face Amount: **$14,601,915**

YEAR	AGE	1 TOTAL POLICY PREMIUMS	2 PREMIUMS PAID BY CLIENT	3 PREMIUMS PAID BY LENDER	4 CUMULATIVE PF LOAN BALANCE	5 FINANCING INTEREST RATE	6 INTEREST DUE	7 INTEREST ACCRUED	8 CLIENT CONTRIBUTION	9 ESTIMATED COLLATERAL	10 HYPOTHETICAL INDEX CREDIT	11 POLICY DRAWDOWNS	12 GROSS ACCUMULATED VALUE	13 POLICY CSV NET OF LOANS	14 DEATH BENEFIT NET OF LOANS	15 DEATH BENEFIT IRR INCLUDING DRAWDOWNS	YEAR	AGE
1	55	$1,250,000	$0	$1,250,000	$1,250,000	1.67%	$20,875	$0	$20,875	$954,642	5.50%	$0	$1,117,457	-$626,087	$14,469,372	69214.36%	1	55
2	56	$1,250,000	$0	$1,250,000	$2,500,000	1.71%	$42,650	$0	$42,650	$954,642	5.50%	$0	$2,302,901	-$644,064	$14,404,816	2426.71%	2	56
3	57	$1,250,000	$0	$1,250,000	$3,750,000	1.75%	$65,730	$0	$65,730	$981,285	5.50%	$0	$3,553,201	-$596,745	$14,405,116	709.60%	3	57
4	58	$1,250,000	$0	$1,250,000	$5,000,000	1.81%	$90,682	$0	$90,682	$945,291	5.50%	$0	$4,872,368	-$479,976	$14,474,283	352.63%	4	58
5	59	$1,250,000	$0	$1,250,000	$6,250,000	1.89%	$118,296	$0	$118,296	$842,580	5.50%	$0	$6,264,505	**-$289,653**	**$14,616,420**	**218.32%**	5	59
6	60	$1,250,000	$0	$1,250,000	$7,500,000	2.00%	$149,666	$0	$149,666	$665,308	5.50%	$0	$7,729,542	-$25,846	$14,831,457	151.72%	6	60
7	61	$1,250,000	$0	$1,250,000	$8,750,000	2.13%	$186,306	$0	$186,306	$419,917	5.50%	$0	$9,274,718	$318,831	$15,126,633	113.06%	7	61
8	62	$1,250,000	$0	$1,250,000	$10,000,000	2.30%	$230,298	$0	$230,298	$95,967	5.50%	$0	$10,903,880	$748,224	$15,505,795	88.24%	8	62
9	63	$1,250,000	$0	$1,250,000	$11,250,000	2.53%	$284,499	$0	$284,499	$0	5.50%	$0	$12,621,144	$1,266,448	$15,973,059	71.11%	9	63
10	64	$1,250,000	$0	$1,250,000	$12,500,000	2.82%	$352,817	$0	$352,817	$0	5.50%	$0	$14,430,812	**$1,877,954**	**$16,532,727**	**58.66%**	10	64
11	65	$0	$0	$0	$12,500,000	3.20%	$400,538	$0	$400,538	$0	5.50%	$0	$15,185,954	$2,685,954	$16,532,727	48.47%	11	65
12	66	$0	$0	$0	$12,500,000	3.70%	$462,574	$0	$462,574	$0	5.50%	$0	$15,983,011	$3,483,011	$16,532,727	40.45%	12	66
13	67	$0	$0	$0	$12,500,000	4.35%	$543,221	$0	$543,221	$0	5.50%	$0	$16,824,914	$4,324,914	$16,532,727	33.95%	13	67
14	68	$0	$0	$0	$12,500,000	5.18%	$648,063	$0	$648,063	$0	5.50%	$0	$17,714,986	$5,214,986	$16,532,727	28.54%	14	68
15	69	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$12,500,000	$18,627,608	**$5,502,608**	**$15,907,727**	**24.24%**	15	69
16	70	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$19,592,173	$5,810,923	$15,251,477	20.74%	16	70
17	71	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$20,612,881	$6,142,569	$14,562,415	17.86%	17	71
18	72	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$21,694,458	$6,500,630	$13,838,899	15.44%	18	72
19	73	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$22,842,646	$6,889,126	$13,079,208	13.39%	19	73
20	74	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$24,064,556	**$7,313,360**	**$12,281,532**	**11.61%**	20	74
21	75	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$25,369,941	$7,781,185	$11,443,972	10.04%	21	75
22	76	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$26,769,596	$8,301,403	$10,564,534	8.63%	22	76
23	77	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$28,275,722	$8,884,119	$10,297,905	7.82%	23	77
24	78	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$29,875,533	$9,514,350	$11,008,126	7.76%	24	78
25	79	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$31,565,667	**$10,186,425**	**$11,764,709**	**7.70%**	25	79
26	80	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$33,433,505	$10,985,301	$12,656,976	7.70%	26	80
27	81	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$35,405,021	$11,834,407	$13,604,658	7.68%	27	81
28	82	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$37,484,733	$12,735,588	$14,609,825	7.67%	28	82
29	83	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$39,677,149	$13,690,547	$15,674,404	7.65%	29	83
30	84	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$41,986,703	**$14,700,771**	**$16,800,106**	**7.63%**	30	84
31	85	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$44,416,394	$15,766,165	$17,986,985	7.60%	31	85
32	86	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$46,971,339	$16,888,599	$19,237,166	7.58%	32	86
33	87	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$49,655,089	$18,068,211	$20,550,966	7.54%	33	87
34	88	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$52,470,234	$19,304,012	$21,927,524	7.51%	34	88
35	89	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$55,418,828	**$20,594,296**	**$23,365,237**	**7.47%**	35	89
36	90	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$58,505,624	$21,939,865	$24,865,146	7.44%	36	90
37	91	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$61,801,515	$23,407,468	$25,879,529	7.32%	37	91
38	92	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$65,329,290	$25,015,540	$26,975,419	7.21%	38	92
39	93	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$69,123,270	$26,793,833	$28,176,298	7.12%	39	93
40	94	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$73,225,709	**$28,779,800**	**$29,512,058**	**7.04%**	40	94

In premium financing, the policy *Cash Surrender Value (CSV)* is typically less than the outstanding loan balance in the first few years due to surrender charges and other frontloaded insurance charges. This shortfall between the *Cumulative Premium Financed Loan Balance* and the policy gross *Cash Surrender Value* must be collateralized based on each specific lender's requirements. In this case study, the lender gives the gross policy *Cash Surrender Value* a 95% valuation, and a 100% valuation of outside cash collateral posted. Using this calculation, and assuming a 5.50% policy index credit each year, the client would be required to post collateral in years 1-8, with no collateral requirement starting in year 9.

In this case study, we are showing the third-party loan being paid off in year 15 using a *Participating Loan* (column 11). The reason we do not see a decrease in the *Gross Accumulated Value* (column 12) is that the drawdown used to payoff the third-party lender is a *Participating Loan*, so as discussed earlier in this book, the total *Accumulated Value* of the index account *inside* the policy plus the *Accumulated Value* of the index account *outside* the policy continues to receive the index credit each year (in this static depiction, 5.50% after policy charges have been deducted). The *Policy Cash Surrender Value Net Of Loans* (column 13) represents the cash value, net of surrender charges, net of the third-party loan balance, and net of the internal policy participating loan balance.

(Pages 60-61)

ALGORITHMICALLY-BASED LIFE INSURANCE SOLUTION

version 426813.98 IUL

FIRST-DOLLAR FINANCING

Health Rating: **PREFERRED**

Initial Gross Policy Face Amount: **$14,601,915**

YEAR	AGE	1 TOTAL POLICY PREMIUMS	2 PREMIUMS PAID BY CLIENT	3 PREMIUMS PAID BY LENDER	4 CUMULATIVE PF LOAN BALANCE	5 FINANCING INTEREST RATE	6 INTEREST DUE	7 INTEREST ACCRUED	8 CLIENT CONTRIBUTION	9 ESTIMATED COLLATERAL	10 HYPOTHETICAL INDEX CREDIT	11 POLICY DRAWDOWNS	12 GROSS ACCUMULATED VALUE	13 POLICY CSV NET OF LOANS	14 DEATH BENEFIT NET OF LOANS	15 DEATH BENEFIT IRR INCLUDING DRAWDOWNS	YEAR	AGE
1	55	$1,250,000	$0	$1,250,000	$1,250,000	1.67%	$20,875	$0	$20,875	$954,642	5.50%	$0	$1,117,457	-$626,087	$14,469,372	69214.36%	1	55
2	56	$1,250,000	$0	$1,250,000	$2,500,000	1.71%	$42,650	$0	$42,650	$954,642	5.50%	$0	$2,302,901	-$644,064	$14,404,816	2426.71%	2	56
3	57	$1,250,000	$0	$1,250,000	$3,750,000	1.75%	$65,730	$0	$65,730	$981,285	5.50%	$0	$3,553,201	-$596,745	$14,405,116	709.60%	3	57
4	58	$1,250,000	$0	$1,250,000	$5,000,000	1.81%	$90,682	$0	$90,682	$945,291	5.50%	$0	$4,872,368	-$479,976	$14,474,283	352.63%	4	58
5	59	$1,250,000	$0	$1,250,000	$6,250,000	1.89%	$118,296	$0	$118,296	$842,580	5.50%	$0	$6,264,505	**-$289,653**	**$14,616,420**	**218.32%**	5	59
6	60	$1,250,000	$0	$1,250,000	$7,500,000	2.00%	$149,666	$0	$149,666	$665,308	5.50%	$0	$7,729,542	-$25,846	$14,831,457	151.72%	6	60
7	61	$1,250,000	$0	$1,250,000	$8,750,000	2.13%	$186,306	$0	$186,306	$419,917	5.50%	$0	$9,274,718	$318,831	$15,126,633	113.06%	7	61
8	62	$1,250,000	$0	$1,250,000	$10,000,000	2.30%	$230,298	$0	$230,298	$95,967	5.50%	$0	$10,903,880	$748,224	$15,505,795	88.24%	8	62
9	63	$1,250,000	$0	$1,250,000	$11,250,000	2.53%	$284,499	$0	$284,499	$0	5.50%	$0	$12,621,144	$1,266,448	$15,973,059	71.11%	9	63
10	64	$1,250,000	$0	$1,250,000	$12,500,000	2.82%	$352,817	$0	$352,817	$0	5.50%	$0	$14,430,812	**$1,877,954**	**$16,532,727**	**58.66%**	10	64
11	65	$0	$0	$0	$12,500,000	3.20%	$400,538	$0	$400,538	$0	5.50%	$0	$15,185,954	$2,685,954	$16,532,727	48.47%	11	65
12	66	$0	$0	$0	$12,500,000	3.70%	$462,574	$0	$462,574	$0	5.50%	$0	$15,983,011	$3,483,011	$16,532,727	40.45%	12	66
13	67	$0	$0	$0	$12,500,000	4.35%	$543,221	$0	$543,221	$0	5.50%	$0	$16,824,914	$4,324,914	$16,532,727	33.95%	13	67
14	68	$0	$0	$0	$12,500,000	5.18%	$648,063	$0	$648,063	$0	5.50%	$0	$17,714,986	$5,214,986	$16,532,727	28.54%	14	68
15	69	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$12,500,000	$18,627,608	**$5,502,608**	**$15,907,727**	**24.24%**	15	69
16	70	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$19,592,173	$5,810,923	$15,251,477	20.74%	16	70
17	71	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$20,612,881	$6,142,569	$14,562,415	17.86%	17	71
18	72	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$21,694,458	$6,500,630	$13,838,899	15.44%	18	72
19	73	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$22,842,646	$6,889,126	$13,079,208	13.39%	19	73
20	74	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$24,064,556	**$7,313,360**	**$12,281,532**	**11.61%**	20	74
21	75	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$25,369,941	$7,781,185	$11,443,972	10.04%	21	75
22	76	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$26,769,596	$8,301,403	$10,564,534	8.63%	22	76
23	77	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$28,275,722	$8,884,119	$10,297,905	7.82%	23	77
24	78	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$29,875,533	$9,514,350	$11,008,126	7.76%	24	78
25	79	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$31,565,667	**$10,186,425**	**$11,764,709**	**7.70%**	25	79
26	80	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$33,433,505	$10,985,301	$12,656,976	7.70%	26	80
27	81	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$35,405,021	$11,834,407	$13,604,658	7.68%	27	81
28	82	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$37,484,733	$12,735,588	$14,609,825	7.67%	28	82
29	83	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$39,677,149	$13,690,547	$15,674,404	7.65%	29	83
30	84	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$41,986,703	**$14,700,771**	**$16,800,106**	**7.63%**	30	84
31	85	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$44,416,394	$15,766,165	$17,986,985	7.60%	31	85
32	86	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$46,971,339	$16,888,599	$19,237,166	7.58%	32	86
33	87	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$49,655,089	$18,068,211	$20,550,966	7.54%	33	87
34	88	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$52,470,234	$19,304,012	$21,927,524	7.51%	34	88
35	89	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$55,418,828	**$20,594,296**	**$23,365,237**	**7.47%**	35	89
36	90	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$58,505,624	$21,939,865	$24,865,146	7.44%	36	90
37	91	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$61,801,515	$23,407,468	$25,879,529	7.32%	37	91
38	92	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$65,329,290	$25,015,540	$26,975,419	7.21%	38	92
39	93	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$69,123,270	$26,793,833	$28,176,298	7.12%	39	93
40	94	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$73,225,709	**$28,779,800**	**$29,512,058**	**7.04%**	40	94

The *Death Benefit Net Of Loans* hits a low point of $10,297,905 in policy year 23 (column 14), accomplishing the $10,000,000 net death benefit need. The *Death Benefit Net Of Loans* increases thereafter due to the carrier-illustrated 5.50% static index credit outpacing the *Participating Loan Rate* of 5.00% and the assumed policy charges. The inaccuracy of this depiction is due to the assumption that the S&P 500 will yield a positive return every year, resulting in a positive arbitrage between the policy index crediting rate and the *Participating Loan Rate.* We addressed these carrier-illustrated deficiencies in the previous chapter where we took an extremely granular look at how these premium financed *IUL* charges and crediting methods behave during times of volatility in the *Leveraged Hypothetical Synthetic Asset* model.

For death benefit-focused cases, we always offer the client a non-financed *IUL* that satisfies their $10,000,000 death benefit need as an alternative to our premium financed solution. On the following page is a non-financed *IUL* using the exact same product, from the exact same carrier, using the exact same 5.50% index crediting assumption, solving for a level death benefit of $10,000,000.

Both the financed and non-financed policies were designed to last until age 120, then endow.

NON-FINANCED IUL					
	AGE	ANNUAL PREMIUM	CASH VALUE	DEATH BENEFIT	CUMULATIVE COST
1	55	$182,840	$0	$10,000,000	$182,840
2	56	$182,840	$0	$10,000,000	$365,680
3	57	$182,840	$86,415	$10,000,000	$548,520
4	58	$182,840	$249,367	$10,000,000	$731,360
5	59	$182,840	$418,613	$10,000,000	$914,200
6	60	$182,840	$591,870	$10,000,000	$1,097,040
7	61	$182,840	$771,485	$10,000,000	$1,279,880
8	62	$182,840	$957,428	$10,000,000	$1,462,720
9	63	$182,840	$1,149,723	$10,000,000	$1,645,560
10	64	$182,840	$1,348,491	$10,000,000	$1,828,400
11	65	$182,840	$1,558,780	$10,000,000	$2,011,240
12	66	$182,840	$1,739,220	$10,000,000	$2,194,080
13	67	$182,840	$1,926,083	$10,000,000	$2,376,920
14	68	$182,840	$2,119,445	$10,000,000	$2,559,760
15	69	$182,840	$2,319,275	$10,000,000	$2,742,600
16	70	$182,840	$2,525,393	$10,000,000	$2,925,440
17	71	$182,840	$2,737,563	$10,000,000	$3,108,280
18	72	$182,840	$2,955,276	$10,000,000	$3,291,120
19	73	$182,840	$3,177,924	$10,000,000	$3,473,960
20	74	$182,840	$3,404,843	$10,000,000	$3,656,800
21	75	$182,840	$3,636,601	$10,000,000	$3,839,640
22	76	$182,840	$3,872,759	$10,000,000	$4,022,480
23	77	$182,840	$4,113,060	$10,000,000	$4,205,320
24	78	$182,840	$4,357,230	$10,000,000	$4,388,160
25	79	$182,840	$4,605,039	$10,000,000	$4,571,000
26	80	$182,840	$4,909,304	$10,000,000	$4,753,840
27	81	$182,840	$5,222,814	$10,000,000	$4,936,680
28	82	$182,840	$5,546,986	$10,000,000	$5,119,520
29	83	$182,840	$5,883,804	$10,000,000	$5,302,360
30	84	$182,840	$6,235,957	$10,000,000	$5,485,200
31	85	$0	$6,411,766	$10,000,000	$5,485,200
32	86	$0	$6,584,648	$10,000,000	$5,485,200
33	87	$0	$6,753,842	$10,000,000	$5,485,200
34	88	$0	$6,917,895	$10,000,000	$5,485,200
35	89	$0	$7,075,498	$10,000,000	$5,485,200
36	90	$0	$7,229,027	$10,000,000	$5,485,200
37	91	$0	$7,381,440	$10,000,000	$5,485,200
38	92	$0	$7,527,918	$10,000,000	$5,485,200
39	93	$0	$7,669,724	$10,000,000	$5,485,200
40	94	$0	$7,813,532	$10,000,000	$5,485,200
		$5,485,200 TOTAL NET COST (OVER 40 YEARS)			

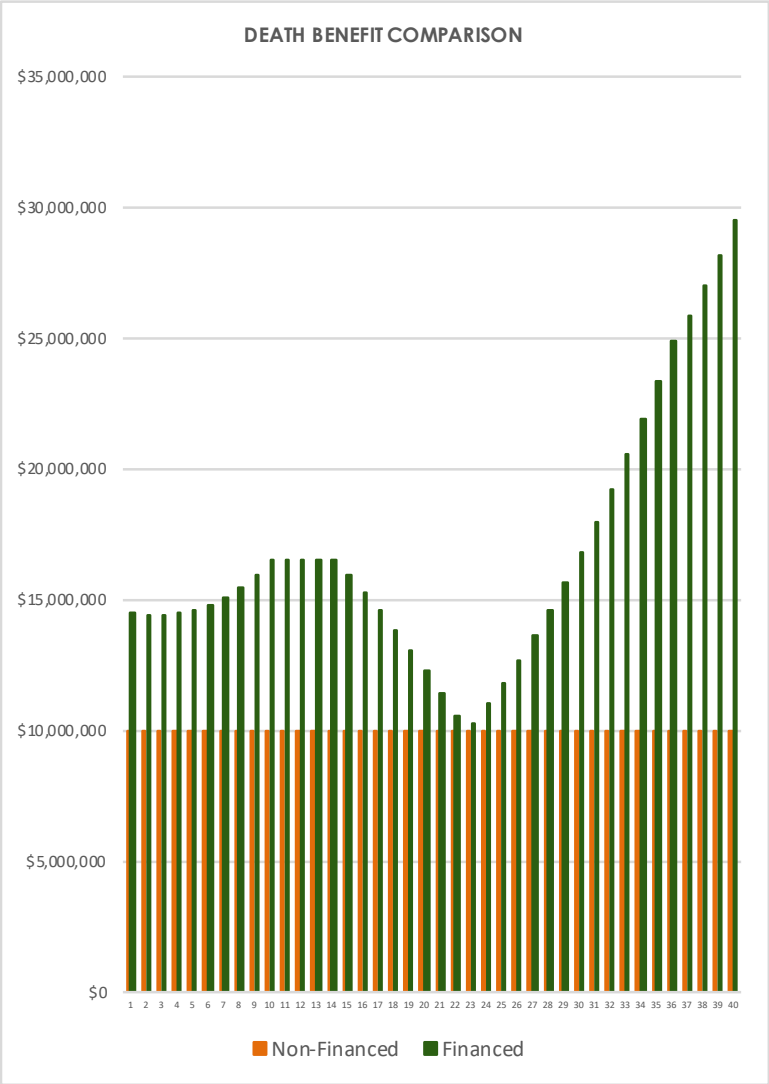
The premium on the non-financed policy is $182,840 per year for thirty years, totaling $5,485,200 in client outlay, versus approximately $3,596,216 in interest payments in the *First-Dollar Financing* design on the next page.

FIRST-DOLLAR FINANCING

	AGE	ANNUAL CONTRIBUTION	CASH VALUE NET OF LOANS	DEATH BENEFIT NET OF LOANS	CUMULATIVE COST
1	55	$20,875	$0	$14,469,372	$20,875
2	56	$42,650	$0	$14,404,816	$63,525
3	57	$65,730	$0	$14,405,116	$129,255
4	58	$90,682	$0	$14,474,283	$219,937
5	59	$118,296	$0	$14,616,420	$338,233
6	60	$149,666	$0	$14,831,457	$487,899
7	61	$186,306	$318,831	$15,126,633	$674,206
8	62	$230,298	$748,224	$15,505,795	$904,504
9	63	$284,499	$1,266,448	$15,973,059	$1,189,002
10	64	$352,817	$1,877,954	$16,532,727	$1,541,820
11	65	$400,538	$2,685,954	$16,532,727	$1,942,358
12	66	$462,574	$3,483,011	$16,532,727	$2,404,932
13	67	$543,221	$4,324,914	$16,532,727	$2,948,153
14	68	$648,063	$5,214,986	$16,532,727	$3,596,216
15	69	$0	$5,502,608	$15,907,727	$3,596,216
16	70	$0	$5,810,923	$15,251,477	$3,596,216
17	71	$0	$6,142,569	$14,562,415	$3,596,216
18	72	$0	$6,500,630	$13,838,899	$3,596,216
19	73	$0	$6,889,126	$13,079,208	$3,596,216
20	74	$0	$7,313,360	$12,281,532	$3,596,216
21	75	$0	$7,781,185	$11,443,972	$3,596,216
22	76	$0	$8,301,403	$10,564,534	$3,596,216
23	77	$0	$8,884,119	$10,297,905	$3,596,216
24	78	$0	$9,514,350	$11,008,126	$3,596,216
25	79	$0	$10,186,425	$11,764,709	$3,596,216
26	80	$0	$10,985,301	$12,656,976	$3,596,216
27	81	$0	$11,834,407	$13,604,658	$3,596,216
28	82	$0	$12,735,588	$14,609,825	$3,596,216
29	83	$0	$13,690,547	$15,674,404	$3,596,216
30	84	$0	$14,700,771	$16,800,106	$3,596,216
31	85	$0	$15,766,165	$17,986,985	$3,596,216
32	86	$0	$16,888,599	$19,237,166	$3,596,216
33	87	$0	$18,068,211	$20,550,966	$3,596,216
34	88	$0	$19,304,012	$21,927,524	$3,596,216
35	89	$0	$20,594,296	$23,365,237	$3,596,216
36	90	$0	$21,939,865	$24,865,146	$3,596,216
37	91	$0	$23,407,468	$25,879,529	$3,596,216
38	92	$0	$25,015,540	$26,975,419	$3,596,216
39	93	$0	$26,793,833	$28,176,298	$3,596,216
40	94	$0	$28,779,800	$29,512,058	$3,596,216

$3,596,216
TOTAL NET COST
(OVER 40 YEARS)

The premium financed arrangement generates an approximate savings of $1,888,984 in total outlay expense, plus the net death benefit in the *First-Dollar Financing* design is substantially greater throughout the life of the policy.



The above graph shows the difference in net death benefit outcomes between the non-financed option and the financed option.

The total savings I alluded to assumes that 3-month Libor only increased at a compounded 30% per year, wherein the third-party lender borrowing rate topped out at 5.18% by year 14.

Now, perhaps you think that borrowing rates will increase at a much more accelerated rate than these assumptions. Whether

that is true or not, there should always be a discussion about this potential issue (and a model depicting this concern) so the client is aware that borrowing rates could trigger substantially greater interest payments required by the lender. Clients need to transparently be shown scenarios wherein detrimental circumstances exist so they can see what challenges may arise.

The ledger below depicts 3-month Libor increasing at a compounded 39% per year each year (instead of only 30%), which results in the third-party lender borrowing rate topping out at 10.23% by year 14 (instead of only 5.18% as depicted earlier).

In this scenario, the client would pay $5,450,710 in total interest payments, which would still be less than the total $5,485,200 of 30-year premium payments in the non-financed *IUL* policy.

YEAR	AGE	TOTAL POLICY PREMIUMS	PREMIUMS PAID BY CLIENT	PREMIUMS PAID BY LENDER	CUMULATIVE PF LOAN BALANCE	FINANCING INTEREST RATE	INTEREST DUE
1	55	$1,250,000	$0	$1,250,000	$1,250,000	1.67%	$20,875
2	56	$1,250,000	$0	$1,250,000	$2,500,000	1.72%	$42,920
3	57	$1,250,000	$0	$1,250,000	$3,750,000	1.78%	$66,819
4	58	$1,250,000	$0	$1,250,000	$5,000,000	1.87%	$93,614
5	59	$1,250,000	$0	$1,250,000	$6,250,000	2.00%	$124,873
6	60	$1,250,000	$0	$1,250,000	$7,500,000	2.17%	$162,950
7	61	$1,250,000	$0	$1,250,000	$8,750,000	2.42%	$211,357
8	62	$1,250,000	$0	$1,250,000	$10,000,000	2.75%	$275,305
9	63	$1,250,000	$0	$1,250,000	$11,250,000	3.22%	$362,502
10	64	$1,250,000	$0	$1,250,000	$12,500,000	3.87%	$484,302
11	65	$0	$0	$0	$12,500,000	4.78%	$597,618
12	66	$0	$0	$0	$12,500,000	6.04%	$755,126
13	67	$0	$0	$0	$12,500,000	7.79%	$974,063
14	68	$0	$0	$0	$12,500,000	10.23%	$1,278,385
		-$12,500,000	**$0**	**-$12,500,000**			**$5,450,710**

It is however possible that borrowing rates might increase even greater than what I have depicted above. I also realize that the past relationship between historical S&P 500 performance and historical Libor rates do not necessarily mean that the future relationship will correlate in the exact same manner, but regardless, I thought it would be interesting to evaluate the history of this past relationship.

On the following page, I will illustrate the historical S&P 500 returns between 1990-2020 and create a hypothetical index

crediting method under the assumption of a 0.00% floor and a 10.00% cap. I will compare these indexed returns to a hypothetical borrowing rate using historical 1-month Libor rates plus a 2.50% lender spread. Currently, none of the lenders I work with charge a 2.50% spread (spreads range between 1.35% and 2.25% depending on the size of the loan), but I will use this larger spread to be more conservative.

During the most recent thirty-one years, the index return (assuming a 0.00% floor and a 10.00% cap) averaged a 1.30% positive spread above the average simulated borrowing rate.

S&P 500		BASE RATE: 1-MONTH LIBOR								
Historical Returns No Dividends		Historical Rate		Lender Spread		Total Lender Rate		Index Return With Floor & Cap		+ or - Spread
2020	16.26%	0.16%	+	2.50%	=	**2.66%**	->	**10.00%**	=	**7.34%**
2019	28.88%	1.76%	+	2.50%	=	**4.26%**	->	**10.00%**	=	**5.74%**
2018	-6.24%	2.52%	+	2.50%	=	**5.02%**	->	**0.00%**	=	-5.02%
2017	19.42%	1.56%	+	2.50%	=	**4.06%**	->	**10.00%**	=	**5.94%**
2016	9.54%	0.77%	+	2.50%	=	**3.27%**	->	**9.54%**	=	**6.27%**
2015	-0.73%	0.43%	+	2.50%	=	**2.93%**	->	**0.00%**	=	-2.93%
2014	11.54%	0.17%	+	2.50%	=	**2.67%**	->	**10.00%**	=	**7.33%**
2013	29.43%	0.17%	+	2.50%	=	**2.67%**	->	**10.00%**	=	**7.33%**
2012	13.29%	0.21%	+	2.50%	=	**2.71%**	->	**10.00%**	=	**7.29%**
2011	0.10%	0.30%	+	2.50%	=	**2.80%**	->	**0.10%**	=	-2.70%
2010	12.63%	0.26%	+	2.50%	=	**2.76%**	->	**10.00%**	=	**7.24%**
2009	23.65%	0.23%	+	2.50%	=	**2.73%**	->	**10.00%**	=	**7.27%**
2008	-38.49%	0.44%	+	2.50%	=	**2.94%**	->	**0.00%**	=	-2.94%
2007	3.52%	4.60%	+	2.50%	=	**7.10%**	->	**3.52%**	=	-3.58%
2006	13.60%	5.32%	+	2.50%	=	**7.82%**	->	**10.00%**	=	**2.18%**
2005	3.00%	4.39%	+	2.50%	=	**6.89%**	->	**3.00%**	=	-3.89%
2004	8.99%	2.40%	+	2.50%	=	**4.90%**	->	**8.99%**	=	**4.09%**
2003	26.38%	1.12%	+	2.50%	=	**3.62%**	->	**10.00%**	=	**6.38%**
2002	23.37%	1.38%	+	2.50%	=	**3.88%**	->	**10.00%**	=	**6.12%**
2001	-13.04%	1.87%	+	2.50%	=	**4.37%**	->	**0.00%**	=	-4.37%
2000	-10.14%	6.56%	+	2.50%	=	**9.06%**	->	**0.00%**	=	-9.06%
1999	19.53%	5.83%	+	2.50%	=	**8.33%**	->	**10.00%**	=	**1.67%**
1998	26.67%	5.06%	+	2.50%	=	**7.56%**	->	**10.00%**	=	**2.44%**
1997	31.01%	5.72%	+	2.50%	=	**8.22%**	->	**10.00%**	=	**1.78%**
1996	20.26%	5.50%	+	2.50%	=	**8.00%**	->	**10.00%**	=	**2.00%**
1995	34.13%	5.69%	+	2.50%	=	**8.19%**	->	**10.00%**	=	**1.81%**
1994	-1.56%	6.00%	+	2.50%	=	**8.50%**	->	**0.00%**	=	-8.50%
1993	7.07%	3.25%	+	2.50%	=	**5.75%**	->	**7.07%**	=	**1.32%**
1992	4.48%	3.31%	+	2.50%	=	**5.81%**	->	**4.48%**	=	-1.33%
1991	26.30%	4.31%	+	2.50%	=	**6.81%**	->	**10.00%**	=	**3.19%**
1990	-6.56%	7.63%	+	2.50%	=	**10.13%**	->	**0.00%**	=	-10.13%
								AVERAGE 31-YEAR SPREAD:		**1.30%**

Some lenders have already moved away from Libor-based loans and are now using the *Secured Overnight Financing Rate (SOFR)*, while others use the *1-Year U.S. Treasury Rate*. On the next page is similar comparison using the *1-Year U.S. Treasury* as

the base rate instead of Libor, using the same 2.50% lender spread. During the same period (1990-2020), the index credit averaged a 1.11% positive spread above the average simulated borrowing rate.

Each lender has different underwriting guidelines, loan terms, and spreads, but for the sake of this comparison, I am using the same 2.50% lender spread on both loan rates (which is substantially larger than most spreads from the lenders I currently work with).

S&P 500		BASE RATE: 1-YEAR U.S. TREASURY									
Historical Returns No Dividends		Historical Rate		Lender Spread		Total Lender Rate		Index Return With Floor & Cap		+ or - Spread
2020	16.26%	1.56%	+	2.50%	=	**4.06%**	->	**10.00%**	=	**5.94%**
2019	28.88%	2.60%	+	2.50%	=	**5.10%**	->	**10.00%**	=	**4.90%**
2018	-6.24%	1.83%	+	2.50%	=	**4.33%**	->	**0.00%**	=	-4.33%
2017	19.42%	0.89%	+	2.50%	=	**3.39%**	->	**10.00%**	=	**6.61%**
2016	9.54%	0.61%	+	2.50%	=	**3.11%**	->	**9.54%**	=	**6.43%**
2015	-0.73%	0.25%	+	2.50%	=	**2.75%**	->	**0.00%**	=	-2.75%
2014	11.54%	0.13%	+	2.50%	=	**2.63%**	->	**10.00%**	=	**7.37%**
2013	29.43%	0.15%	+	2.50%	=	**2.65%**	->	**10.00%**	=	**7.35%**
2012	13.29%	0.12%	+	2.50%	=	**2.62%**	->	**10.00%**	=	**7.38%**
2011	0.10%	0.29%	+	2.50%	=	**2.79%**	->	**0.10%**	=	-2.69%
2010	12.63%	0.45%	+	2.50%	=	**2.95%**	->	**10.00%**	=	**7.05%**
2009	23.65%	0.40%	+	2.50%	=	**2.90%**	->	**10.00%**	=	**7.10%**
2008	-38.49%	3.17%	+	2.50%	=	**5.67%**	->	**0.00%**	=	-5.67%
2007	3.52%	5.00%	+	2.50%	=	**7.50%**	->	**3.52%**	=	-3.98%
2006	13.60%	4.38%	+	2.50%	=	**6.88%**	->	**10.00%**	=	**3.12%**
2005	3.00%	2.79%	+	2.50%	=	**5.29%**	->	**3.00%**	=	-2.29%
2004	8.99%	1.31%	+	2.50%	=	**3.81%**	->	**8.99%**	=	**5.18%**
2003	26.38%	1.42%	+	2.50%	=	**3.92%**	->	**10.00%**	=	**6.08%**
2002	23.37%	2.28%	+	2.50%	=	**4.78%**	->	**10.00%**	=	**5.22%**
2001	-13.04%	5.11%	+	2.50%	=	**7.61%**	->	**0.00%**	=	-7.61%
2000	-10.14%	6.09%	+	2.50%	=	**8.59%**	->	**0.00%**	=	-8.59%
1999	19.53%	4.58%	+	2.50%	=	**7.08%**	->	**10.00%**	=	**2.92%**
1998	26.67%	5.46%	+	2.50%	=	**7.96%**	->	**10.00%**	=	**2.04%**
1997	31.01%	5.63%	+	2.50%	=	**8.13%**	->	**10.00%**	=	**1.87%**
1996	20.26%	5.17%	+	2.50%	=	**7.67%**	->	**10.00%**	=	**2.33%**
1995	34.13%	7.23%	+	2.50%	=	**9.73%**	->	**10.00%**	=	**0.27%**
1994	-1.56%	3.67%	+	2.50%	=	**6.17%**	->	**0.00%**	=	-6.17%
1993	7.07%	3.56%	+	2.50%	=	**6.06%**	->	**7.07%**	=	**1.01%**
1992	4.48%	4.13%	+	2.50%	=	**6.63%**	->	**4.48%**	=	-2.15%
1991	26.30%	6.74%	+	2.50%	=	**9.24%**	->	**10.00%**	=	**0.76%**
1990	-6.56%	7.81%	+	2.50%	=	**10.31%**	->	**0.00%**	=	-10.31%
								AVERAGE 31-YEAR SPREAD:		**1.11%**

Although backtesting comparisons do not give us any guarantees of future symbiotic relationships between borrowing rates and policy index crediting rates, it is interesting to see the historical correlation.

Chapter 9
Estate Planning & Life Insurance

When it comes to estate tax planning, I generally explain to wealthy clients that they have two options:

1. Do nothing and give away 40% of their wealth to the government in the form of estate taxes, or…
2. Use life insurance to pay the estate taxes for them.

If they do nothing, the money they would have spent on life insurance is going to be inherited by their heirs anyway, and then it will be taxed at the estate tax rate at the time of death (currently 40.00%) as will the rest of their wealth, above the estate tax exemption threshold. That is why making the decision to buy life insurance should be based on one simple mathematical equation:

> *If the money you would have spent on life insurance can be invested in an alternative asset, and that asset value (after 40.00% estate taxes) becomes greater than the tax-free death benefit of the life insurance policy, then you should NOT buy the life insurance policy. But if 60% of that alternative asset value is less valuable than the net death benefit, then you SHOULD buy the life insurance. It really is that simple.*

We will model this alternative asset (which we will refer to as a *Hypothetical Equities & Bonds Account*) and calculate its value after the 40% estate tax due.

We will then compare it to the *Premium Financed IUL Proxy* during the 40-year S&P 500 historical period that produced the *Best Compounded Annual Growth Rate* of the 121 different 40-year periods analyzed, AND ALSO during the 40-year S&P 500 historical period that produced the *Worst Compounded Annual Growth Rate* of the 121 different 40-year periods analyzed.

HYPOTHETICAL EQUITIES & BONDS ACCOUNT vs. LEVERAGED HYPOTHETICAL SYNTHETIC ASSET (LHSA)

WORST CAGR 40-YEAR PERIOD OUT OF 121 DIFFERENT INDEX PERIODS ANALYZED (STARTING 10/1/1971)

	EQUITIES	BONDS
<AGE 56:	**70.00%**	**30.00%**
AGE 56+:	**70.00%**	**30.00%**

Current Adjusted Gross Income (AGI):	**$175,000**
Current Income Tax Rate:	**24.00%**
Long-Term Capital Gains Tax Rate:	**15.00%**
State of Residence:	**TX**

% of Equities Taxed at STCG Tax Rates:	**0.00%**
% of Equities Taxed at LTCG Tax Rates:	**100.00%**
% of Bonds Taxed at STCG Tax Rates:	**100.00%**
Estate Tax Rates:	**40.00%**

Advisor Fee:	0.06%
Fund Manager Fee:	0.08%
Broker Dealer Fee:	0.02%
Investment Fees (All-In):	0.16%

# YEAR	AGE	1 ANNUAL INVESTED	2 CALENDAR YEAR	3 GROSS EQUITIES RETURN	4 AFTER-FEE EQUITIES RETURN	5 AFTER-FEE & TAX EQUITIES RETURN	6 CALENDAR YEAR	7 GROSS BOND RETURN	8 AFTER-FEE BOND RETURN	9 AFTER-FEE & TAX BOND RETURN	10 TOTAL CHARGES	11 NET RETURN	12 INCOME DRAWDOWNS	13 AFTER-TAX ACCOUNT VALUE	14 AFTER-ESTATE TAX ACCOUNT VALUE	15 GREATER OF DB & LHSA ACCOUNT VALUE	16 LHSA INCREASE
1	55	$20,875	1971	14.42%	14.25%	12.12%	1971	5.27%	5.11%	3.88%	0.16%	9.65%	$0	$22,888	$13,733	$14,469,372	105261.44%
2	56	$42,920	1972	0.08%	-0.08%	-0.08%	1972	-0.44%	-0.60%	-0.60%	0.16%	-0.24%	$0	$65,653	$39,392	$14,404,816	36468.05%
3	57	$66,819	1973	-39.40%	-39.56%	-39.56%	1973	-2.37%	-2.53%	-2.53%	0.16%	-28.45%	$0	$94,779	$56,867	$14,405,116	25231.04%
4	58	$93,614	1974	34.00%	33.83%	28.76%	1974	-8.16%	-8.33%	-8.33%	0.16%	17.63%	$0	$221,613	$132,968	$14,474,283	10785.57%
5	59	$124,873	1975	27.48%	27.32%	23.22%	1975	-5.07%	-5.24%	-5.24%	0.16%	14.68%	$0	$397,361	$238,417	$14,616,420	6030.62%
6	60	$162,950	1976	-6.28%	-6.44%	-6.44%	1976	9.68%	9.52%	7.24%	0.16%	-2.34%	$0	$547,222	$328,333	$14,831,457	4417.19%
7	61	$211,357	1977	8.23%	8.06%	6.85%	1977	-4.89%	-5.06%	-5.06%	0.16%	3.28%	$0	$783,471	$470,083	$15,126,633	3117.87%
8	62	$275,305	1978	8.61%	8.45%	7.18%	1978	-7.81%	-7.97%	-7.97%	0.16%	2.64%	$0	$1,086,680	$652,008	$15,505,795	2278.16%
9	63	$362,502	1979	16.76%	16.60%	14.11%	1979	-9.51%	-9.68%	-9.68%	0.16%	6.98%	$0	$1,550,273	$930,164	$15,973,059	1617.23%
10	64	$484,302	1980	-5.40%	-5.56%	-5.56%	1980	-14.57%	-14.73%	-14.73%	0.16%	-8.31%	$0	$1,865,515	**$1,119,309**	**$16,532,727**	1377.05%
11	65	$597,618	1981	5.65%	5.49%	4.66%	1981	-1.94%	-2.10%	-2.10%	0.16%	2.64%	$0	$2,528,056	$1,516,834	$16,532,727	989.95%
12	66	$755,126	1982	39.91%	39.75%	33.78%	1982	25.14%	24.98%	18.98%	0.16%	29.34%	$0	$4,246,626	$2,547,976	$16,532,727	548.86%
13	67	$974,063	1983	2.02%	1.86%	1.58%	1983	-0.01%	-0.17%	-0.17%	0.16%	1.05%	$0	$5,275,622	$3,165,373	$16,532,727	422.30%
14	68	$1,278,385	1984	11.62%	11.46%	9.74%	1984	9.04%	8.88%	6.75%	0.16%	8.84%	$0	$7,133,578	$4,280,147	$16,532,727	286.27%
15	69	$0	1985	29.04%	28.88%	24.55%	1985	21.41%	21.25%	16.15%	0.16%	22.03%	$0	$8,704,982	$5,222,989	$15,907,727	204.57%
16	70	$0	1986	41.13%	40.97%	34.82%	1986	21.97%	21.81%	16.57%	0.16%	29.35%	$0	$11,259,595	$6,755,757	$15,251,477	125.76%
17	71	$0	1987	-13.51%	-13.67%	-13.67%	1987	-8.32%	-8.48%	-8.48%	0.16%	-12.12%	$0	$9,895,388	$5,937,233	$14,562,415	145.27%
18	72	$0	1988	30.41%	30.24%	25.71%	1988	3.98%	3.82%	2.90%	0.16%	18.87%	$0	$11,762,325	$7,057,395	$13,838,899	96.09%
19	73	$0	1989	-10.34%	-10.51%	-10.51%	1989	12.27%	12.11%	9.21%	0.16%	-4.59%	$0	$11,222,103	$6,733,262	$13,079,208	94.25%
20	74	$0	1990	28.73%	28.57%	24.28%	1990	0.79%	0.63%	0.48%	0.16%	17.14%	$0	$13,145,878	**$7,887,527**	**$12,281,532**	55.71%
21	75	$0	1991	9.72%	9.56%	8.12%	1991	10.33%	10.17%	7.73%	0.16%	8.01%	$0	$14,198,250	$8,518,950	$11,443,972	34.34%
22	76	$0	1992	11.84%	11.68%	9.93%	1992	6.15%	5.98%	4.55%	0.16%	8.32%	$0	$15,378,912	$9,227,347	$10,564,534	14.49%
23	77	$0	1993	2.82%	2.66%	2.26%	1993	10.94%	10.77%	8.19%	0.16%	4.04%	$0	$16,000,261	$9,600,157	$10,297,905	7.27%
24	78	$0	1994	28.30%	28.14%	23.92%	1994	-10.37%	-10.54%	-10.54%	0.16%	13.58%	$0	$18,173,474	$10,904,084	$11,008,126	0.95%
25	79	$0	1995	19.61%	19.45%	16.53%	1995	20.11%	19.95%	15.16%	0.16%	16.12%	$0	$21,103,133	$12,661,880	$12,032,241	-4.97%
26	80	$0	1996	39.82%	39.66%	33.71%	1996	-1.46%	-1.62%	-1.62%	0.16%	23.11%	$0	$25,980,093	$15,588,056	$14,412,890	-7.54%
27	81	$0	1997	9.36%	9.20%	7.82%	1997	7.43%	7.27%	5.52%	0.16%	7.13%	$0	$27,832,487	$16,699,492	$16,753,972	0.33%
28	82	$0	1998	28.13%	27.96%	23.77%	1998	13.16%	13.00%	9.88%	0.16%	19.60%	$0	$33,288,484	$19,973,090	$19,727,542	-1.23%
29	83	$0	1999	13.99%	13.83%	11.75%	1999	-10.22%	-10.38%	-10.38%	0.16%	5.11%	$0	$34,990,726	$20,994,436	$23,063,300	9.85%
30	84	$0	2000	-25.54%	-25.70%	-25.70%	2000	12.84%	12.68%	9.64%	0.16%	-15.10%	$0	$29,707,977	**$17,824,786**	**$21,178,130**	18.81%
31	85	$0	2001	-19.68%	-19.84%	-19.84%	2001	2.67%	2.51%	1.91%	0.16%	-13.32%	$0	$25,751,948	$15,451,169	$19,215,090	24.36%
32	86	$0	2002	24.16%	24.00%	20.40%	2002	13.32%	13.16%	10.00%	0.16%	17.28%	$0	$30,201,981	$18,121,189	$22,650,269	24.99%
33	87	$0	2003	13.91%	13.75%	11.68%	2003	-1.85%	-2.01%	-2.01%	0.16%	7.58%	$0	$32,489,796	$19,493,877	$26,496,799	35.92%
34	88	$0	2004	12.25%	12.09%	10.27%	2004	1.77%	1.60%	1.22%	0.16%	7.56%	$0	$34,945,161	$20,967,096	$30,796,338	46.88%
35	89	$0	2005	10.71%	10.55%	8.97%	2005	-0.51%	-0.67%	-0.67%	0.16%	6.08%	$0	$37,068,281	$22,240,968	$35,594,396	60.04%
36	90	$0	2006	16.29%	16.13%	13.71%	2006	-1.23%	-1.39%	-1.39%	0.16%	9.18%	$0	$40,471,242	$24,282,745	$40,944,155	68.61%
37	91	$0	2007	-21.61%	-21.77%	-21.77%	2007	7.15%	6.99%	5.31%	0.16%	-13.64%	$0	$34,949,776	$20,969,865	$38,099,907	81.69%
38	92	$0	2008	-7.37%	-7.53%	-7.53%	2008	15.66%	15.50%	11.78%	0.16%	-1.74%	$0	$34,342,290	$20,605,374	$35,204,347	70.85%
39	93	$0	2009	9.96%	9.80%	8.33%	2009	-10.80%	-10.96%	-10.96%	0.16%	2.54%	$0	$35,214,591	$21,128,755	$40,879,365	93.48%
40	94	$0	2010	1.14%	0.98%	0.83%	2010	6.71%	6.55%	4.98%	0.16%	2.08%	$0	$35,946,099	**$21,567,660**	**$37,841,738**	75.46%

Average Equities Return: **10.02%** **Average T-Bond Return:** **3.46%** **Average Net Portfolio Return:** **6.04%**

WORST 40

In this *Hypothetical Equities & Bonds Account*, 70% of the portfolio uses historical S&P 500 returns plus an additional 2.00% bonus added as a hypothetical S&P 500 dividend, and 30% of the portfolio uses historical 10-year T-Bond returns. The all-in investment fee in this model is only 0.16%, which is incredibly low.

(Pages 72-73)

The S&P returns are only taxed at 15.00% and the 10-year T-Bonds are only taxed at 24.00% (which assumes that the client has magically reduced their taxable income down to warrant such low tax rates). And finally, the account balance is taxed at 40.00% upon generational transfer to represent estate taxes. To make it easier for you to reference the ledger while reading my commentary, I will repeat the above ledger in the following pages.

HYPOTHETICAL EQUITIES & BONDS ACCOUNT vs. LEVERAGED HYPOTHETICAL SYNTHETIC ASSET (LHSA)

WORST CAGR 40-YEAR PERIOD OUT OF 121 DIFFERENT INDEX PERIODS ANALYZED (STARTING 10/1/1971)

	EQUITIES	BONDS
<AGE 56:	**70.00%**	**30.00%**
AGE 56+:	**70.00%**	**30.00%**

Current Adjusted Gross Income (AGI):	**$175,000**
Current Income Tax Rate:	**24.00%**
Long-Term Capital Gains Tax Rate:	**15.00%**
State of Residence:	**TX**

% of Equities Taxed at STCG Tax Rates:	**0.00%**
% of Equities Taxed at LTCG Tax Rates:	**100.00%**
% of Bonds Taxed at STCG Tax Rates:	**100.00%**
Estate Tax Rates:	**40.00%**

Advisor Fee:	0.06%
Fund Manager Fee:	0.08%
Broker Dealer Fee:	0.02%
Investment Fees (All-In):	0.16%

# YEAR	AGE	1 ANNUAL INVESTED	2 CALENDAR YEAR	3 GROSS EQUITIES RETURN	4 AFTER-FEE EQUITIES RETURN	5 AFTER-FEE & TAX EQUITIES RETURN	6 CALENDAR YEAR	7 GROSS BOND RETURN	8 AFTER-FEE BOND RETURN	9 AFTER-FEE & TAX BOND RETURN	10 TOTAL CHARGES	11 NET RETURN	12 INCOME DRAWDOWNS	13 AFTER-TAX ACCOUNT VALUE	14 AFTER-ESTATE TAX ACCOUNT VALUE	15 GREATER OF DB & LHSA ACCOUNT VALUE	16 LHSA INCREASE
1	55	$20,875	1971	14.42%	14.25%	12.12%	1971	5.27%	5.11%	3.88%	0.16%	9.65%	$0	$22,888	$13,733	$14,469,372	105261.44%
2	56	$42,920	1972	0.08%	-0.08%	-0.08%	1972	-0.44%	-0.60%	-0.60%	0.16%	-0.24%	$0	$65,653	$39,392	$14,404,816	36468.05%
3	57	$66,819	1973	-39.40%	-39.56%	-39.56%	1973	-2.37%	-2.53%	-2.53%	0.16%	-28.45%	$0	$94,779	$56,867	$14,405,116	25231.04%
4	58	$93,614	1974	34.00%	33.83%	28.76%	1974	-8.16%	-8.33%	-8.33%	0.16%	17.63%	$0	$221,613	$132,968	$14,474,283	10785.57%
5	59	$124,873	1975	27.48%	27.32%	23.22%	1975	-5.07%	-5.24%	-5.24%	0.16%	14.68%	$0	$397,361	$238,417	$14,616,420	6030.62%
6	60	$162,950	1976	-6.28%	-6.44%	-6.44%	1976	9.68%	9.52%	7.24%	0.16%	-2.34%	$0	$547,222	$328,333	$14,831,457	4417.19%
7	61	$211,357	1977	8.23%	8.06%	6.85%	1977	-4.89%	-5.06%	-5.06%	0.16%	3.28%	$0	$783,471	$470,083	$15,126,633	3117.87%
8	62	$275,305	1978	8.61%	8.45%	7.18%	1978	-7.81%	-7.97%	-7.97%	0.16%	2.64%	$0	$1,086,680	$652,008	$15,505,795	2278.16%
9	63	$362,502	1979	16.76%	16.60%	14.11%	1979	-9.51%	-9.68%	-9.68%	0.16%	6.98%	$0	$1,550,273	$930,164	$15,973,059	1617.23%
10	64	$484,302	1980	-5.40%	-5.56%	-5.56%	1980	-14.57%	-14.73%	-14.73%	0.16%	-8.31%	$0	$1,865,515	**$1,119,309**	**$16,532,727**	1377.05%
11	65	$597,618	1981	5.65%	5.49%	4.66%	1981	-1.94%	-2.10%	-2.10%	0.16%	2.64%	$0	$2,528,056	$1,516,834	$16,532,727	989.95%
12	66	$755,126	1982	39.91%	39.75%	33.78%	1982	25.14%	24.98%	18.98%	0.16%	29.34%	$0	$4,246,626	$2,547,976	$16,532,727	548.86%
13	67	$974,063	1983	2.02%	1.86%	1.58%	1983	-0.01%	-0.17%	-0.17%	0.16%	1.05%	$0	$5,275,622	$3,165,373	$16,532,727	422.30%
14	68	$1,278,385	1984	11.62%	11.46%	9.74%	1984	9.04%	8.88%	6.75%	0.16%	8.84%	$0	$7,133,578	$4,280,147	$16,532,727	286.27%
15	69	$0	1985	29.04%	28.88%	24.55%	1985	21.41%	21.25%	16.15%	0.16%	22.03%	$0	$8,704,982	$5,222,989	$15,907,727	204.57%
16	70	$0	1986	41.13%	40.97%	34.82%	1986	21.97%	21.81%	16.57%	0.16%	29.35%	$0	$11,259,595	$6,755,757	$15,251,477	125.76%
17	71	$0	1987	-13.51%	-13.67%	-13.67%	1987	-8.32%	-8.48%	-8.48%	0.16%	-12.12%	$0	$9,895,388	$5,937,233	$14,562,415	145.27%
18	72	$0	1988	30.41%	30.24%	25.71%	1988	3.98%	3.82%	2.90%	0.16%	18.87%	$0	$11,762,325	$7,057,395	$13,838,899	96.09%
19	73	$0	1989	-10.34%	-10.51%	-10.51%	1989	12.27%	12.11%	9.21%	0.16%	-4.59%	$0	$11,222,103	$6,733,262	$13,079,208	94.25%
20	74	$0	1990	28.73%	28.57%	24.28%	1990	0.79%	0.63%	0.48%	0.16%	17.14%	$0	$13,145,878	**$7,887,527**	**$12,281,532**	55.71%
21	75	$0	1991	9.72%	9.56%	8.12%	1991	10.33%	10.17%	7.73%	0.16%	8.01%	$0	$14,198,250	$8,518,950	$11,443,972	34.34%
22	76	$0	1992	11.84%	11.68%	9.93%	1992	6.15%	5.98%	4.55%	0.16%	8.32%	$0	$15,378,912	$9,227,347	$10,564,534	14.49%
23	77	$0	1993	2.82%	2.66%	2.26%	1993	10.94%	10.77%	8.19%	0.16%	4.04%	$0	$16,000,261	$9,600,157	$10,297,905	7.27%
24	78	$0	1994	28.30%	28.14%	23.92%	1994	-10.37%	-10.54%	-10.54%	0.16%	13.58%	$0	$18,173,474	$10,904,084	$11,008,126	0.95%
25	79	$0	1995	19.61%	19.45%	16.53%	1995	20.11%	19.95%	15.16%	0.16%	16.12%	$0	$21,103,133	$12,661,880	$12,032,241	-4.97%
26	80	$0	1996	39.82%	39.66%	33.71%	1996	-1.46%	-1.62%	-1.62%	0.16%	23.11%	$0	$25,980,093	$15,588,056	$14,412,890	-7.54%
27	81	$0	1997	9.36%	9.20%	7.82%	1997	7.43%	7.27%	5.52%	0.16%	7.13%	$0	$27,832,487	$16,699,492	$16,753,972	0.33%
28	82	$0	1998	28.13%	27.96%	23.77%	1998	13.16%	13.00%	9.88%	0.16%	19.60%	$0	$33,288,484	$19,973,090	$19,727,542	-1.23%
29	83	$0	1999	13.99%	13.83%	11.75%	1999	-10.22%	-10.38%	-10.38%	0.16%	5.11%	$0	$34,990,726	$20,994,436	$23,063,300	9.85%
30	84	$0	2000	-25.54%	-25.70%	-25.70%	2000	12.84%	12.68%	9.64%	0.16%	-15.10%	$0	$29,707,977	**$17,824,786**	**$21,178,130**	18.81%
31	85	$0	2001	-19.68%	-19.84%	-19.84%	2001	2.67%	2.51%	1.91%	0.16%	-13.32%	$0	$25,751,948	$15,451,169	$19,215,090	24.36%
32	86	$0	2002	24.16%	24.00%	20.40%	2002	13.32%	13.16%	10.00%	0.16%	17.28%	$0	$30,201,981	$18,121,189	$22,650,269	24.99%
33	87	$0	2003	13.91%	13.75%	11.68%	2003	-1.85%	-2.01%	-2.01%	0.16%	7.58%	$0	$32,489,796	$19,493,877	$26,496,799	35.92%
34	88	$0	2004	12.25%	12.09%	10.27%	2004	1.77%	1.60%	1.22%	0.16%	7.56%	$0	$34,945,161	$20,967,096	$30,796,338	46.88%
35	89	$0	2005	10.71%	10.55%	8.97%	2005	-0.51%	-0.67%	-0.67%	0.16%	6.08%	$0	$37,068,281	$22,240,968	$35,594,396	60.04%
36	90	$0	2006	16.29%	16.13%	13.71%	2006	-1.23%	-1.39%	-1.39%	0.16%	9.18%	$0	$40,471,242	$24,282,745	$40,944,155	68.61%
37	91	$0	2007	-21.61%	-21.77%	-21.77%	2007	7.15%	6.99%	5.31%	0.16%	-13.64%	$0	$34,949,776	$20,969,865	$38,099,907	81.69%
38	92	$0	2008	-7.37%	-7.53%	-7.53%	2008	15.66%	15.50%	11.78%	0.16%	-1.74%	$0	$34,342,290	$20,605,374	$35,204,347	70.85%
39	93	$0	2009	9.96%	9.80%	8.33%	2009	-10.80%	-10.96%	-10.96%	0.16%	2.54%	$0	$35,214,591	$21,128,755	$40,879,365	93.48%
40	94	$0	2010	1.14%	0.98%	0.83%	2010	6.71%	6.55%	4.98%	0.16%	2.08%	$0	$35,946,099	**$21,567,660**	**$37,841,738**	75.46%

Average Equities Return: **10.02%** **Average T-Bond Return:** **3.46%** **Average Net Portfolio Return:** **6.04%**

WORST 40

The purpose of this model is to compare the value of this hypothetical non-insurance-based asset to the *Premium Financed IUL Proxy*. In column 15, I have taken the greater of the *Net Account Value* in the *Leveraged Hypothetical Synthetic* Asset during the same backtested period and the as-illustrated death benefit (as depicted in the carrier illustration).

(Pages 74-75)

Column 16 shows the percentage of greater return over the *Hypothetical Equities & Bonds Account*. In years 25, 26 and 28, the ROI is slightly less than the *Hypothetical Equities & Bonds Account*, however in all other years, the ROI is significantly greater. Keep in mind, this comparison assumes a 24.00% short-term capital gains tax rate and only a 15% long-term capital gains tax rate, as well as 0.16% all-in investment fee.

HYPOTHETICAL EQUITIES & BONDS ACCOUNT vs. LEVERAGED HYPOTHETICAL SYNTHETIC ASSET (LHSA)

WORST CAGR 40-YEAR PERIOD OUT OF 121 DIFFERENT INDEX PERIODS ANALYZED (STARTING 10/1/1971)

	EQUITIES	BONDS
<AGE 56:	**70.00%**	**30.00%**
AGE 56+:	**70.00%**	**30.00%**

Current Adjusted Gross Income (AGI):	**$175,000**
Current Income Tax Rate:	**24.00%**
Long-Term Capital Gains Tax Rate:	**15.00%**
State of Residence:	**TX**

% of Equities Taxed at STCG Tax Rates:	**0.00%**
% of Equities Taxed at LTCG Tax Rates:	**100.00%**
% of Bonds Taxed at STCG Tax Rates:	**100.00%**
Estate Tax Rates:	**40.00%**

Advisor Fee:	0.06%
Fund Manager Fee:	0.08%
Broker Dealer Fee:	0.02%
Investment Fees (All-In):	0.16%

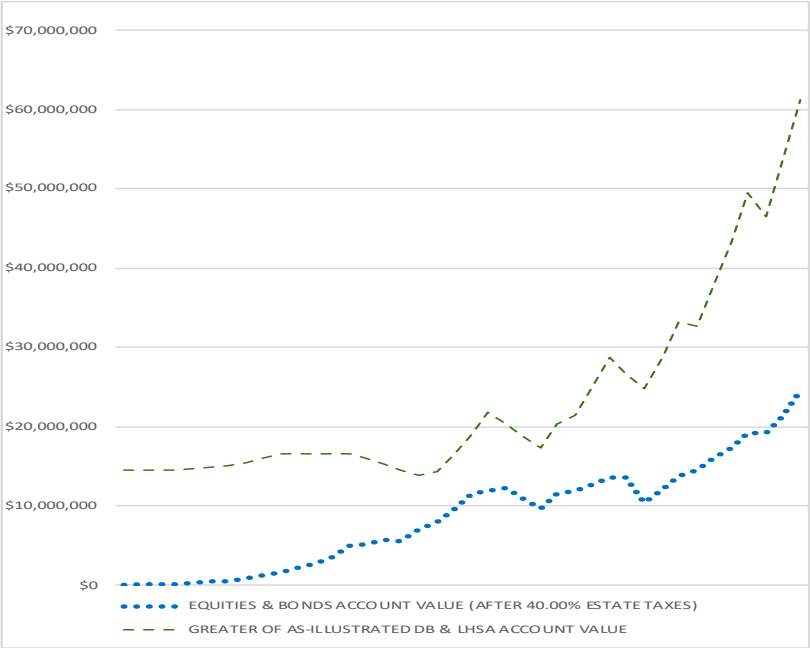
# YEAR	AGE	1 ANNUAL INVESTED	2 CALENDAR YEAR	3 GROSS EQUITIES RETURN	4 AFTER-FEE EQUITIES RETURN	5 AFTER-FEE & TAX EQUITIES RETURN	6 CALENDAR YEAR	7 GROSS BOND RETURN	8 AFTER-FEE BOND RETURN	9 AFTER-FEE & TAX BOND RETURN	10 TOTAL CHARGES	11 NET RETURN	12 INCOME DRAWDOWNS	13 AFTER-TAX ACCOUNT VALUE	14 AFTER-ESTATE TAX ACCOUNT VALUE	15 GREATER OF DB & LHSA ACCOUNT VALUE	16 LHSA INCREASE
1	55	$20,875	1971	14.42%	14.25%	12.12%	1971	5.27%	5.11%	3.88%	0.16%	9.65%	$0	$22,888	$13,733	$14,469,372	105261.44%
2	56	$42,920	1972	0.08%	-0.08%	-0.08%	1972	-0.44%	-0.60%	-0.60%	0.16%	-0.24%	$0	$65,653	$39,392	$14,404,816	36468.05%
3	57	$66,819	1973	-39.40%	-39.56%	-39.56%	1973	-2.37%	-2.53%	-2.53%	0.16%	-28.45%	$0	$94,779	$56,867	$14,405,116	25231.04%
4	58	$93,614	1974	34.00%	33.83%	28.76%	1974	-8.16%	-8.33%	-8.33%	0.16%	17.63%	$0	$221,613	$132,968	$14,474,283	10785.57%
5	59	$124,873	1975	27.48%	27.32%	23.22%	1975	-5.07%	-5.24%	-5.24%	0.16%	14.68%	$0	$397,361	$238,417	$14,616,420	6030.62%
6	60	$162,950	1976	-6.28%	-6.44%	-6.44%	1976	9.68%	9.52%	7.24%	0.16%	-2.34%	$0	$547,222	$328,333	$14,831,457	4417.19%
7	61	$211,357	1977	8.23%	8.06%	6.85%	1977	-4.89%	-5.06%	-5.06%	0.16%	3.28%	$0	$783,471	$470,083	$15,126,633	3117.87%
8	62	$275,305	1978	8.61%	8.45%	7.18%	1978	-7.81%	-7.97%	-7.97%	0.16%	2.64%	$0	$1,086,680	$652,008	$15,505,795	2278.16%
9	63	$362,502	1979	16.76%	16.60%	14.11%	1979	-9.51%	-9.68%	-9.68%	0.16%	6.98%	$0	$1,550,273	$930,164	$15,973,059	1617.23%
10	64	$484,302	1980	-5.40%	-5.56%	-5.56%	1980	-14.57%	-14.73%	-14.73%	0.16%	-8.31%	$0	$1,865,515	**$1,119,309**	**$16,532,727**	1377.05%
11	65	$597,618	1981	5.65%	5.49%	4.66%	1981	-1.94%	-2.10%	-2.10%	0.16%	2.64%	$0	$2,528,056	$1,516,834	$16,532,727	989.95%
12	66	$755,126	1982	39.91%	39.75%	33.78%	1982	25.14%	24.98%	18.98%	0.16%	29.34%	$0	$4,246,626	$2,547,976	$16,532,727	548.86%
13	67	$974,063	1983	2.02%	1.86%	1.58%	1983	-0.01%	-0.17%	-0.17%	0.16%	1.05%	$0	$5,275,622	$3,165,373	$16,532,727	422.30%
14	68	$1,278,385	1984	11.62%	11.46%	9.74%	1984	9.04%	8.88%	6.75%	0.16%	8.84%	$0	$7,133,578	$4,280,147	$16,532,727	286.27%
15	69	$0	1985	29.04%	28.88%	24.55%	1985	21.41%	21.25%	16.15%	0.16%	22.03%	$0	$8,704,982	$5,222,989	$15,907,727	204.57%
16	70	$0	1986	41.13%	40.97%	34.82%	1986	21.97%	21.81%	16.57%	0.16%	29.35%	$0	$11,259,595	$6,755,757	$15,251,477	125.76%
17	71	$0	1987	-13.51%	-13.67%	-13.67%	1987	-8.32%	-8.48%	-8.48%	0.16%	-12.12%	$0	$9,895,388	$5,937,233	$14,562,415	145.27%
18	72	$0	1988	30.41%	30.24%	25.71%	1988	3.98%	3.82%	2.90%	0.16%	18.87%	$0	$11,762,325	$7,057,395	$13,838,899	96.09%
19	73	$0	1989	-10.34%	-10.51%	-10.51%	1989	12.27%	12.11%	9.21%	0.16%	-4.59%	$0	$11,222,103	$6,733,262	$13,079,208	94.25%
20	74	$0	1990	28.73%	28.57%	24.28%	1990	0.79%	0.63%	0.48%	0.16%	17.14%	$0	$13,145,878	**$7,887,527**	**$12,281,532**	55.71%
21	75	$0	1991	9.72%	9.56%	8.12%	1991	10.33%	10.17%	7.73%	0.16%	8.01%	$0	$14,198,250	$8,518,950	$11,443,972	34.34%
22	76	$0	1992	11.84%	11.68%	9.93%	1992	6.15%	5.98%	4.55%	0.16%	8.32%	$0	$15,378,912	$9,227,347	$10,564,534	14.49%
23	77	$0	1993	2.82%	2.66%	2.26%	1993	10.94%	10.77%	8.19%	0.16%	4.04%	$0	$16,000,261	$9,600,157	$10,297,905	7.27%
24	78	$0	1994	28.30%	28.14%	23.92%	1994	-10.37%	-10.54%	-10.54%	0.16%	13.58%	$0	$18,173,474	$10,904,084	$11,008,126	0.95%
25	79	$0	1995	19.61%	19.45%	16.53%	1995	20.11%	19.95%	15.16%	0.16%	16.12%	$0	$21,103,133	$12,661,880	$12,032,241	-4.97%
26	80	$0	1996	39.82%	39.66%	33.71%	1996	-1.46%	-1.62%	-1.62%	0.16%	23.11%	$0	$25,980,093	$15,588,056	$14,412,890	-7.54%
27	81	$0	1997	9.36%	9.20%	7.82%	1997	7.43%	7.27%	5.52%	0.16%	7.13%	$0	$27,832,487	$16,699,492	$16,753,972	0.33%
28	82	$0	1998	28.13%	27.96%	23.77%	1998	13.16%	13.00%	9.88%	0.16%	19.60%	$0	$33,288,484	$19,973,090	$19,727,542	-1.23%
29	83	$0	1999	13.99%	13.83%	11.75%	1999	-10.22%	-10.38%	-10.38%	0.16%	5.11%	$0	$34,990,726	$20,994,436	$23,063,300	9.85%
30	84	$0	2000	-25.54%	-25.70%	-25.70%	2000	12.84%	12.68%	9.64%	0.16%	-15.10%	$0	$29,707,977	**$17,824,786**	**$21,178,130**	18.81%
31	85	$0	2001	-19.68%	-19.84%	-19.84%	2001	2.67%	2.51%	1.91%	0.16%	-13.32%	$0	$25,751,948	$15,451,169	$19,215,090	24.36%
32	86	$0	2002	24.16%	24.00%	20.40%	2002	13.32%	13.16%	10.00%	0.16%	17.28%	$0	$30,201,981	$18,121,189	$22,650,269	24.99%
33	87	$0	2003	13.91%	13.75%	11.68%	2003	-1.85%	-2.01%	-2.01%	0.16%	7.58%	$0	$32,489,796	$19,493,877	$26,496,799	35.92%
34	88	$0	2004	12.25%	12.09%	10.27%	2004	1.77%	1.60%	1.22%	0.16%	7.56%	$0	$34,945,161	$20,967,096	$30,796,338	46.88%
35	89	$0	2005	10.71%	10.55%	8.97%	2005	-0.51%	-0.67%	-0.67%	0.16%	6.08%	$0	$37,068,281	$22,240,968	$35,594,396	60.04%
36	90	$0	2006	16.29%	16.13%	13.71%	2006	-1.23%	-1.39%	-1.39%	0.16%	9.18%	$0	$40,471,242	$24,282,745	$40,944,155	68.61%
37	91	$0	2007	-21.61%	-21.77%	-21.77%	2007	7.15%	6.99%	5.31%	0.16%	-13.64%	$0	$34,949,776	$20,969,865	$38,099,907	81.69%
38	92	$0	2008	-7.37%	-7.53%	-7.53%	2008	15.66%	15.50%	11.78%	0.16%	-1.74%	$0	$34,342,290	$20,605,374	$35,204,347	70.85%
39	93	$0	2009	9.96%	9.80%	8.33%	2009	-10.80%	-10.96%	-10.96%	0.16%	2.54%	$0	$35,214,591	$21,128,755	$40,879,365	93.48%
40	94	$0	2010	1.14%	0.98%	0.83%	2010	6.71%	6.55%	4.98%	0.16%	2.08%	$0	$35,946,099	**$21,567,660**	**$37,841,738**	75.46%

Average Equities Return: **10.02%** **Average T-Bond Return:** **3.46%** **Average Net Portfolio Return:** **6.04%** **WORST 40**

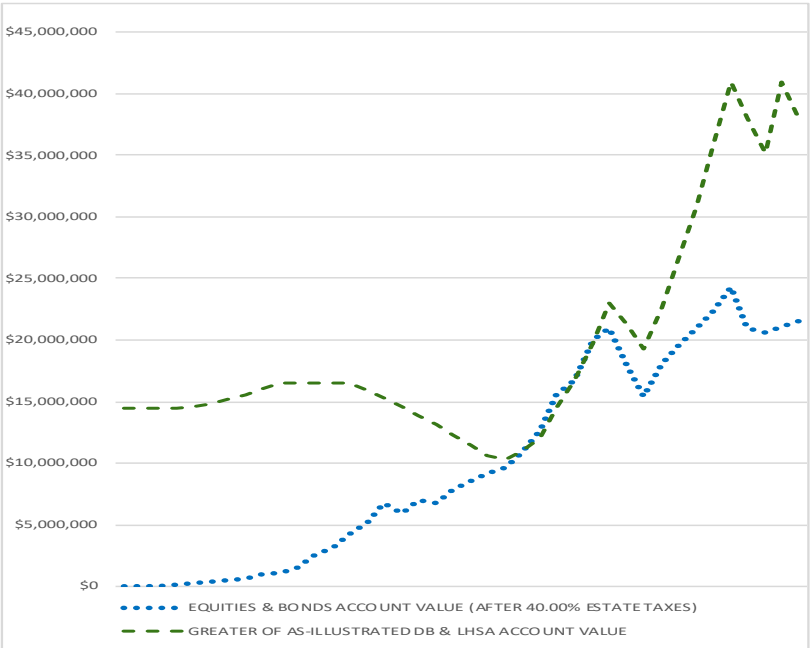
In the above model, 3-month Libor experiences a compounded annual increase of 39.00%, making the third-party lender borrowing rates top out at 10.23% in year 14. Overall, I would say that this comparison gives the non-leveraged *Hypothetical Equities & Bonds Account* several substantial advantages that may not be very realistic in a real-world scenario, however I wanted to avoid being accused of being overly biased towards the *Premium Financed IUL Proxy*, hence the unrealistic advantages credited to the *Hypothetical Equities & Bonds Account.*

The graphs on the following two pages display the difference in after-estate tax values of the two models during the *Best 40* and *Worst 40* periods.

BEST CAGR PERIOD OUT OF 121 DIFFERENT 40-YEAR S&P PERIODS ANALYZED



WORST CAGR PERIOD OUT OF 121 DIFFERENT 40-YEAR S&P PERIODS ANALYZED



We evaluated the net values of each of these models during both the 40-year S&P 500 historical period that produced the *Best Compounded Annual Growth Rate* of the 121 different 40-year periods analyzed, and the 40-year S&P 500 historical period that produced the *Worst Compounded Annual Growth Rate* of the 121 different 40-year periods analyzed.

As a reminder, for the *Hypothetical Equities & Bonds Account*, we assumed 0.16% investment fees, 15.00% tax rates on the equities gains (taxed each year), 24.00% tax rates on bond gains (taxed each year), and a 40% estate tax rate on EOY account values assuming generational wealth transfer in each given year.

For the *Premium Financed IUL Proxy*, we assumed a 0.00% floor, an 8.00% cap, a 1.45x multiplier bonus (resulting in a maximum annual index credit of 11.60%), and a 1.00% asset-based multiplier charge.

The following comparison graphs depict the greater of the as-illustrated death benefit in the carrier illustration and the net account values of the *Premium Financed IUL Proxy* (because we do not attempt to estimate death benefit amounts in these synthetic proxies).

Now that we have discussed why backtesting during times of volatility is so important when making decisions regarding whether or not *Premium Financed Life Insurance* should be used in estate planning, we will now evaluate several different ways of financing life insurance premiums.

Each method utilizes a different methodology based on very specific client wants and needs. The second most important thing for an advisor to understand when implementing a particular method of premium financing is the client's unique financial situation.

However the single-most important thing for an advisor to understand is how to identify the difference between what a client *says* they want today, versus how they will *feel* in the future if their personal financial situation does not meet their aspirations.

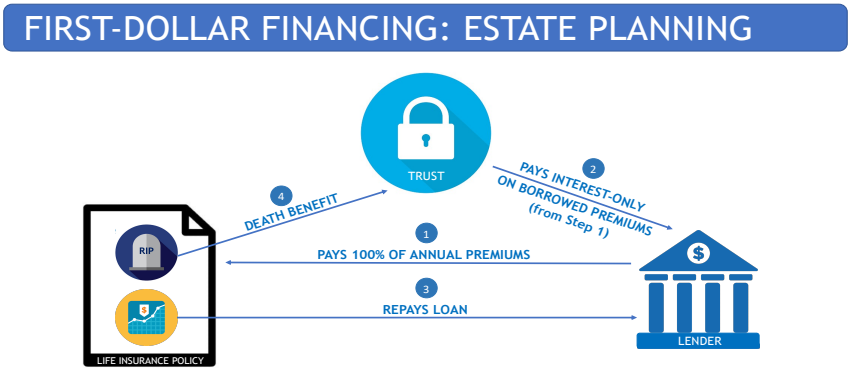
In the following chapters, I will model three very different premium financing platforms and we will discuss when each one is most suitable for a specific type of client.

The three different models are:

1. First-Dollar Financing with Cost Recovery
2. Partial-Equity Interest Accrual
3. Third-Year Financing with No Collateral

Chapter 10
First-Dollar Financing With Cost Recovery

The first case study I shared with you earlier in this book utilized *First-Dollar Financing*. In this scenario, the client borrows 100% of the premium, pays interest out-of-pocket each year, and posts outside collateral in the form of cash, CDs, securities, bonds, or a Letter Of Credit.



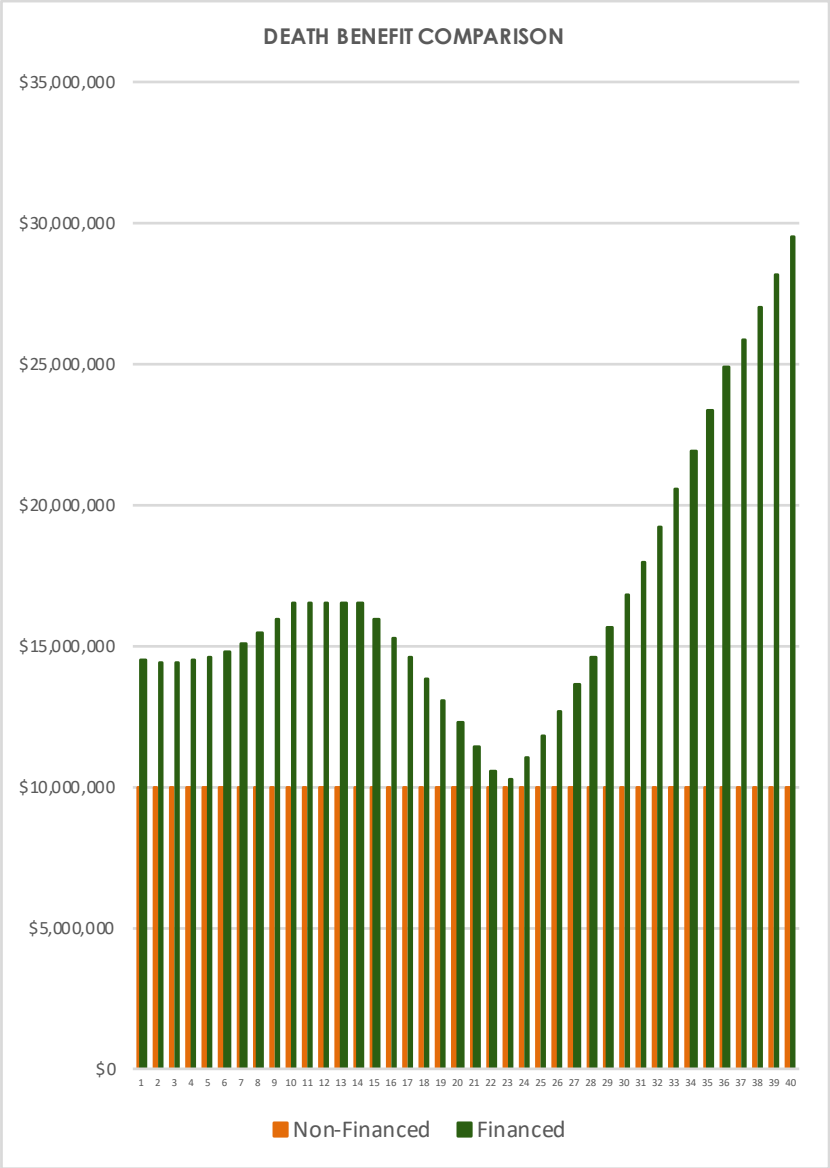
FIRST-DOLLAR PREMIUM FINANCING: DEATH BENEFIT FOCUS
1. The lender will pay the life insurance premiums directly to the life insurance carrier. The policy is owned by a trust.
2. The trust will pay interest-only to the lender each year on the cumulative borrowed premiums and post the policy (and additional outside assets) as collateral.
3. The appreciated policy value will repay the loan balance to the lender.
4. Upon the insured's death, the policy death benefit will pay to the trust.

This design is very straight-forward and it is what most premium financing arrangements use. Since we already reviewed the mechanics of this design, we will skip the ledger review and focus on the logical insurance-based alternative to *First-Dollar Financing*: A non-financed *IUL*.

In the previously reviewed case study, the 55-year old male client needed a low point death benefit of $10,000,000. The *First-Dollar Financing* solution started with a $14,601,915 face amount and hit a low point death benefit of $10,297,905 in policy year 23 (age 77) in the carrier illustration.

As a comparison, I also ran a non-financed policy using the exact same product from the exact same carrier, solving for a level

death benefit of $10,000,000. Although the low point net death benefit in the *Premium Financed IUL* was close to $10,000,000, the net death benefit was substantially larger during the majority of the 40-year period than the level $10,000,000 death benefit of the non-financed policy. See below.



In addition, the annual premium on the non-financed *IUL* was $182,840 per year for thirty years ($5,485,200 in total client outlay), versus only $3,596,216 in the total interest payments in the *Premium Financed IUL* model.

NON-FINANCED IUL					
	AGE	ANNUAL PREMIUM	CASH VALUE	DEATH BENEFIT	CUMULATIVE COST
1	55	$182,840	$0	$10,000,000	$182,840
2	56	$182,840	$0	$10,000,000	$365,680
3	57	$182,840	$86,415	$10,000,000	$548,520
4	58	$182,840	$249,367	$10,000,000	$731,360
5	59	$182,840	$418,613	$10,000,000	$914,200
6	60	$182,840	$591,870	$10,000,000	$1,097,040
7	61	$182,840	$771,485	$10,000,000	$1,279,880
8	62	$182,840	$957,428	$10,000,000	$1,462,720
9	63	$182,840	$1,149,723	$10,000,000	$1,645,560
10	64	$182,840	$1,348,491	$10,000,000	$1,828,400
11	65	$182,840	$1,558,780	$10,000,000	$2,011,240
12	66	$182,840	$1,739,220	$10,000,000	$2,194,080
13	67	$182,840	$1,926,083	$10,000,000	$2,376,920
14	68	$182,840	$2,119,445	$10,000,000	$2,559,760
15	69	$182,840	$2,319,275	$10,000,000	$2,742,600
16	70	$182,840	$2,525,393	$10,000,000	$2,925,440
17	71	$182,840	$2,737,563	$10,000,000	$3,108,280
18	72	$182,840	$2,955,276	$10,000,000	$3,291,120
19	73	$182,840	$3,177,924	$10,000,000	$3,473,960
20	74	$182,840	$3,404,843	$10,000,000	$3,656,800
21	75	$182,840	$3,636,601	$10,000,000	$3,839,640
22	76	$182,840	$3,872,759	$10,000,000	$4,022,480
23	77	$182,840	$4,113,060	$10,000,000	$4,205,320
24	78	$182,840	$4,357,230	$10,000,000	$4,388,160
25	79	$182,840	$4,605,039	$10,000,000	$4,571,000
26	80	$182,840	$4,909,304	$10,000,000	$4,753,840
27	81	$182,840	$5,222,814	$10,000,000	$4,936,680
28	82	$182,840	$5,546,986	$10,000,000	$5,119,520
29	83	$182,840	$5,883,804	$10,000,000	$5,302,360
30	84	$182,840	$6,235,957	$10,000,000	$5,485,200
31	85	$0	$6,411,766	$10,000,000	$5,485,200
32	86	$0	$6,584,648	$10,000,000	$5,485,200
33	87	$0	$6,753,842	$10,000,000	$5,485,200
34	88	$0	$6,917,895	$10,000,000	$5,485,200
35	89	$0	$7,075,498	$10,000,000	$5,485,200
36	90	$0	$7,229,027	$10,000,000	$5,485,200
37	91	$0	$7,381,440	$10,000,000	$5,485,200
38	92	$0	$7,527,918	$10,000,000	$5,485,200
39	93	$0	$7,669,724	$10,000,000	$5,485,200
40	94	$0	$7,813,532	$10,000,000	$5,485,200

$5,485,200
TOTAL NET COST
(OVER 40 YEARS)

ALGORITHMICALLY-BASED LIFE INSURANCE SOLUTION

version 426813.98 IUL

FIRST-DOLLAR FINANCING

Health Rating: **PREFERRED**

Initial Gross Policy Face Amount: **$14,601,915**

YEAR	AGE	1 TOTAL POLICY PREMIUMS	2 PREMIUMS PAID BY CLIENT	3 PREMIUMS PAID BY LENDER	4 CUMULATIVE PF LOAN BALANCE	5 FINANCING INTEREST RATE	6 INTEREST DUE	7 INTEREST ACCRUED	8 CLIENT CONTRIBUTION	9 ESTIMATED COLLATERAL	10 HYPOTHETICAL INDEX CREDIT	11 POLICY DRAWDOWNS	12 GROSS ACCUMULATED VALUE	13 POLICY CSV NET OF LOANS	14 DEATH BENEFIT NET OF LOANS	15 DEATH BENEFIT IRR INCLUDING DRAWDOWNS	YEAR	AGE
1	55	$1,250,000	$0	$1,250,000	$1,250,000	1.67%	$20,875	$0	$20,875	$954,642	5.50%	$0	$1,117,457	-$626,087	$14,469,372	69214.36%	1	55
2	56	$1,250,000	$0	$1,250,000	$2,500,000	1.71%	$42,650	$0	$42,650	$954,642	5.50%	$0	$2,302,901	-$644,064	$14,404,816	2426.71%	2	56
3	57	$1,250,000	$0	$1,250,000	$3,750,000	1.75%	$65,730	$0	$65,730	$981,285	5.50%	$0	$3,553,201	-$596,745	$14,405,116	709.60%	3	57
4	58	$1,250,000	$0	$1,250,000	$5,000,000	1.81%	$90,682	$0	$90,682	$945,291	5.50%	$0	$4,872,368	-$479,976	$14,474,283	352.63%	4	58
5	59	$1,250,000	$0	$1,250,000	$6,250,000	1.89%	$118,296	$0	$118,296	$842,580	5.50%	$0	$6,264,505	**-$289,653**	**$14,616,420**	**218.32%**	5	59
6	60	$1,250,000	$0	$1,250,000	$7,500,000	2.00%	$149,666	$0	$149,666	$665,308	5.50%	$0	$7,729,542	-$25,846	$14,831,457	151.72%	6	60
7	61	$1,250,000	$0	$1,250,000	$8,750,000	2.13%	$186,306	$0	$186,306	$419,917	5.50%	$0	$9,274,718	$318,831	$15,126,633	113.06%	7	61
8	62	$1,250,000	$0	$1,250,000	$10,000,000	2.30%	$230,298	$0	$230,298	$95,967	5.50%	$0	$10,903,880	$748,224	$15,505,795	88.24%	8	62
9	63	$1,250,000	$0	$1,250,000	$11,250,000	2.53%	$284,499	$0	$284,499	$0	5.50%	$0	$12,621,144	$1,266,448	$15,973,059	71.11%	9	63
10	64	$1,250,000	$0	$1,250,000	$12,500,000	2.82%	$352,817	$0	$352,817	$0	5.50%	$0	$14,430,812	**$1,877,954**	**$16,532,727**	**58.66%**	10	64
11	65	$0	$0	$0	$12,500,000	3.20%	$400,538	$0	$400,538	$0	5.50%	$0	$15,185,954	$2,685,954	$16,532,727	48.47%	11	65
12	66	$0	$0	$0	$12,500,000	3.70%	$462,574	$0	$462,574	$0	5.50%	$0	$15,983,011	$3,483,011	$16,532,727	40.45%	12	66
13	67	$0	$0	$0	$12,500,000	4.35%	$543,221	$0	$543,221	$0	5.50%	$0	$16,824,914	$4,324,914	$16,532,727	33.95%	13	67
14	68	$0	$0	$0	$12,500,000	5.18%	$648,063	$0	$648,063	$0	5.50%	$0	$17,714,986	$5,214,986	$16,532,727	28.54%	14	68
15	69	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$12,500,000	$18,627,608	**$5,502,608**	**$15,907,727**	**24.24%**	15	69
16	70	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$19,592,173	$5,810,923	$15,251,477	20.74%	16	70
17	71	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$20,612,881	$6,142,569	$14,562,415	17.86%	17	71
18	72	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$21,694,458	$6,500,630	$13,838,899	15.44%	18	72
19	73	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$22,842,646	$6,889,126	$13,079,208	13.39%	19	73
20	74	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$24,064,556	**$7,313,360**	**$12,281,532**	**11.61%**	20	74
21	75	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$25,369,941	$7,781,185	$11,443,972	10.04%	21	75
22	76	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$26,769,596	$8,301,403	$10,564,534	8.63%	22	76
23	77	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$28,275,722	$8,884,119	$10,297,905	7.82%	23	77
24	78	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$746,341	$29,873,786	$8,728,946	$10,222,635	7.77%	24	78
25	79	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$746,341	$31,560,218	**$8,574,477**	**$10,152,488**	**7.73%**	25	79
26	80	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$746,341	$33,422,155	$8,503,469	$10,174,577	7.76%	26	80
27	81	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$746,341	$35,385,331	$8,437,052	$10,206,319	7.78%	27	81
28	82	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$746,341	$37,453,995	$8,374,645	$10,247,344	7.80%	28	82
29	83	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$746,341	$39,632,366	$8,315,390	$10,297,009	7.82%	29	83
30	84	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$746,341	$41,924,573	**$8,258,090**	**$10,354,319**	**7.83%**	30	84
31	85	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$746,341	$44,333,294	$8,199,829	$10,416,493	7.85%	31	85
32	86	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$46,865,027	$8,924,889	$11,268,140	7.86%	32	86
33	87	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$49,523,158	$9,686,013	$12,162,171	7.86%	33	87
34	88	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$52,310,113	$10,481,110	$13,096,616	7.86%	34	88
35	89	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$55,227,780	**$11,307,327**	**$14,068,716**	**7.84%**	35	89
36	90	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$58,280,738	$12,164,263	$15,078,300	7.83%	36	90
37	91	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$61,539,270	$13,116,971	$15,578,542	7.72%	37	91
38	92	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$65,025,770	$14,182,356	$16,133,130	7.63%	38	92
39	93	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$68,774,070	$15,388,486	$16,763,967	7.54%	39	93
40	94	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$72,825,867	**$16,771,003**	**$17,499,262**	**7.48%**	40	94
		-$12,500,000	$0	-$12,500,000			$3,596,216	$0	$3,596,216	INCOME DRAWN DOWN:		-$5,970,728						

PREMIUM FINANCING INTEREST ASSUMPTIONS

Base Rate:	3-Month Libor
3-Month Libor Rate:	0.12%
Date Base Rate Calculated:	10/25/2021
Compounded Annual Base Rate Increase:	30.00%
Base Rate Increase Schedule:	20/20
Lender Spread:	1.55%
Total Rate Floor:	1.55%
Additional Origination Fee on New $:	0.00%

POLICY INDEX CREDIT ASSUMPTIONS

AG-49 (Average of every 25-yr run over last 65 years):	5.47%
Reduced Assumed Index Credit:	5.50%

GAP COLLATERAL REQUIREMENTS

Type Of Gap Collateral:	Cash
Collateral Valued:	100.00%

The additional gap collateral required is calculated by the cumulative loan balance in a given year, subtracted by 95% of the previous year's EOY value. Such value is then decreased by the sum of the new premium entering the policy in such current year minus all policy charges and surrender charges in such given year, multiplied by the % of "Collateral Valued" above. This is just a hypothetical calculation. Each lender has different collateral requirements and terms.

THIRD PARTY LENDER PAYOFF ASSUMPTIONS

Loan Payoff Type:	PAR LOAN	Income Type:	PAR LOAN
PLR:	5.00%	PLR:	5.00%

FINANCIAL BENEFIT SUMMARY

1ST YEAR COLLATERAL REQUIREMENT:	$954,642
PREMIUMS PAID BY CLIENT:	$0
LOAN INTEREST & PROGRAM FEES PAID BY CLIENT:	$3,596,216
TOTAL CLIENT OUTLAY:	-$3,596,216
TOTAL DRAWDOWNS (excluding loan payoff):	$5,970,728
40-YEAR PROGRAM NET CASH FLOW:	$2,374,512
YEAR 40 NET CASH SURRENDER VALUE:	$16,771,003
40-YEAR CASH GAIN (excluding death benefit):	**$19,145,516**
40-YEAR NET CSV IRR:	**7.38%**

Everything about this premium financing design above is the same as the very first case study depicted in this book, however in addition to the drawdown to pay off the third-party lender in year 15, this model takes additional drawdowns in years 24-31 (column 11), but not for supplemental retirement income per say.

The reason we are taking these drawdowns is to recover the $3,596,216 in interest payments the client made (column 8), plus an additional $2,374,512, totaling $5,970,728 in drawdowns (not including the $12,500,000 drawdown to pay off the third-party lender). This is called *100% Cost Recovery Plus The Cost Of Capital*.

(Pages 84-85)

	FIRST-DOLLAR FINANCING				3.00%
	AGE	ANNUAL CONTRIBUTION	CASH VALUE NET OF LOANS	DEATH BENEFIT NET OF LOANS	ALTERNATIVE ASSET
1	55	$20,875	$0	$14,469,372	$21,501
2	56	$42,650	$0	$14,404,816	$66,076
3	57	$65,730	$0	$14,405,116	$135,760
4	58	$90,682	$0	$14,474,283	$233,235
5	59	$118,296	$0	$14,616,420	$362,077
6	60	$149,666	$0	$14,831,457	$527,096
7	61	$186,306	$318,831	$15,126,633	$734,804
8	62	$230,298	$748,224	$15,505,795	$994,055
9	63	$284,499	$1,266,448	$15,973,059	$1,316,911
10	64	$352,817	$1,877,954	$16,532,727	$1,719,820
11	65	$400,538	$2,685,954	$16,532,727	$2,183,968
12	66	$462,574	$3,483,011	$16,532,727	$2,725,939
13	67	$543,221	$4,324,914	$16,532,727	$3,367,235
14	68	$648,063	$5,214,986	$16,532,727	$4,135,756
15	69	$0	$5,502,608	$15,907,727	$4,259,829
16	70	$0	$5,810,923	$15,251,477	$4,387,624
17	71	$0	$6,142,569	$14,562,415	$4,519,253
18	72	$0	$6,500,630	$13,838,899	$4,654,830
19	73	$0	$6,889,126	$13,079,208	$4,794,475
20	74	$0	$7,313,360	$12,281,532	$4,938,310
21	75	$0	$7,781,185	$11,443,972	$5,086,459
22	76	$0	$8,301,403	$10,564,534	$5,239,053
23	77	$0	$8,884,119	$10,297,905	$5,396,224
24	78	-$746,336	$8,728,946	$10,222,635	$4,789,385
25	79	-$746,336	$8,574,477	$10,152,488	$4,164,340
26	80	-$746,336	$8,503,469	$10,174,577	$3,520,544
27	81	-$746,336	$8,437,052	$10,206,319	$2,857,435
28	82	-$746,336	$8,374,645	$10,247,344	$2,174,432
29	83	-$746,336	$8,315,390	$10,297,009	$1,470,938
30	84	-$746,336	$8,258,090	$10,354,319	$746,341
31	85	-$746,341	$8,199,829	$10,416,493	$0
32	86	$0	$8,924,889	$11,268,140	$0
33	87	$0	$9,686,013	$12,162,171	$0
34	88	$0	$10,481,110	$13,096,616	$0
35	89	$0	$11,307,327	$14,068,716	$0
36	90	$0	$12,164,263	$15,078,300	$0
37	91	$0	$13,116,971	$15,578,542	$0
38	92	$0	$14,182,356	$16,133,130	$0
39	93	$0	$15,388,486	$16,763,967	$0
40	94	$0	$16,771,003	$17,499,262	$0

$0

TOTAL NET COST

(AFTER COST RECOVERY DRAWDOWNS)

In the ledger to the left, if the client had invested the interest they paid (left column) in an investment account and earned a net 3.00% return (after taxes and investment fees), they would have had an alternative asset growing over time (the far right column).

$746,336 is being drawn down from the policy in years 24-30, and $746,341 in year 31. Those same amounts are being drawn down from the alternative asset (in the far right column), which is depleted to $0 in year 31.

What this means is that the client was able to recover 100% of their interest expense paid ($3,596,216), plus an additional $2,374,512 to compensate for the lost opportunity cost he might have been to earn elsewhere.

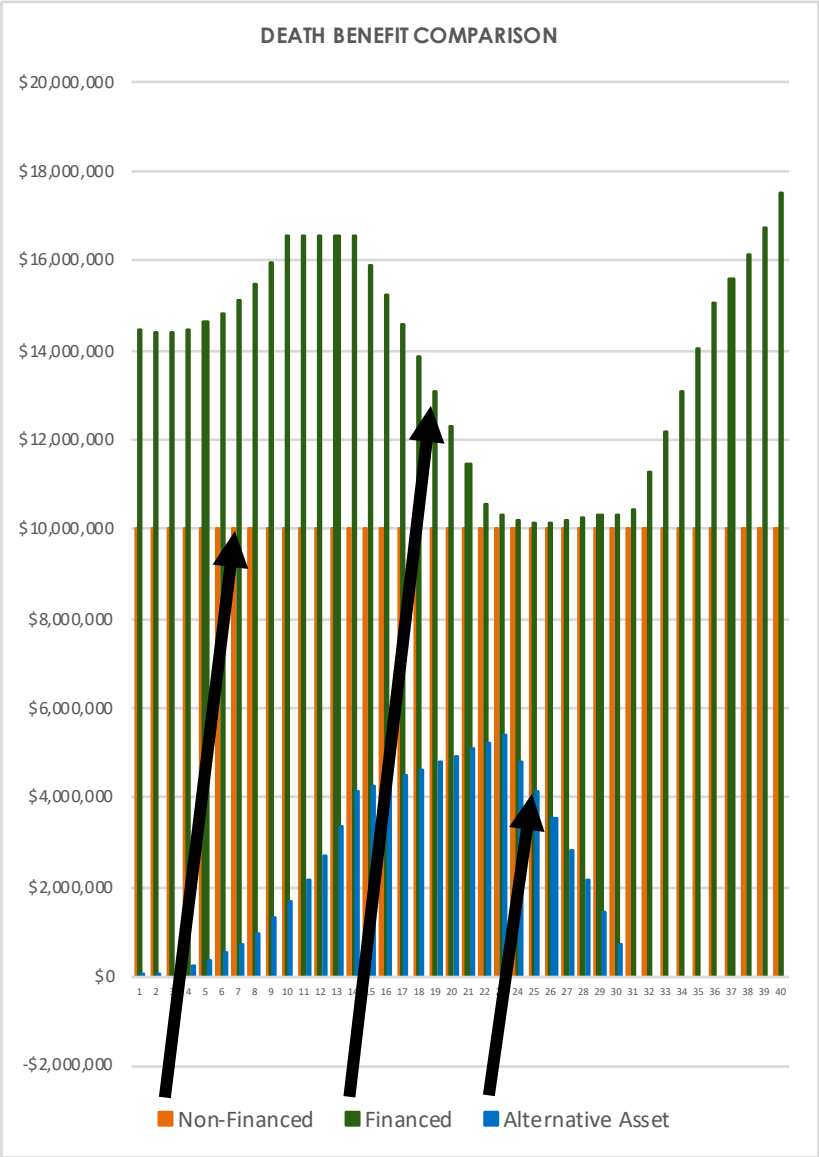
	$5,970,728	Total Drawn Down From Policy
-	$3,596,216	Interest Paid By Client on Premium Financing Loan
	$2,374,512	**Additional Drawdown To Recover Lost Opportunity Cost**

When it comes to life insurance, I have often times heard clients wrestle with the emotions of not wanting to pay for the insurance.

But when it comes to estate tax planning, in most cases there is no product or strategy that is more cash flow efficient than *Premium Financed Life Insurance*.

The graph on the following page illustrates a very clear visual comparison between:

1. A non-financed *IUL* policy.
2. A premium financed IUL policy with additional drawdowns to recover 100% of the interest paid out-of-pocket and lost opportunity cost.
3. The ongoing value of the alternative asset the client could have invested in (investing the same amount as the interest expense).



In this *Premium Financed IUL* (with the *100% Cost Recovery* strategy), the client maintains their $10,000,000 low point death benefit need, recovers 100% of his interest paid out-of-pocket, and recovers an additional $2,374,512 to compensate for the potential lost opportunity cost. We have truly created a ***Zero Net Cost Solution*** for this client.

Chapter 11
Partial-Equity Interest Accrual

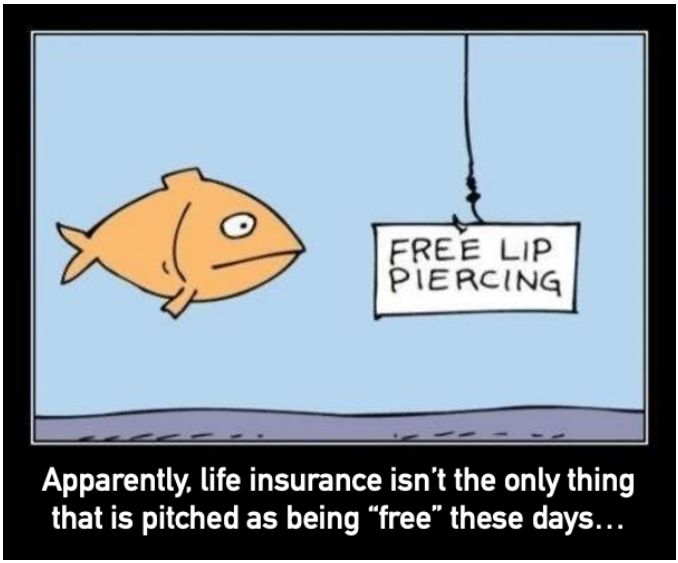
I have openly spoken out against over-leveraged, overly-aggressive interest accrual programs in the past, and I continue to do so, simply because:

1. The risk is unnecessary.
2. The risk is unsuitable for most clients.
3. The offer of *free life insurance* is very misleading.

There are very few things in life that are truly free, and life insurance is not one of them.

A few months ago, I broadcasted a national webinar addressing the irresponsible *free insurance* concept that many premium financing intermediaries are promoting. These models encourage the client to borrow 100% of the premium, accrue 100% of the interest, pay nothing, and simply post collateral.

I liken these offers to the cartoon illustrated below.



This *free insurance* concept is often times used to attract clients who "don't want to pay" the interest on borrowed premiums in a traditional *First-Dollar Financing* arrangement (which usually means they can't really afford the interest due).

I am often asked if there is ever a place for premium financed life insurance programs wherein the client pays zero out-of-pocket, knowingly takes on the risks of negative arbitrage potential, and puts a huge amount of collateral at risk.

If the client fully understands the risk – and their liquid net worth could support an upside-down scenario wherein the compounding debt with the third-party lender outpaces the policy value growth – I suppose the client should have the right to do this. But it reminds me of the mid-2000's where unknowing victims bought homes they couldn't afford under normal circumstances, and carelessly entered negative amortization mortgage loans without truly understanding the risks, and we all know what happened in 2008.

I suppose a client that likes higher-risk strategies should be able to make grown-up decisions regarding their finances and enter this type of arrangement, however for me personally, putting a client in this type of over-leveraged high-risk situation is just not something my firm does.

If a client who once claimed that they understood the risks associated with this type of *zero outlay premium financing program* suddenly falls on hard times during a period when the policy's index is performing far worse than what was initially depicted in the carrier illustration, you will most likely get sued as the advisor. If this type of client decides to litigate and you find yourself in front of a jury (who are not your peers from a financial sophistication standpoint), and you are accused of "tricking" your client into going into massive debt to buy *free insurance* (which turned out to NOT be free after all), and they lost millions of dollars they posted in collateral, the optics are not in your favor.

Even if the insurance strategy is mathematically sound, I have major concerns about this type of *zero out-of-pocket* premium financing arrangement, largely due to the optics – not just the math,

but the optics. Unless you expect the jury to be comprised of mathematicians, insurance actuaries, and sophisticated financial advisors that specialize in cash value life insurance, it is my personal opinion that you should be hesitant to recommend this arrangement to a client.

Perhaps you think I'm being overly conservative in my stance on this issue, and that's okay. We can agree to disagree on the subject of risk, but remember what I alluded to earlier in this book regarding the *Probability Of Risk* versus the *Consequence Of Risk*.

If a person's net worth is below $25,000,000, they likely do not have the liquidity to weather the storm of a *free insurance program gone bad* program, and you – the advisor – will be the first person they blame.

I always say that premium financing is NOT for someone that can't afford the premiums. It is for the type of person that CAN afford the premiums, but would rather deploy that cash in another asset class or in a business that may potentially give them greater returns. *Premium Financed Life Insurance* is a cash flow efficiency strategy for wealthy individuals, not a *get-something-for-nothing* strategy.

That being said, there are mathematically prudent premium financing strategies that employ *interest accrual*, but require the client to pay some out-of-pocket premiums, then borrow the remaining premiums from a third-party lender. If they are putting some skin-in-the-game, accruing interest is not necessarily a bad thing to do.

One method I will often times use is called *Partial-Equity Interest Accrual* wherein the client will pay approximately 10% of the premium (sometimes more, sometimes less), borrow 90% of the premiums, then accrue 100% of the interest due. This is typically done when the client wants to contribute a set annual budget instead of varying interest payments each year.

Alternatively, the client could elect to have their fixed annual budget go towards paying interest, however in the early years, the interest due is relatively small.

Policy Year	1 Annual Policy Premiums	2 Client Contributions Applied To Interest	3 Annual Premium Borrowed By Client	4 Cumulative Loan Balance w/ Accrual	5 Lender Interest Rate	6 Lender Interest Due	7 Interest Paid From Contributions & Reserve Account	8 Interest Accrued Added To Loan Balance (column 4)	9 Reserve Account From Excess Payments
1	$1,000,000	$100,000	$1,000,000	$1,000,000	2.00%	$20,000	$20,000	$0	$80,000
2	$1,000,000	$100,000	$1,000,000	$2,000,000	2.00%	$40,000	$40,000	$0	$140,000
3	$1,000,000	$100,000	$1,000,000	$3,000,000	2.00%	$60,000	$60,000	$0	$180,000
4	$1,000,000	$100,000	$1,000,000	$4,000,000	2.00%	$80,000	$80,000	$0	$200,000
5	$1,000,000	$100,000	$1,000,000	$5,000,000	2.00%	$100,000	$100,000	$0	$200,000
6	$1,000,000	$100,000	$1,000,000	$6,000,000	2.00%	$120,000	$120,000	$0	$180,000
7	$1,000,000	$100,000	$1,000,000	$7,000,000	2.00%	$140,000	$140,000	$0	$140,000
8	$1,000,000	$100,000	$1,000,000	$8,000,000	2.00%	$160,000	$160,000	$0	$80,000
9	$1,000,000	$100,000	$1,000,000	$9,000,000	2.00%	$180,000	$180,000	$0	$0
10	$1,000,000	$100,000	$1,000,000	$10,000,000	2.00%	$200,000	$100,000	$100,000	$0
11				**$10,100,000**					

In this ledger, the client makes fixed contributions of $100,000 per year for ten years (column 2).

In this scenario, the *Lender Interest Due* (column 6) is being paid by the $100,000 annual contributions for the first five years, and because the *Lender Interest Due* is less than $100,000 during the first four years, the excess is deposited into a *Reserve Account* (column 9).

Once the *Lender Interest Due* (column 6) becomes greater than the client's $100,000 annual contributions (starting in year 6), the reserve account begins paying for the overage.

This reserve account balance is enough to supplement the $100,000 annual client contributions through year 9 wherein the interest due is now $200,000.

At this point, the reserve account is depleted and the additional $100,000 in interest due is accrued (column 8).

After ten years, the total *Cumulative Loan Balance With Accrual* is $10,100,000 (year 11 in column 4).

This is definitely not the most efficient use of capital, though it does allow the client to enjoy a fixed annual contribution for ten years. There are however two alternative methods that allow the client to contribute the same fixed annual contribution, but accomplish a much better outcome for the client, which we will discuss in the next few pages.

(Pages 92-93)

Policy Year	1 Annual Policy Premiums	2 Client Contributions Applied To Interest	3 Annual Premium Borrowed By Client	4 Cumulative Loan Balance w/ Accrual	5 Lender Interest Rate	6 Lender Interest Due	7 Interest Paid From Client Contributions	8 Interest Accrued Added To Loan Balance (column 4)	9 Excess Payments Applied To Principal The Next Year
1	$1,000,000	$100,000	$1,000,000	$1,000,000	2.00%	$20,000	$20,000	$0	$80,000
2	$1,000,000	$100,000	$1,000,000	$1,920,000	2.00%	$38,400	$38,400	$0	$61,600
3	$1,000,000	$100,000	$1,000,000	$2,858,400	2.00%	$57,168	$57,168	$0	$42,832
4	$1,000,000	$100,000	$1,000,000	$3,815,568	2.00%	$76,311	$76,311	$0	$23,689
5	$1,000,000	$100,000	$1,000,000	$4,791,879	2.00%	$95,838	$95,838	$0	$4,162
6	$1,000,000	$100,000	$1,000,000	$5,787,717	2.00%	$115,754	$100,000	$15,754	$0
7	$1,000,000	$100,000	$1,000,000	$6,803,471	2.00%	$136,069	$100,000	$36,069	$0
8	$1,000,000	$100,000	$1,000,000	$7,839,541	2.00%	$156,791	$100,000	$56,791	$0
9	$1,000,000	$100,000	$1,000,000	$8,896,332	2.00%	$177,927	$100,000	$77,927	$0
10	$1,000,000	$100,000	$1,000,000	$9,974,258	2.00%	$199,485	$100,000	$99,485	$0
11				**$10,073,743**					

In the above scenario, the client has their excess payment pay down the cumulative loan balance instead of sitting dormant.

In other words, their $100,000 contribution could pay the *Interest Due* (column 6), and in years 1-5 wherein the interest due is less than the $100,000 client contributions, the excess (column 9) could be used to pay down the *Cumulative Loan Balance* (column 4) the very next year.

This method would also reduce the interest due the following year because the lender borrowing interest rate would be applied to this lower cumulative loan balance.

This reduction in loan balance each year would result in a lesser *Cumulative Loan Balance* of only $10,073,743 after the tenth year (column 4, year 11) compared to $10,100,000 in the previous model.

This would not be the most efficient method because the client would be paying interest on the greater amount borrowed each year. Yes, the excess would pay down the loan balance, but as long as the client pays a contribution that creates an excess amount (column 9), there are unused funds that sit dormant for an entire year.

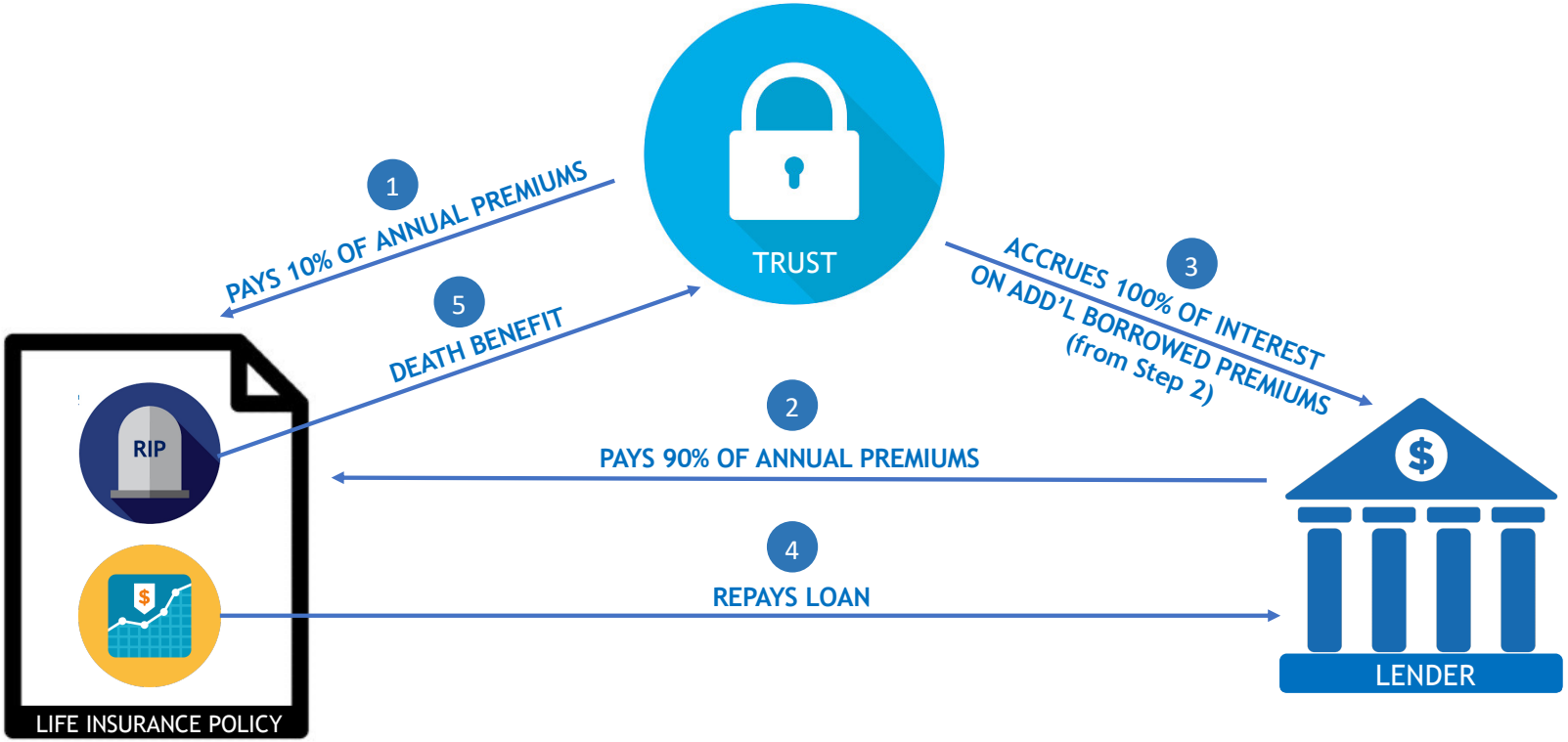
It could be argued that the client could use the excess to "immediately" pay down the loan balance, but if the client paid the annual interest due at the beginning of the loan year, they would have already overpaid interest on the larger amount.

I suppose it could also be argued that if interest was paid monthly or at year-end, the immediate pay-down in loan balance would lower the interest due, but there is no need to go through these shenanigans in my opinion.

The most efficient way to design a premium financing structure wherein the client has a fixed annual contribution is a method we call *Partial-Equity Interest Accrual*.

On the following page is an infographic that outlines how this platform works.

PARTIAL-EQUITY INTEREST ACCRUAL: ESTATE PLANNING



Policy Year	1 Annual Policy Premiums	2 Client Contributions Applied To Premium	3 Annual Premium Borrowed By Client	4 Cumulative Loan Balance w/ Accrual	5 Lender Interest Rate	6 Lender Interest Due	7 Interest Paid From Client Contributions	8 Interest Accrued Added To Loan Balance (column 4)
1	$1,000,000	$100,000	$900,000	$900,000	2.00%	$18,000	$0	$18,000
2	$1,000,000	$100,000	$900,000	$1,818,000	2.00%	$36,360	$0	$36,360
3	$1,000,000	$100,000	$900,000	$2,736,360	2.00%	$54,727	$0	$54,727
4	$1,000,000	$100,000	$900,000	$3,654,727	2.00%	$73,095	$0	$73,095
5	$1,000,000	$100,000	$900,000	$4,573,095	2.00%	$91,462	$0	$91,462
6	$1,000,000	$100,000	$900,000	$5,491,462	2.00%	$109,829	$0	$109,829
7	$1,000,000	$100,000	$900,000	$6,409,829	2.00%	$128,197	$0	$128,197
8	$1,000,000	$100,000	$900,000	$7,328,197	2.00%	$146,564	$0	$146,564
9	$1,000,000	$100,000	$900,000	$8,246,564	2.00%	$164,931	$0	$164,931
10	$1,000,000	$100,000	$900,000	$9,164,931	2.00%	$183,299	$0	$183,299
11				**$9,164,931**				

The *Partial-Equity Interest Accrual* ledger above shows that by paying 10% of the premiums each year and only borrowing 90% of the premiums, even with accruing 100% of the interest due on the smaller loan balance, after ten years, the *Cumulative Loan Balance* is less than the two previous models we just analyzed.

Of the $1,000,000 annual premiums in this example (column 1), the client's $100,000 annual contributions (column 2) are applied to the policy premium (not the interest), so the annual borrowed premium is only $900,000 (column 3) instead of the full $1,000,000 as it was in the previous two models we reviewed.

In this model, 100% of the interest due (column 6) is accrued (column 8) and capitalized back into the *Cumulative Loan Balance* (column 4). Even when accruing 100% of the interest, due to reducing the cumulative loan balance by only borrowing 90% of the premium instead of 100%, the loan balance is only $9,164,931 by year eleven (column 4, year 11). Compare this loan balance to the previous two examples, it is $935,069 less than the first example, and $908,812 less than the second example.

Understanding the most efficient use of capital and being able to mathematically compare all options is incredibly important for obvious reasons, yet I see so many premium financing arrangements that use the methods I described in the first two examples. It makes no sense whatsoever.

It should also be noted that in many cases, our *Partial-Equity Interest Accrual* platform could also be combined with our *100% Cost Recovery* strategy as well.

The idea of recovering 100% of the out-of-pocket expense is extremely intriguing to virtually every client I have ever talked to. This is somewhat ironic because if the policy is being used for estate planning purposes, recovering this cost just pulls the value back into the client's estate, making it taxable when it transfers to the next generation. It would be more mathematically prudent to leave that cash in the policy and maximize the tax-free death benefit.

In reality, it would only make sense to take drawdowns from the policy value if the client wanted to:

1. Use those funds for supplemental retirement income or to fund a trust expense (assuming the policy is in an ILIT), or…

2. Emotionally feel like they "got their money back."

You would be amazed at how appealing reason #2 has been to many of the clients I have personally talked to.

Even though most of them admit that they will probably leave the cash in the policy (because they don't anticipate needing it for lifestyle expenses) , they

love the idea of not incurring a net expense to fund their life insurance policy.

Regardless of how wealthy a person is, the emotional gratification of "getting all of their money back" is incredibly appealing, and regardless of how mathematically driven I am, I do understand the importance of optics and client emotions.

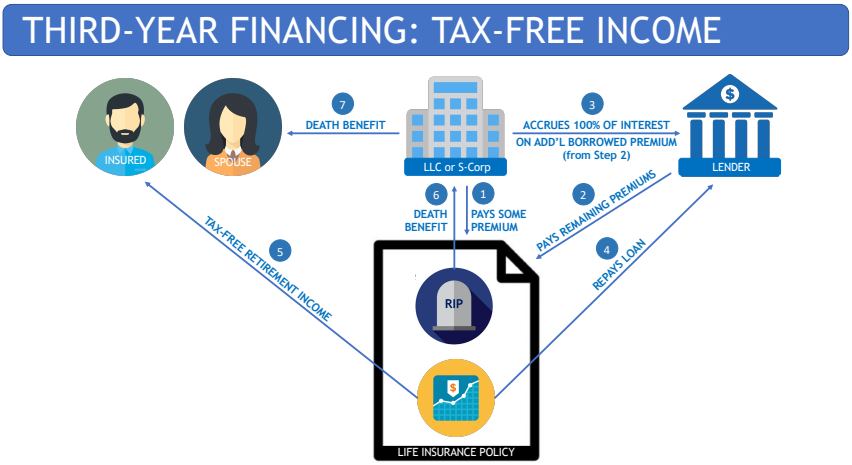
Chapter 12
Third-Year Financing & Zero Collateral: A Wealth Accumulation Strategy

So far I have shared several *Premium Financed Life Insurance* case studies wherein the focus was on using the net death benefit for estate planning purposes.

However many of our clients view *Premium Financed Life Insurance* as a tax-advantaged asset class within their overall financial portfolio. These types of clients are typically young professionals earning high incomes and they are looking for a place to park some of their income or reposition some of their other assets into a tax-advantaged asset.

In this design, the client pays a fixed annual contribution which pays for 100% of the policy premium in years 1-2 (step 1 in the infographic below). The policy premium in years 3-10 increases to approximately 3.75 larger than premiums in years 1-2.

The client's fixed annual contribution is applied to the policy premium in years 3-10, the remaining premium is borrowed from a third-party lender (step 2), and 100% of the interest is accrued (step 3).



In this design, there is typically no outside collateral required because borrowing does not start until policy year 3. As I stated earlier, the client pays 100% of the premium in years 1-2 which gives the policy cash value time to grow, unencumbered by any third-party debt. When lender funds enter the picture in year three, the policy value is typically greater than the outstanding loan balance, allowing the policy to serve as the sole collateral.

In this type of premium financing design, we will typically either lock in a guaranteed 10-year fixed borrowing rate with the third-party lender (currently 4.50% with one particular lender), or we will secure a different 10-year loan wherein the borrowing rate is locked in for years 1-5 (currently 3.90%), which then resets in policy year 6 based on the *1-Year U.S. Treasury Rate* at that time, and the rate remains fixed in years 6-10.

The client could obviously opt for an annual renewable rate loan at a lower borrowing rate, but sometimes clients prefer to lock in a fixed rate to give them peace of mind.

When it comes to multi-year fixed borrowing rates versus the currently lower annual variable rates, there is no "right" or "wrong" answer. The majority of capital sources we currently work with tell us they expect borrowing rates to remain low for the next several years, but of course these are just opinions, not guarantees.

Regardless of what the future holds with regards to borrowing interest rates, the fact of the matter is that current borrowing rates are at an all-time low. In my opinion, there has never been a better time to finance life insurance premiums, whether you are looking to secure a death benefit for estate tax planning, or if you are looking to use *Premium Financed Life Insurance* as a tax-advantaged asset class or a supplemental retirement plan.

In June 2019, there was a scathing online article published by an attorney named Lawrence Rybka who made some extremely defamatory comments about using a premium financed *IUL* as a retirement supplemental plan.

The article was titled *How To Retire In The Magical Retirement Income Castle In The Clouds* and it caused a lot of anger amongst the life insurance agent community.

I decided to read the article with a discriminating eye, but to my surprise, many of his criticisms were spot-on. The problem however was that they were only spot-on regarding certain overly-aggressive, opaquely-articulated premium financing designs. He lumped all premium financing designs into one category, assuming that all premium financed programs were the same.

This is a very narrow-minded viewpoint.

One of the most important things you must understand about *Premium Financed Life Insurance* is that there are many different disciplines and designs within this category.

Premium Financed Life Insurance is a general category, similar to certain ethnic foods as a category.

For example, *Asian food* is a general category of ethnic food, and this general category, there are several sub-categories including but not limited to Japanese food, Chinese food, Korean food, Vietnamese food, etc.

Yes, these types of ethnic food would fall into the category of *Asian food*, but they are all quite different.

Sure some of them share similarities in that they share certain ingredients (e.g., soy sauce), but not all Asian food sub-categories use soy sauce (like Indian food).

Similarly, not all premium financing methods use the same ingredients either.

Third-Year Financing With Zero Collateral is a very different version of premium financing. In fact, for the first two years of the policy, there are no financed premiums. One could even argue that for these first two years of the policy, the policy is a non-financed policy.

The following ledger outlines this unique method.

3RD YEAR FINANCING

Health Rating: **PREFERRED**

Initial Gross Policy Face Amount: **$5,045,482**

YEAR	AGE	1 TOTAL POLICY PREMIUMS	2 PREMIUMS PAID BY CLIENT	3 PREMIUMS PAID BY LENDER	4 CUMULATIVE PF LOAN BALANCE	5 FINANCING INTEREST RATE	6 INTEREST DUE	7 INTEREST ACCRUED	8 CLIENT CONTRIBUTION	9 ESTIMATED COLLATERAL	10 HYPOTHETICAL INDEX CREDIT	11 POLICY DRAWDOWNS	12 GROSS ACCUMULATED VALUE	13 POLICY CSV NET OF LOANS	14 DEATH BENEFIT NET OF LOANS	15 DEATH BENEFIT +YTY INCOME DRAWDOWN IRR	YEAR	AGE
1	45	$94,500	$94,500	$0	$0	0.00%	$0	$0	$100,000	$0	5.50%	$0	$71,872	$0	$5,117,354	5017.35%	1	45
2	46	$94,500	$94,500	$0	$0	0.00%	$0	$0	$100,000	$0	5.50%	$0	$147,766	$35,706	$5,193,248	572.37%	2	46
3	47	$375,000	$100,000	$275,000	$275,000	3.90%	$10,725	$10,725	$100,000	$0	5.50%	$0	$500,369	$125,166	$5,270,851	236.30%	3	47
4	48	$375,000	$100,000	$275,000	$560,725	3.90%	$21,868	$21,868	$100,000	$0	5.50%	$0	$872,761	$223,791	$5,357,518	137.95%	4	48
5	49	$375,000	$100,000	$275,000	$857,593	3.90%	$33,446	$33,446	$100,000	$0	5.50%	$0	$1,266,101	**$332,422**	**$5,453,989**	**93.91%**	5	49
6	50	$375,000	$100,000	$275,000	$1,166,039	4.52%	$52,676	$52,676	$100,000	$0	5.50%	$0	$1,680,946	$451,081	$5,560,388	69.63%	6	50
7	51	$375,000	$100,000	$275,000	$1,493,715	4.52%	$67,478	$67,478	$100,000	$0	5.50%	$0	$2,119,055	$573,977	$5,670,822	54.49%	7	51
8	52	$375,000	$100,000	$275,000	$1,836,193	4.52%	$82,950	$82,950	$100,000	$0	5.50%	$0	$2,581,677	$706,734	$5,790,965	44.27%	8	52
9	53	$375,000	$100,000	$275,000	$2,194,143	4.52%	$99,120	$99,120	$100,000	$0	5.50%	$0	$3,070,087	$849,960	$5,921,426	36.99%	9	53
10	54	$375,000	$100,000	$275,000	$2,568,263	4.52%	$116,021	$116,021	$100,000	$0	5.50%	$0	$3,585,620	**$1,004,289**	**$6,062,839**	**31.57%**	10	54
11	55	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$2,684,284	$3,781,459	$962,961	$2,853,691	15.92%	11	55
12	56	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$3,988,808	$1,029,385	$2,864,237	14.00%	12	56
13	57	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$4,208,381	$1,100,987	$2,868,507	12.45%	13	57
14	58	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$4,440,964	$1,178,200	$2,865,766	11.18%	14	58
15	59	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$4,687,406	**$1,261,504**	**$2,855,222**	**10.11%**	15	59
16	60	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$4,948,682	$1,351,485	$2,836,089	9.19%	16	60
17	61	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$5,225,441	$1,448,384	$2,911,507	8.68%	17	61
18	62	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$5,518,627	$1,552,717	$2,987,560	8.24%	18	62
19	63	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$5,829,233	$1,665,027	$3,064,043	7.85%	19	63
20	64	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$6,158,293	**$1,785,878**	**$3,140,702**	**7.51%**	20	64
21	65	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	$0	$6,506,886	$1,915,850	$3,217,227	7.21%	21	65
22	66	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$6,875,282	$1,837,999	$3,144,302	7.04%	22	66
23	67	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$7,264,464	$1,758,622	$3,066,226	6.87%	23	67
24	68	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$7,675,450	$1,677,621	$2,982,448	6.70%	24	68
25	69	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$8,109,305	**$1,594,890**	**$2,892,379**	**6.53%**	25	69
26	70	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$8,566,753	$1,509,922	$2,794,935	6.36%	26	70
27	71	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$9,050,873	$1,424,506	$2,601,120	6.09%	27	71
28	72	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$9,563,734	$1,339,355	$2,391,365	5.83%	28	72
29	73	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$10,108,487	$1,256,193	$2,165,957	5.57%	29	73
30	74	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$10,687,011	**$1,175,408**	**$1,923,499**	**5.31%**	30	74
31	75	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$11,302,190	$1,098,312	$1,663,422	5.05%	31	75
32	76	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$11,952,490	$1,021,724	$1,619,348	5.03%	32	76
33	77	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$12,639,671	$945,671	$1,577,655	5.00%	33	77
34	78	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$13,365,537	$870,143	$1,538,420	4.97%	34	78
35	79	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$14,131,938	**$795,079**	**$1,501,676**	**4.94%**	35	79
36	80	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$14,959,116	$738,720	$1,486,676	4.92%	36	80
37	81	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$15,831,786	$683,675	$1,475,264	4.90%	37	81
38	82	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$16,751,953	$629,742	$1,467,339	4.88%	38	82
39	83	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$17,721,634	$576,618	$1,462,699	4.85%	39	83
40	84	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.50%	-$206,376	$18,742,836	**$523,874**	**$1,461,016**	**4.83%**	40	84
		-$3,189,000	**-$989,000**	**-$2,200,000**			**$484,284**	**$484,284**	***$1,000,000***	***INCOME DRAWN DOWN:***		***-$3,921,143***						

In this model, the 45-year old client pays a fixed contribution of $100,000 each year for 10 years (column 8). The actual policy premium is $94,500 in years 1-2 (column 1) because there is a loan fee of 0.25% applied to the entire 10-year loan that is charged in years 1-2 to lock in a 10-year loan. This particular 10-year loan rate is fixed for the first five years at 3.90%. The base rate is the *1-Year U.S. Treasury Rate* (0.12% at the time this book was written) and has a lender spread of 2.25% with a 3.90% floor. This depiction assumes the *1-Year U.S. Treasury Rate* will increase at a compounded annual rate of 80%, hence the borrowing rate resets in the sixth year at 4.52% and remains fixed at that rate in years 6-10. This 80% increase on the base rate is a purely hypothetical inflated rate for the purpose of modeling this case study. The *Interest Due* (column 6) is accrued (column 7) in a sii fashion as the *Partial-Equity Interest Accrual* model we discussed in the previous chapter.

The third-party loan is paid off in year 11 using a *Participating Policy Loan* (column 11, year 11, in the amount of $2,684,284), and starting in year 12, the carrier illustration depicts an annual income stream of $206,376 (column 11) based on a static index return of 5.50% (column 10). Also, notice there is no outside collateral required (column 9) due to the unencumbered premiums paid in years 1-2.

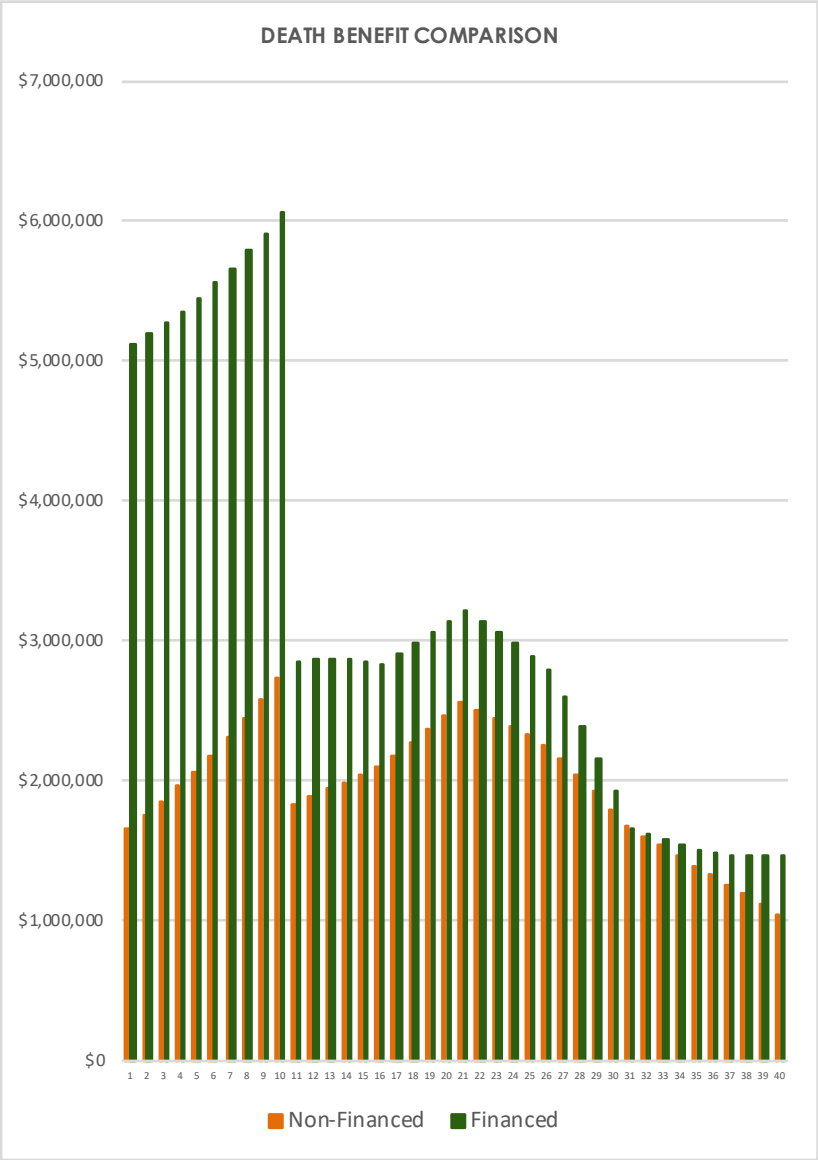
	NON-FINANCED IUL				
	AGE	ANNUAL PREMIUM	INCOME DRAWDOWNS	CASH VALUE	DEATH BENEFIT
1	45	$100,000	$0	$50,961	$1,658,863
2	46	$100,000	$0	$149,616	$1,753,878
3	47	$100,000	$0	$253,601	$1,854,174
4	48	$100,000	$0	$363,218	$1,960,072
5	49	$100,000	$0	$478,831	$2,071,903
6	50	$100,000	$0	$600,524	$2,189,781
7	51	$100,000	$0	$728,856	$2,314,237
8	52	$100,000	$0	$864,158	$2,445,616
9	53	$100,000	$0	$1,006,787	$2,584,275
10	54	$100,000	$0	$1,157,106	$2,730,576
11	55	$0	$0	$1,225,753	$1,838,629
12	56	$0	$0	$1,294,252	$1,889,607
13	57	$0	$0	$1,366,917	$1,941,021
14	58	$0	$0	$1,444,024	$1,992,753
15	59	$0	$0	$1,525,872	$2,044,668
16	60	$0	$0	$1,612,803	$2,096,644
17	61	$0	$0	$1,705,050	$2,182,464
18	62	$0	$0	$1,802,946	$2,271,712
19	63	$0	$0	$1,906,844	$2,364,487
20	64	$0	$0	$2,017,113	$2,460,877
21	65	$0	$0	$2,134,135	$2,560,962
22	66	$0	-$170,814	$2,078,431	$2,507,410
23	67	$0	-$170,814	$2,020,714	$2,450,624
24	68	$0	-$170,814	$1,960,870	$2,390,339
25	69	$0	-$170,814	$1,898,782	$2,326,274
26	70	$0	-$170,814	$1,834,179	$2,257,963
27	71	$0	-$170,814	$1,767,586	$2,155,967
28	72	$0	-$170,814	$1,699,094	$2,046,628
29	73	$0	-$170,814	$1,628,854	$1,929,592
30	74	$0	-$170,814	$1,557,092	$1,804,525
31	75	$0	-$170,814	$1,484,141	$1,671,143
32	76	$0	-$170,814	$1,408,706	$1,606,543
33	77	$0	-$170,814	$1,330,634	$1,539,906
34	78	$0	-$170,814	$1,249,749	$1,471,081
35	79	$0	-$170,814	$1,165,843	$1,399,890
36	80	$0	-$170,814	$1,085,534	$1,333,321
37	81	$0	-$170,814	$1,002,045	$1,264,302
38	82	$0	-$170,814	$915,049	$1,192,531
39	83	$0	-$170,814	$824,271	$1,117,768
40	84	$0	-$170,814	$729,325	$1,039,656
	TOTAL CONTRIBUTION:			-$1,000,000	
	TOTAL INCOME:			$3,245,461	
	YEAR 40 NET CASH VALUE:			$729,325	
	YEAR 40 TOTAL VALUE:			$3,974,786	

If we compare this to a non-financed policy using the exact same *IUL* product from the exact same carrier, and use the same client contribution of $100,000 for ten years (assuming a $100,000 of non-financed annual premiums), the income drawdowns starting

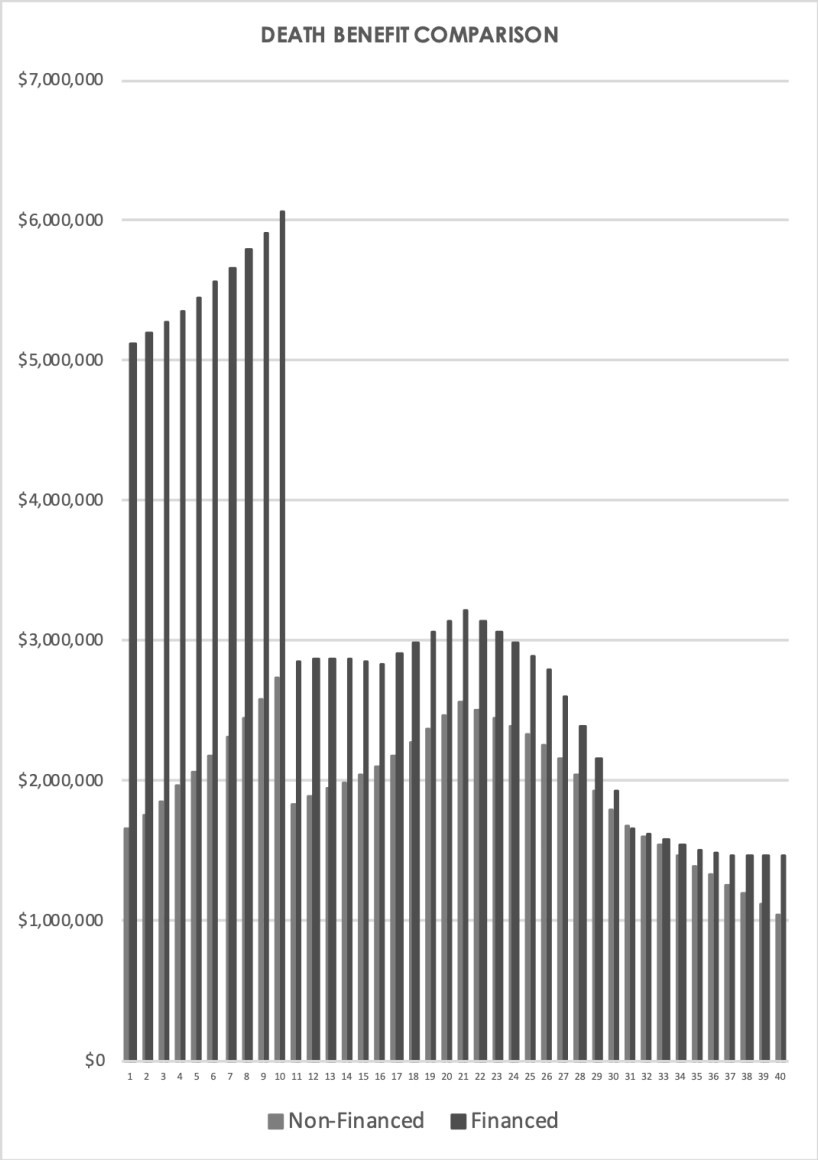
3RD YEAR FINANCING					
	AGE	ANNUAL CONTRIBUTION	INCOME DRAWDOWNS	CASH VALUE NET OF LOANS	DEATH BENEFIT NET OF LOANS
1	45	$100,000	$0	$0	$5,117,354
2	46	$100,000	$0	$35,706	$5,193,248
3	47	$100,000	$0	$125,166	$5,270,851
4	48	$100,000	$0	$223,791	$5,357,518
5	49	$100,000	$0	$332,422	$5,453,989
6	50	$100,000	$0	$451,081	$5,560,388
7	51	$100,000	$0	$573,977	$5,670,822
8	52	$100,000	$0	$706,734	$5,790,965
9	53	$100,000	$0	$849,960	$5,921,426
10	54	$100,000	$0	$1,004,289	$6,062,839
11	55	$0	$0	$962,961	$2,853,691
12	56	$0	$0	$1,029,385	$2,864,237
13	57	$0	$0	$1,100,987	$2,868,507
14	58	$0	$0	$1,178,200	$2,865,766
15	59	$0	$0	$1,261,504	$2,855,222
16	60	$0	$0	$1,351,485	$2,836,089
17	61	$0	$0	$1,448,384	$2,911,507
18	62	$0	$0	$1,552,717	$2,987,560
19	63	$0	$0	$1,665,027	$3,064,043
20	64	$0	$0	$1,785,878	$3,140,702
21	65	$0	$0	$1,915,850	$3,217,227
22	66	$0	-$206,376	$1,837,999	$3,144,302
23	67	$0	-$206,376	$1,758,622	$3,066,226
24	68	$0	-$206,376	$1,677,621	$2,982,448
25	69	$0	-$206,376	$1,594,890	$2,892,379
26	70	$0	-$206,376	$1,509,922	$2,794,935
27	71	$0	-$206,376	$1,424,506	$2,601,120
28	72	$0	-$206,376	$1,339,355	$2,391,365
29	73	$0	-$206,376	$1,256,193	$2,165,957
30	74	$0	-$206,376	$1,175,408	$1,923,499
31	75	$0	-$206,376	$1,098,312	$1,663,422
32	76	$0	-$206,376	$1,021,724	$1,619,348
33	77	$0	-$206,376	$945,671	$1,577,655
34	78	$0	-$206,376	$870,143	$1,538,420
35	79	$0	-$206,376	$795,079	$1,501,676
36	80	$0	-$206,376	$738,720	$1,486,676
37	81	$0	-$206,376	$683,675	$1,475,264
38	82	$0	-$206,376	$629,742	$1,467,339
39	83	$0	-$206,376	$576,618	$1,462,699
40	84	$0	-$206,376	$523,874	$1,461,016
			TOTAL CONTRIBUTION:	-$1,000,000	
			TOTAL INCOME:	$3,921,143	
			YEAR 40 NET CASH VALUE:	$523,874	
			YEAR 40 TOTAL VALUE:	$4,445,016	

in year 12 (same as the *Third-Year Financing With Zero Collateral* design) are $170,814 versus $206,376 in the premium financed design. That's a difference of $675,682 in total income drawdowns – a 20.82% increase in income drawdowns – favoring the *Third-Year Financing With Zero Collateral* design.

In addition, the *Third-Year Financing With Zero Collateral* design provides significantly more death benefit. Even though this was designed with the primary focus on income drawdowns and minimum death benefit, having more death benefit is better than having less death benefit, as long as the income drawdowns are greater. See below.



In addition, the *Third-Year Financing With Zero Collateral* design provides significantly more death benefit. Even though this was designed with the primary focus on income drawdowns and minimum death benefit, having more death benefit is better than having less death benefit, as long as the income drawdowns are greater. See below.



Perhaps an even more compelling comparison is the one between the *Third-Year Financing* design and the same non-insurance based hypothetical investment account we discussed earlier in this book called the *Hypothetical Equities & Bonds Account*.

In this hypothetical model, 70% of the portfolio uses historical S&P 500 returns + an additional 2.00% bonus added as a dividend, and 30% of the portfolio uses historical 10-year T-Bond returns.

The all-in investment fee in this model is only 0.16% (similar to a SPDR ETF) which is incredibly low.

The S&P returns are taxed at 22.00% and the 10-year T-Bonds are taxed at 15.00% (which assumes that the client is sheltering and reducing taxable income down to only $100,000 per year and living in Texas where there is no state income tax).

For the *Third-Year Financing* platform, we assumed a 0.00% floor, an 8.00% cap, a 1.45x multiplier bonus (resulting in a maximum annual index credit of 11.60%), and a 1.00% asset-based multiplier charge.

When we compare the income drawdown amounts between these two models in both the 40-year S&P 500 historical period that produced the *Best Compounded Annual Growth Rate* of the 121 different 40-year periods analyzed, and the 40-year S&P 500 historical period that produced the *Worst Compounded Annual Growth Rate* of the 121 different 40-year periods analyzed, there is a staggering disparity in income drawdowns favoring the *Third-Year Financing* platform.

In addition, when we attempted to drawdown the same annual income from the *Hypothetical Equities & Bonds Account*, the account was drawn down to a $0 account balance before the end of the 40-year period.

The next two pages will illustrate the *Leveraged Hypothetical Synthetic Asset* during the Worst 40, and the two pages following that will illustrate the *Hypothetical Equities & Bonds Account*.

WORST CAGR 40-YEAR PERIOD OUT OF 121 DIFFERENT INDEX PERIODS ANALYZED (STARTING 10/1/1971)

Current Cap: **9.00%** Floor Modeled: **0.00%** **PAGE 7**

Upside Design: **CAPPED** Cap Modeled: **8.00%** Participation Rate: **100.00%**

# YEAR	AGE	1 TOTAL INDEX CONTRIBUTION	2 CLIENT INDEX CONTRIBUTIONS	3 LENDER INDEX CONTRIBUTIONS	4 CUMULATIVE LOAN BALANCE	5 THIRD PARTY LOAN PAYOFF	6 FINANCING INTEREST RATE	7 INTEREST DUE	8 INTEREST ACCRUED	9 TOTAL CLIENT OUTLAY	10 ESTIMATED COLLATERAL	11 CALENDAR YEAR	12 INDEX RETURN (GROSS)	13 INDEX RETURN (FLOOR & CAP)	14 INDEX RETURN (EFFECTIVE)	15 ANNUAL INCOME DRAWDOWNS	16 EOY GROSS INDEX ACCOUNT VALUE	17 EOY NET INDEX ACCOUNT VALUE
1	45	$94,500	$94,500	$0	$0		0.00%	$0	$0	$100,000	$0	1971	12.42%	8.00%	8.00%	$0	$72,570	$698
2	46	$94,500	$94,500	$0	$0		0.00%	$0	$0	$100,000	$0	1972	-1.92%	0.00%	0.00%	$0	$138,358	$26,298
3	47	$375,000	$100,000	$275,000	$275,000		3.90%	$10,725	$10,725	$100,000	$0	1973	-41.40%	0.00%	0.00%	$0	$457,013	$81,810
4	48	$375,000	$100,000	$275,000	$560,725		3.90%	$21,868	$21,868	$100,000	$0	1974	32.00%	8.00%	11.60%	$0	$859,733	$210,762
5	49	$375,000	$100,000	$275,000	$857,593		3.90%	$33,446	$33,446	$100,000	$0	1975	25.48%	8.00%	11.60%	$0	$1,302,230	$368,551
6	50	$375,000	$100,000	$275,000	$1,166,039		4.52%	$52,676	$52,676	$100,000	$0	1976	-8.28%	0.00%	0.00%	$0	$1,602,054	$372,189
7	51	$375,000	$100,000	$275,000	$1,493,715		4.52%	$67,478	$67,478	$100,000	$0	1977	6.23%	6.23%	9.03%	$0	$2,067,573	$522,495
8	52	$375,000	$100,000	$275,000	$1,836,193		4.52%	$82,950	$82,950	$100,000	$0	1978	6.61%	6.61%	9.59%	$0	$2,580,278	$705,335
9	53	$375,000	$100,000	$275,000	$2,194,143		4.52%	$99,120	$99,120	$100,000	$0	1979	14.76%	8.00%	11.60%	$0	$3,190,840	$970,712
10	54	$375,000	$100,000	$275,000	$2,568,263		4.52%	$116,021	$116,021	$100,000	$0	1980	-7.40%	0.00%	0.00%	$0	$3,460,430	**$879,099**
11	55	$0	$0	$0	$0	-$2,684,284	0.00%	$0	$0	$0	$0	1981	3.65%	3.65%	5.29%	$0	$3,585,335	$766,837
12	56	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1982	37.91%	8.00%	11.60%	$0	$3,937,759	$978,336
13	57	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1983	0.02%	0.02%	0.03%	$0	$3,878,051	$770,657
14	58	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1984	9.62%	8.00%	11.60%	$0	$4,260,492	$997,728
15	59	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1985	27.04%	8.00%	11.60%	$0	$4,682,779	$1,256,877
16	60	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1986	39.13%	8.00%	11.60%	$0	$5,149,229	$1,552,031
17	61	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1987	-15.51%	0.00%	0.00%	$0	$5,075,459	$1,298,402
18	62	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1988	28.41%	8.00%	11.60%	$0	$5,582,346	$1,616,436
19	63	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1989	-12.34%	0.00%	0.00%	$0	$5,503,593	$1,339,388
20	64	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1990	26.73%	8.00%	11.60%	$0	$6,054,612	**$1,682,197**
21	65	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1991	7.72%	7.72%	11.19%	$0	$6,638,670	$2,047,634
22	66	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1992	9.84%	8.00%	11.60%	-$204,763	$7,307,385	$2,271,796
23	67	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1993	0.82%	0.82%	1.19%	-$227,180	$7,295,001	$1,769,093
24	68	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1994	26.30%	8.00%	11.60%	-$176,909	$8,030,165	$2,042,207
25	69	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1995	17.61%	8.00%	11.60%	-$204,221	$8,840,882	$2,339,095
26	70	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1996	37.82%	8.00%	11.60%	-$233,909	$9,734,419	$2,661,937
27	71	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1997	7.36%	7.36%	10.67%	-$266,194	$10,632,204	$2,926,594
28	72	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1998	26.13%	8.00%	11.60%	-$292,659	$11,713,015	$3,314,833
29	73	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	1999	11.99%	8.00%	11.60%	-$331,483	$12,907,521	$3,741,372
30	74	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2000	-27.54%	0.00%	0.00%	-$374,137	$12,749,375	**$2,732,074**
31	75	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2001	-21.68%	0.00%	0.00%	-$273,207	$12,594,562	$1,789,529
32	76	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2002	22.16%	8.00%	11.60%	-$178,953	$13,882,422	$2,349,237
33	77	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2003	11.91%	8.00%	11.60%	-$234,924	$15,302,850	$2,946,336
34	78	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2004	10.25%	8.00%	11.60%	-$294,634	$16,869,299	$3,585,594
35	79	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2005	8.71%	8.00%	11.60%	-$358,559	$18,596,560	$4,272,182
36	80	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2006	14.29%	8.00%	11.60%	-$427,218	$20,520,640	$5,031,464
37	81	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2007	-23.61%	0.00%	0.00%	-$503,146	$20,288,348	$3,496,409
38	82	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2008	-9.37%	0.00%	0.00%	-$349,641	$20,053,509	$2,054,850
39	83	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2009	7.96%	7.96%	11.54%	-$205,485	$22,101,782	$2,987,432
40	84	$0	$0	$0	$0		0.00%	$0	$0	$0	$0	2010	-0.86%	0.00%	0.00%	-$298,743	$21,836,506	**$1,452,758**
			$989,000	**$2,200,000**				**$484,284**	$484,284	**$1,000,000**					***AVERAGE ANNUAL INCOME DRAWDOWN:***	***$286,104***		**WORST 40**

In this 40-year period that produced the *Worst Compounded Annual Growth Rate* out of the 121 different 40-year periods analyzed, the gross historical S&P 500 returns (column 12) are depicted, the cap is then applied (column 13), and the 1.45x multiplier bonus is applied, producing the *Effective Index Return* (column 14).

It is important to note that at the time this book was written, the actual IUL cap this proxy was inspired by had a 9.00%, however we are modeling an 8.00% cap to be more conservative. The income drawdowns that in years 22-40 are equal to 10.00% of the previous year's *EOY Net Index Account Value*.

Due to the volatility illustrated during the backtesting periods analyzed, instead of drawing down a static amount the way a carrier illustration does, our model draws down this variable amount which would be a more prudent thing to do in a real world application because with volatility, years wherein the index produced lower returns (even 0.00%), the 10.00% drawdown accommodates for such underperforming years.

However, even in this particular unfavorable 40-year sequence, the 10.00% drawdowns produced a higher average annual drawdown of $286,104 (column 15) than the static drawdown of $206,376 in the carrier illustration (as shown on page 103, column 11).

(Pages 108-109)

HYPOTHETICAL EQUITIES & BONDS ACCOUNT vs. 3RD YEAR FINANCING

WORST CAGR 40-YEAR PERIOD OUT OF 121 DIFFERENT INDEX PERIODS ANALYZED (STARTING 10/1/1971)

	EQUITIES	BONDS
<AGE 56:	**70.00%**	**30.00%**
AGE 56+:	**70.00%**	**30.00%**

Current Adjusted Gross Income (AGI):	**$100,000**
Current Income Tax Rate:	**22.00%**
Long-Term Capital Gains Tax Rate:	**15.00%**
State of Residence:	**TX**

% of Equities Taxed at STCG Tax Rates:	**0.00%**
% of Equities Taxed at LTCG Tax Rates:	**100.00%**
% of Bonds Taxed at STCG Tax Rates:	**100.00%**

Advisor Fee:	0.06%
Fund Manager Fee:	0.08%
Broker Dealer Fee:	0.02%
Investment Fees (All-In):	0.16%

# YEAR	AGE	1 ANNUAL INVESTED	2 CALENDAR YEAR	3 GROSS EQUITIES RETURN	4 AFTER-FEE EQUITIES RETURN	5 AFTER-FEE & TAX EQUITIES RETURN	6 CALENDAR YEAR	7 GROSS BOND RETURN	8 AFTER-FEE BOND RETURN	9 AFTER-FEE & TAX BOND RETURN	10 TOTAL CHARGES	11 NET RETURN	12 INCOME DRAWDOWNS	13 AFTER-TAX ACCOUNT VALUE		14 LEVERAGED SYNTHETIC ACCOUNT VALUE	15 LEVERAGED SYNTHETIC INCREASE
1	45	$100,000	1971	14.42%	14.25%	12.12%	1971	5.27%	5.11%	3.98%	0.16%	9.68%	$0	$109,676	vs	$698	
2	46	$100,000	1972	0.08%	-0.08%	-0.08%	1972	-0.44%	-0.60%	-0.60%	0.16%	-0.24%	$0	$209,181	vs	$26,298	
3	47	$100,000	1973	-39.40%	-39.56%	-39.56%	1973	-2.37%	-2.53%	-2.53%	0.16%	-28.45%	$0	$221,207	vs	$81,810	
4	48	$100,000	1974	34.00%	33.83%	28.76%	1974	-8.16%	-8.33%	-8.33%	0.16%	17.63%	$0	$377,847	vs	$210,762	
5	49	$100,000	1975	27.48%	27.32%	23.22%	1975	-5.07%	-5.24%	-5.24%	0.16%	14.68%	$0	$548,011	vs	$368,551	
6	50	$100,000	1976	-6.28%	-6.44%	-6.44%	1976	9.68%	9.52%	7.43%	0.16%	-2.28%	$0	$633,244	vs	$372,189	
7	51	$100,000	1977	8.23%	8.06%	6.85%	1977	-4.89%	-5.06%	-5.06%	0.16%	3.28%	$0	$757,305	vs	$522,495	
8	52	$100,000	1978	8.61%	8.45%	7.18%	1978	-7.81%	-7.97%	-7.97%	0.16%	2.64%	$0	$879,899	vs	$705,335	
9	53	$100,000	1979	16.76%	16.60%	14.11%	1979	-9.51%	-9.68%	-9.68%	0.16%	6.98%	$0	$1,048,253	vs	$970,712	
10	54	$100,000	1980	-5.40%	-5.56%	-5.56%	1980	-14.57%	-14.73%	-14.73%	0.16%	-8.31%	$0	**$1,052,840**	vs	**$879,099**	-16.50%
11	55	$0	1981	5.65%	5.49%	4.66%	1981	-1.94%	-2.10%	-2.10%	0.16%	2.64%	$0	$1,080,591	vs	$766,837	-29.04%
12	56	$0	1982	39.91%	39.75%	33.78%	1982	25.14%	24.98%	19.48%	0.16%	29.49%	$0	$1,399,308	vs	$978,336	-30.08%
13	57	$0	1983	2.02%	1.86%	1.58%	1983	-0.01%	-0.17%	-0.17%	0.16%	1.05%	$0	$1,414,032	vs	$770,657	-45.50%
14	58	$0	1984	11.62%	11.46%	9.74%	1984	9.04%	8.88%	6.93%	0.16%	8.90%	$0	$1,539,828	vs	$997,728	-35.21%
15	59	$0	1985	29.04%	28.88%	24.55%	1985	21.41%	21.25%	16.57%	0.16%	22.16%	$0	$1,880,989	vs	$1,256,877	-33.18%
16	60	$0	1986	41.13%	40.97%	34.82%	1986	21.97%	21.81%	17.01%	0.16%	29.48%	$0	$2,435,455	vs	$1,552,031	-36.27%
17	61	$0	1987	-13.51%	-13.67%	-13.67%	1987	-8.32%	-8.48%	-8.48%	0.16%	-12.12%	$0	$2,140,377	vs	$1,298,402	-39.34%
18	62	$0	1988	30.41%	30.24%	25.71%	1988	3.98%	3.82%	2.98%	0.16%	18.89%	$0	$2,544,687	vs	$1,616,436	-36.48%
19	63	$0	1989	-10.34%	-10.51%	-10.51%	1989	12.27%	12.11%	9.45%	0.16%	-4.52%	$0	$2,429,663	vs	$1,339,388	-44.87%
20	64	$0	1990	28.73%	28.57%	24.28%	1990	0.79%	0.63%	0.49%	0.16%	17.15%	$0	**$2,846,266**	vs	**$1,682,197**	-40.90%
21	65	$0	1991	9.72%	9.56%	8.12%	1991	10.33%	10.17%	7.93%	0.16%	8.07%	$0	$3,075,856	vs	$2,047,634	-33.43%
22	66	$0	1992	11.84%	11.68%	9.93%	1992	6.15%	5.98%	4.67%	0.16%	8.35%	-$204,763	$3,110,871	vs	$2,271,796	-25.31%
23	67	$0	1993	2.82%	2.66%	2.26%	1993	10.94%	10.77%	8.40%	0.16%	4.10%	-$227,180	$3,002,064	vs	$1,769,093	-35.90%
24	68	$0	1994	28.30%	28.14%	23.92%	1994	-10.37%	-10.54%	-10.54%	0.16%	13.58%	-$176,909	$3,208,878	vs	$2,042,207	-30.56%
25	69	$0	1995	19.61%	19.45%	16.53%	1995	20.11%	19.95%	15.56%	0.16%	16.24%	-$204,221	$3,492,620	vs	$2,339,095	-26.79%
26	70	$0	1996	39.82%	39.66%	33.71%	1996	-1.46%	-1.62%	-1.62%	0.16%	23.11%	-$233,909	$4,011,802	vs	$2,661,937	-26.68%
27	71	$0	1997	9.36%	9.20%	7.82%	1997	7.43%	7.27%	5.67%	0.16%	7.17%	-$266,194	$4,014,305	vs	$2,926,594	-20.42%
28	72	$0	1998	28.13%	27.96%	23.77%	1998	13.16%	13.00%	10.14%	0.16%	19.68%	-$292,659	$4,454,103	vs	$3,314,833	-18.80%
29	73	$0	1999	13.99%	13.83%	11.75%	1999	-10.22%	-10.38%	-10.38%	0.16%	5.11%	-$331,483	$4,333,434	vs	$3,741,372	-9.44%
30	74	$0	2000	-25.54%	-25.70%	-25.70%	2000	12.84%	12.68%	9.89%	0.16%	-15.02%	-$374,137	**$3,364,552**	vs	**$2,732,074**	-11.14%
31	75	$0	2001	-19.68%	-19.84%	-19.84%	2001	2.67%	2.51%	1.96%	0.16%	-13.30%	-$273,207	$2,680,155	vs	$1,789,529	-16.92%
32	76	$0	2002	24.16%	24.00%	20.40%	2002	13.32%	13.16%	10.26%	0.16%	17.36%	-$178,953	$2,935,393	vs	$2,349,237	-10.29%
33	77	$0	2003	13.91%	13.75%	11.68%	2003	-1.85%	-2.01%	-2.01%	0.16%	7.58%	-$234,924	$2,905,032	vs	$2,946,336	0.70%
34	78	$0	2004	12.25%	12.09%	10.27%	2004	1.77%	1.60%	1.25%	0.16%	7.57%	-$294,634	$2,807,926	vs	$3,585,594	12.75%
35	79	$0	2005	10.71%	10.55%	8.97%	2005	-0.51%	-0.67%	-0.67%	0.16%	6.08%	-$358,559	$2,598,180	vs	$4,272,182	26.78%
36	80	$0	2006	16.29%	16.13%	13.71%	2006	-1.23%	-1.39%	-1.39%	0.16%	9.18%	-$427,218	$2,370,261	vs	$5,031,464	41.26%
37	81	$0	2007	-21.61%	-21.77%	-21.77%	2007	7.15%	6.99%	5.45%	0.16%	-13.60%	-$503,146	$1,613,169	vs	$3,496,409	30.40%
38	82	$0	2008	-7.37%	-7.53%	-7.53%	2008	15.66%	15.50%	12.09%	0.16%	-1.65%	-$349,641	$1,242,741	vs	$2,054,850	13.15%
39	83	$0	2009	9.96%	9.80%	8.33%	2009	-10.80%	-10.96%	-10.96%	0.16%	2.54%	-$205,485	$1,063,602	vs	$2,987,432	31.03%
40	84	$0	2010	1.14%	0.98%	0.83%	2010	6.71%	6.55%	5.11%	0.16%	2.12%	-$298,743	**$781,048**	vs	**$1,452,758**	10.80%

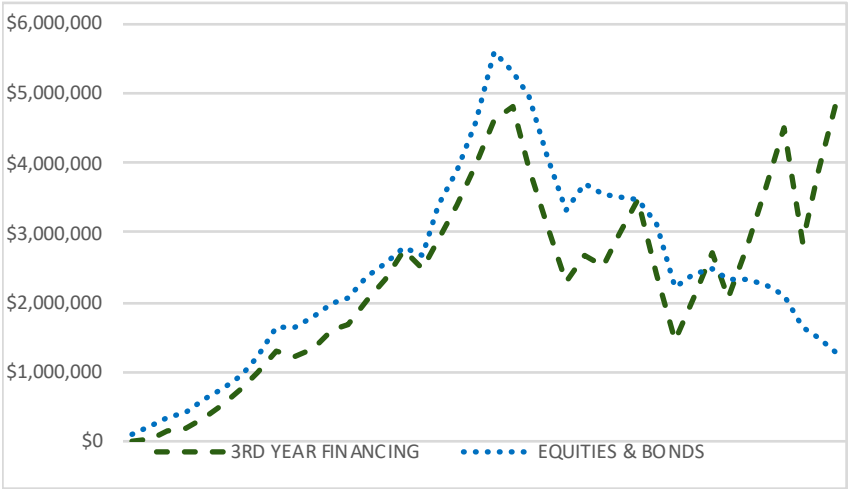
Average Equities Return: **10.02%** **Average T-Bond Return:** **3.46%** **Average Net Portfolio Return:** **6.07%** **WORST 40**

Above is the *Hypothetical Equities & Bonds Account* during the same 40-year period that produced the *Worst Compounded Annual Growth Rate* out of the 121 different 40-year periods analyzed. The *After-Tax Account Value* (column 13) shows the net values of this *Hypothetical Equities & Bonds Account* year-by-year based on drawing down the same income amounts as the *Leveraged Hypothetical Synthetic Asset*.

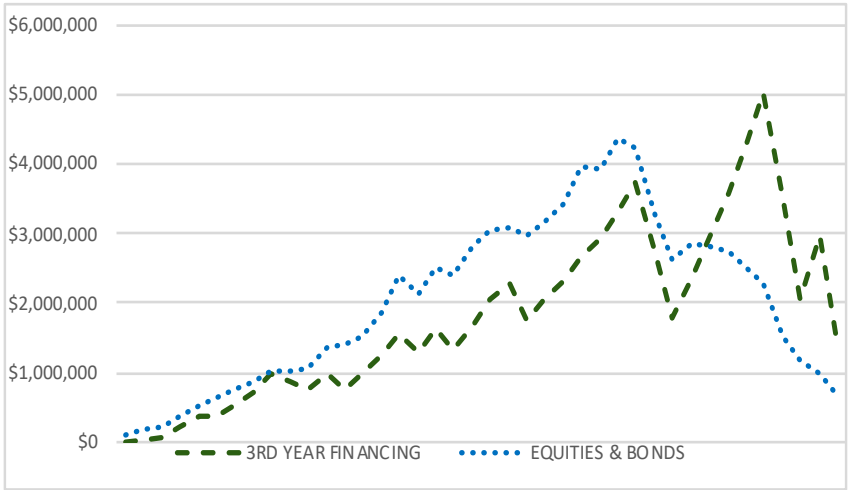
In year 33, the net value of the *Leveraged Hypothetical Synthetic Asset (LHSA)* eclipses the account value of the *Hypothetical Equities & Bonds Account (HEBA)*, and from that point forward, the *LHSA* drastically outperforms the *HEBA*. Again, this assumes the *HEBA* is only being taxed at 22.00% in short-term capital gains tax and 15.00 long-term capital gains tax, as well as only incurring an all-in investment fee of 0.16%.

Below are two graphs that depict the ongoing account balances in each strategy, during the *Best 40* and the *Worst 40* periods. The heavily dashed line represents the account value (net of loans) in the *Leveraged Hypothetical Synthetic Asset (LHSA)* model, and the lightly dotted line represents the *Hypothetical Equities & Bonds Account (HEBA)*.

BEST CAGR PERIOD OUT OF 121 DIFFERENT 40-YEAR S&P PERIODS ANALYZED

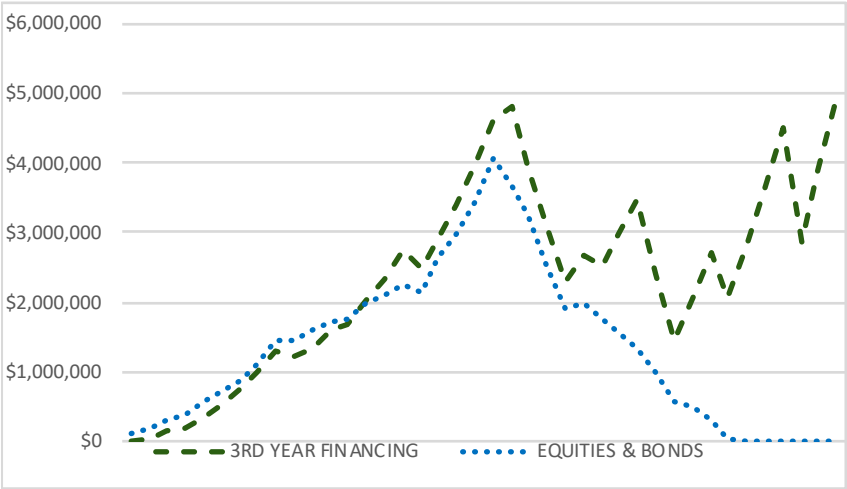


WORST CAGR PERIOD OUT OF 121 DIFFERENT 40-YEAR S&P PERIODS ANALYZED

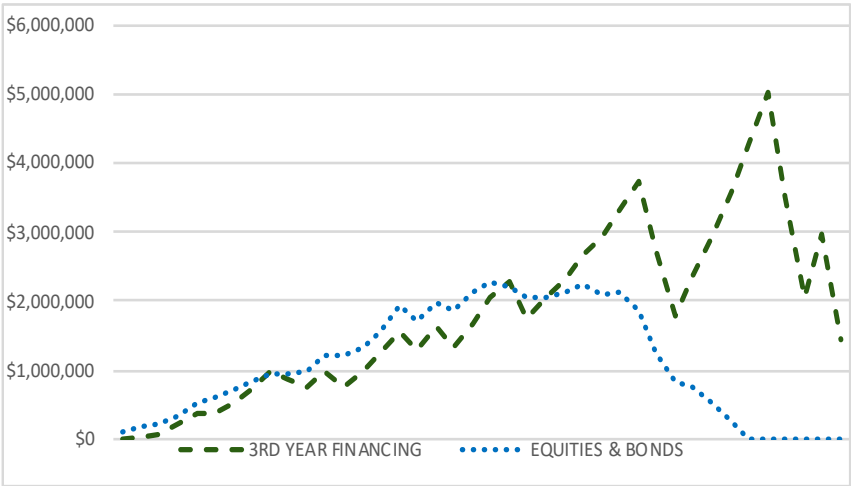


If however the short-term capital gains tax rate was 38.80% (instead of only 22.00%) and the long-term capital gains tax rate was 23.80% (instead of only 15.00%, and if the all-in investment fee was 1.00% (instead of only 16 bps), the *HEBA* would be drawn down to zero value in year 35 during the *Best 40*, and year 36 during the *Worst 40*, whereas the *LHSA* would continue providing income drawdowns and still have a positive account value past year 40.

BEST CAGR PERIOD OUT OF 121 DIFFERENT 40-YEAR S&P PERIODS ANALYZED



WORST CAGR PERIOD OUT OF 121 DIFFERENT 40-YEAR S&P PERIODS ANALYZED



As you can see, using this *Third-Year Financing* arrangement can be a fantastic addition to an overall retirement portfolio above and beyond a mere death benefit.

I have a financed policy on myself as well as one on my wife for this very purpose.

I don't know many people that think income taxes are going to decrease in the future. In fact, it has been my experience that the large majority of people believe income taxes in this country will undoubtedly increase over time, and so using *Premium Financed Life Insurance* as a supplemental retirement strategy is extremely appealing for the purposes of creating:

1. A tax-free income stream.
2. Participating loan positive arbitrage potential.
3. A risk mitigation strategy with the *IUL's* 0.00% floor.
4. Leverage using lender capital while deploying cash flow elsewhere.
5. A windfall of tax-free funds for heirs in the event of the insured's premature death.

Again, the proof is in the math. Having the backtesting modeling abilities to mathematically draw comparisons of net outcomes is the only way to know whether or not these types of solutions make sense for specific clients.

Chapter 13
All That Glitters

When it comes to *Premium Financed Life Insurance,* all that glitters ain't gold. There are several gimmicks that some premium financing designs use to make their value propositions appear greater than what they actually are.

There is no such thing as a free lunch in *Premium Financed Life Insurance.* In addition, there are some gimmicks that I believe lure the wrong type of clients into premium financing, creating an unsuitable arrangement for all parties involved. Not everyone should finance their life insurance premiums, but not because the math doesn't work, and not because the risk is too high.

The reason I say that *Premium Financed Life Insurance* is not a suitable strategy for some people is that it typically requires substantial liquidity – not *stated liquidity* or *future/aspirational liquidity* – but current liquidity.

But if a client's net worth is truly equal to or greater than the carrier's requirements, and their current liquidity is greater than the projected peak collateral in our *Leveraged Hypothetical Synthetic Asset* (the proxy for the premium financed *IUL*) during the 40-year period with the *Worst Compounded Annual Growth Rate*… AND assuming the client doesn't mind posting that amount as collateral (not touching it until the lender's collateral requirement outside the policy value is zero), premium financing is most likely a suitable strategy for them.

However if the client does not have the liquid assets required by the lender to use as collateral, premium financing is just not a viable option for them. One exception to the rule is that if they can get their own lender to post a *Letter Of Credit* against one of their illiquid assets – like real estate or crypto currency for example – perhaps *Premium Financed Life Insurance* is suitable for them. The other exception to the rule is if they use the *Third-Year Financing With Zero Collateral* design I talked about in Chapter 12 of this book.

FIRST-DOLLAR FINANCING

Health Rating: **PREFERRED**

Initial Gross Policy Face Amount: **$11,238,426**

YEAR	AGE	1 TOTAL POLICY PREMIUMS	2 PREMIUMS PAID BY CLIENT	3 PREMIUMS PAID BY LENDER	4 CUMULATIVE PF LOAN BALANCE	5 FINANCING INTEREST RATE	6 INTEREST DUE	7 INTEREST ACCRUED	8 CLIENT CONTRIBUTION	9 ESTIMATED COLLATERAL	10 HYPOTHETICAL INDEX CREDIT	11 POLICY DRAWDOWNS	12 GROSS ACCUMULATED VALUE	13 POLICY CSV NET OF LOANS	14 DEATH BENEFIT NET OF LOANS	15 DEATH BENEFIT IRR INCLUDING DRAWDOWNS	YEAR	AGE
1	55	$1,000,000	$0	$1,000,000	$1,000,000	1.67%	$16,700	$0	$16,700	$953,996	5.43%	$0	$922,739	-$534,233	$11,161,165	66733.33%	1	55
2	56	$1,000,000	$0	$1,000,000	$2,000,000	1.71%	$34,120	$0	$34,120	$953,996	5.43%	$0	$1,890,731	-$553,836	$11,129,157	2381.37%	2	56
3	57	$1,000,000	$0	$1,000,000	$3,000,000	1.75%	$52,584	$0	$52,584	$1,010,632	5.43%	$0	$2,908,310	-$523,846	$11,146,736	699.79%	3	57
4	58	$1,000,000	$0	$1,000,000	$4,000,000	1.81%	$72,546	$0	$72,546	$1,018,192	5.43%	$0	$3,978,816	-$440,850	$11,217,242	348.49%	4	58
5	59	$1,000,000	$0	$1,000,000	$5,000,000	1.89%	$94,637	$0	$94,637	$972,573	5.43%	$0	$5,105,027	**-$302,089**	**$11,343,453**	**215.98%**	5	59
6	60	$1,000,000	$0	$1,000,000	$6,000,000	2.00%	$119,733	$0	$119,733	$870,101	5.43%	$0	$6,288,864	-$105,682	$11,527,290	150.18%	6	60
7	61	$1,000,000	$0	$1,000,000	$7,000,000	2.13%	$149,045	$0	$149,045	$708,716	5.43%	$0	$7,532,103	$150,091	$11,770,529	111.95%	7	61
8	62	$1,000,000	$0	$1,000,000	$8,000,000	2.30%	$184,239	$0	$184,239	$427,649	5.43%	$0	$8,836,880	$526,661	$12,075,306	87.37%	8	62
9	63	$1,000,000	$0	$1,000,000	$9,000,000	2.53%	$227,599	$0	$227,599	$0	5.43%	$0	$10,206,309	$1,051,200	$12,444,735	70.40%	9	63
10	64	$1,000,000	$0	$1,000,000	$10,000,000	2.82%	$282,254	$0	$282,254	$0	5.43%	$0	$11,642,313	**$1,642,313**	**$12,880,739**	**58.04%**	10	64
11	65	$0	$0	$0	$10,000,000	3.20%	$320,430	$0	$320,430	$0	5.43%	$0	$12,287,052	$2,287,052	$12,880,739	47.92%	11	65
12	66	$0	$0	$0	$10,000,000	3.70%	$370,059	$0	$370,059	$0	5.43%	$0	$12,966,175	$2,966,175	$12,880,739	39.95%	12	66
13	67	$0	$0	$0	$10,000,000	4.35%	$434,577	$0	$434,577	$0	5.43%	$0	$13,682,252	$3,682,252	$12,880,739	33.49%	13	67
14	68	$0	$0	$0	$10,000,000	5.18%	$518,450	$0	$518,450	$0	5.43%	$0	$14,438,043	$4,438,043	$12,880,739	28.10%	14	68
15	69	$0	$0	$0	$10,000,000	6.27%	$627,485	$0	$627,485	$0	5.43%	$0	$15,236,640	**$5,236,640**	**$12,880,739**	**23.49%**	15	69
16	70	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$10,000,000	$15,931,682	$5,531,682	$12,480,739	20.02%	16	70
17	71	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$16,655,158	$5,367,642	$11,593,223	17.27%	17	71
18	72	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$17,409,329	$5,198,798	$10,670,208	15.05%	18	72
19	73	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$18,196,892	$5,026,424	$9,710,271	13.22%	19	73
20	74	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$19,021,209	**$4,852,407**	**$8,711,937**	**11.69%**	20	74
21	75	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$19,886,243	$4,679,175	$7,673,670	10.36%	21	75
22	76	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$20,797,314	$4,510,447	$6,593,872	9.19%	22	76
23	77	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$21,761,173	$4,351,317	$5,470,882	8.13%	23	77
24	78	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$22,786,106	$4,208,340	$5,347,645	8.07%	24	78
25	79	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$23,852,205	**$4,059,814**	**$5,252,424**	**8.04%**	25	79
26	80	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$24,959,361	$3,903,759	$5,151,727	8.02%	26	80
27	81	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$26,108,711	$3,739,369	$5,044,804	8.00%	27	81
28	82	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$27,301,154	$3,565,523	$4,930,581	7.99%	28	82
29	83	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$28,537,511	$3,380,940	$4,807,816	7.97%	29	83
30	84	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$29,818,462	**$3,184,113**	**$4,675,036**	**7.96%**	30	84
31	85	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$31,143,718	$2,972,479	$4,529,665	7.95%	31	85
32	86	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$32,513,168	$2,743,565	$4,369,223	7.94%	32	86
33	87	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$33,926,350	$2,494,448	$4,190,765	7.92%	33	87
34	88	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$35,382,076	$2,221,382	$3,990,486	7.91%	34	88
35	89	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$36,878,748	**$1,920,111**	**$3,764,049**	**7.90%**	35	89
36	90	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$38,415,017	$1,586,519	$3,507,270	7.88%	36	90
37	91	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$40,007,012	$1,233,860	$2,834,140	7.76%	37	91
38	92	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$41,665,207	$869,613	$2,119,569	7.65%	38	92
39	93	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$43,402,542	$503,610	$1,371,661	7.55%	39	93
40	94	$0	$0	$0	$0	0.00%	$0	$0	$0	$0	5.43%	-$453,380	$45,235,162	**$148,757**	**$601,109**	**7.47%**	40	94
		-$10,000,000	**$0**	**-$10,000,000**			**$3,504,458**	**$0**	***$3,504,458***	***INCOME DRAWN DOWN:***		***-$10,881,120***						

But in most cases, when a client says they have the liquidity but just don't want to post it as collateral, it usually means they don't truly have the liquidity they say they do. When this is the case, the first request I most often get from life insurance agents is to use a *High Early Cash Value Rider*. There are several reasons why I am not a fan of using this gimmick. The first reason is this rider comes at a substantial cost that acts as an eroding factor, making the cash value accumulation suffer over time. The example above uses carrier illustrated numbers assuming a 5.47% index return, $1,000,000 annual premiums, using our *First-Dollar Financing* platform. The third-party lender is paid off in policy year 16 (column 11) using a *Participating Loan Rate* of 5.00%, and income drawdowns are taken using the same *Participating Loan Rate* of 5.00%. This model above does NOT use the *High Early Cash Value Rider (HECVR)*, however I will also show the exact same policy with the *HECVR* for comparative purposes so you can see the difference in income drawdowns. This particular version above is illustrated using a 5.43% index credit, and the carrier as-illustrated depiction shows annual income drawdowns of $453,380 starting in policy year 17 (column 11) and continuing through policy year 40 (client age 94). The *Gross Accumulated Value* is $45,235,162 in year 40 (column 12) and a *Policy Cash Surrender Value Net Of Loans* (which includes internal *Participating Loan* balances) of $148,757.

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FIRST-DOLLAR FINANCING

Health Rating: **PREFERRED**

Initial Gross Policy Face Amount: **$11,238,426**

YEAR	AGE	1 TOTAL POLICY PREMIUMS	2 PREMIUMS PAID BY CLIENT	3 PREMIUMS PAID BY LENDER	4 CUMULATIVE PF LOAN BALANCE	5 FINANCING INTEREST RATE	6 INTEREST DUE	7 INTEREST ACCRUED	8 CLIENT CONTRIBUTION	9 ESTIMATED COLLATERAL	10 HYPOTHETICAL INDEX CREDIT	11 POLICY DRAWDOWNS	12 GROSS ACCUMULATED VALUE	13 POLICY CSV NET OF LOANS	14 DEATH BENEFIT NET OF LOANS	15 DEATH BENEFIT IRR INCLUDING DRAWDOWNS	YEAR	AGE
1	55	$1,000,000	$0	$1,000,000	$1,000,000	1.67%	$16,700	$0	*$16,700*	$48,309	5.43%	$0	$918,128	-$81,872	$11,156,554	66705.71%	1	55
2	56	$1,000,000	$0	$1,000,000	$2,000,000	1.71%	$34,120	$0	*$34,120*	$48,309	5.43%	$0	$1,876,630	-$123,370	$11,115,056	2379.73%	2	56
3	57	$1,000,000	$0	$1,000,000	$3,000,000	1.75%	$52,584	$0	*$52,584*	$134,667	5.43%	$0	$2,879,366	-$120,634	$11,117,792	699.03%	3	57
4	58	$1,000,000	$0	$1,000,000	$4,000,000	1.81%	$72,546	$0	*$72,546*	$177,174	5.43%	$0	$3,929,158	-$70,842	$11,167,584	347.91%	4	58
5	59	$1,000,000	$0	$1,000,000	$5,000,000	1.89%	$94,637	$0	*$94,637*	$172,287	5.43%	$0	$5,028,224	**$28,224**	**$11,266,650**	**215.45%**	5	59
6	60	$1,000,000	$0	$1,000,000	$6,000,000	2.00%	$119,733	$0	*$119,733*	$116,825	5.43%	$0	$6,177,888	$177,888	$11,416,314	149.67%	6	60
7	61	$1,000,000	$0	$1,000,000	$7,000,000	2.13%	$149,045	$0	*$149,045*	$9,222	5.43%	$0	$7,379,290	$379,290	$11,617,716	111.43%	7	61
8	62	$1,000,000	$0	$1,000,000	$8,000,000	2.30%	$184,239	$0	*$184,239*	$0	5.43%	$0	$8,633,885	$633,885	$11,872,311	86.82%	8	62
9	63	$1,000,000	$0	$1,000,000	$9,000,000	2.53%	$227,599	$0	*$227,599*	$0	5.43%	$0	$9,944,065	$944,065	$12,182,491	69.82%	9	63
10	64	$1,000,000	$0	$1,000,000	$10,000,000	2.82%	$282,254	$0	*$282,254*	$0	5.43%	$0	$11,310,978	**$1,310,978**	**$12,549,404**	**57.42%**	10	64
11	65	$0	$0	$0	$10,000,000	3.20%	$320,430	$0	*$320,430*	$0	5.43%	$0	$11,935,598	$1,935,598	$12,549,404	47.37%	11	65
12	66	$0	$0	$0	$10,000,000	3.70%	$370,059	$0	*$370,059*	$0	5.43%	$0	$12,593,253	$2,593,253	$12,549,404	39.45%	12	66
13	67	$0	$0	$0	$10,000,000	4.35%	$434,577	$0	*$434,577*	$0	5.43%	$0	$13,286,386	$3,286,386	$12,549,404	33.03%	13	67
14	68	$0	$0	$0	$10,000,000	5.18%	$518,450	$0	*$518,450*	$0	5.43%	$0	$14,017,612	$4,017,612	$12,549,404	27.67%	14	68
15	69	$0	$0	$0	$10,000,000	6.27%	$627,485	$0	*$627,485*	$0	5.43%	$0	$14,789,853	**$4,789,853**	**$12,549,404**	**23.07%**	15	69
16	70	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$10,000,000*	$15,456,549	$5,056,549	$12,149,404	19.63%	16	70
17	71	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$16,150,076	$4,903,409	$11,302,736	16.90%	17	71
18	72	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$16,872,507	$4,745,306	$10,422,203	14.69%	18	72
19	73	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$17,626,303	$4,583,347	$9,506,447	12.87%	19	73
20	74	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$18,414,550	**$4,419,209**	**$8,554,062**	**11.34%**	20	74
21	75	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$19,240,856	$4,255,034	$7,563,581	10.01%	21	75
22	76	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$20,110,118	$4,094,195	$6,533,481	8.84%	22	76
23	77	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$21,028,591	$3,941,365	$5,462,177	7.77%	23	77
24	78	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$22,003,949	$3,802,567	$4,902,764	7.29%	24	78
25	79	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$23,029,889	**$3,669,785**	**$4,821,279**	**7.30%**	25	79
26	80	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$24,095,479	$3,530,303	$4,735,077	7.30%	26	80
27	81	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$25,201,825	$3,383,375	$4,643,466	7.31%	27	81
28	82	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$26,349,810	$3,227,954	$4,545,445	7.31%	28	82
29	83	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$27,540,236	$3,062,839	$4,439,851	7.31%	29	83
30	84	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$28,773,774	**$2,886,614**	**$4,325,302**	**7.32%**	30	84
31	85	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$30,050,160	$2,696,846	$4,199,354	7.32%	31	85
32	86	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$31,369,304	$2,491,191	$4,059,656	7.32%	32	86
33	87	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$32,730,779	$2,266,875	$3,903,414	7.31%	33	87
34	88	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$34,133,458	$2,020,330	$3,727,003	7.31%	34	88
35	89	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$35,575,821	**$1,747,501**	**$3,526,292**	**7.30%**	35	89
36	90	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$37,056,589	$1,444,469	$3,297,298	7.28%	36	90
37	91	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$38,591,348	$1,124,076	$2,667,730	7.16%	37	91
38	92	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$40,190,223	$793,593	$1,999,300	7.04%	38	92
39	93	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$41,865,726	$462,564	$1,299,878	6.94%	39	93
40	94	$0	$0	$0	$0	0.00%	$0	$0	*$0*	$0	5.43%	*-$414,103*	$43,633,453	**$143,498**	**$579,832**	**6.84%**	40	94
		-$10,000,000	**$0**	**-$10,000,000**			**$3,504,458**	**$0**	***$3,504,458***	***INCOME DRAWN DOWN:***		***-$9,938,472***						

However this alternative ledger above illustrates the same exact same product from the exact same carrier, but it includes the *High-Early Cash Value Rider (HECVR)*. The policy is also illustrated at the same 5.43% index credit assumption using our *First-Dollar Financing* platform. The third-party lender is paid off in policy year 16 (column 11) using the same *Participating Loan Rate* of 5.00%, and income drawdowns are taken using the same *Participating Loan Rate* of 5.00%. Notice the income drawdowns in the policy WITH the *HECVR* are only $414,103 compared to $453,380 in the policy WITHOUT the *HECVR* (column 16). Over this 40-year period, that's a difference of $942,648 in total income drawdowns (favoring the design without the *HECVR*).

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The reason for this huge disparity in income drawdowns is due to the additional charges the policy incurs with the *HECVR*. In this particular comparison, there are $260,606 in additional charges in the policy due to the *HECVR*.

$3,979,862 Total Policy Charges with HECVR
- $3,719,256 Total Policy Charges without HECVR
$260,606 Additional Policy Charges with HECVR

There is only one reason why someone would ever use a *HECVR* despite the charges creating such a drag on performance: They want to minimize the outside collateral required in the early years (compare column 9 in this example below versus the column 9 in the previous example without the *HECVR*).

There is definitely a trade-off that comes with lowering expected collateral requirement amounts in the form of lowering expected income drawdown amounts (and cash value accumulation) when it comes to using a *HECVR* in an *IUL*. In a death benefit-focused design, this rider will also reduce the cash value as well as the death benefit in the later years of the policy.

The decision to give up $942,648 of income (or accept lesser cash value and a lower death benefit) can only be justified if they have significant illiquid assets that the premium financing lender will not accept as collateral (e,g., real estate or crypto currency), and they just don't have the liquidity. If they have a long-standing relationship with their current bank, they should be able to have them issue a *Letter Of Credit* against their illiquid assets, and this *Letter Of Credit* is deemed as acceptable collateral by most premium financing lenders.

However for the most part, a client financing a large amount of premium should only be doing so if they have the liquid collateral to do so. In many cases, lenders will allow the client to keep the assets with the current custodian, and if the assets are marketable securities, they can usually keep those assets exactly as they are.

Premium financing lenders will typically give the client 70% credit for such marketable securities if they are going to post them as collateral. As an example, if the lender's required collateral is $700,000 in cash, and the client wanted to use marketable securities instead of cash, they would have to post $1,000,000 of these securities as collateral ($1,000,000 x 70% = $700,000). So if the client has enough liquid collateral sitting in an investment account that they don't need to touch for 7-9 years anyway, there should not be an issue with them posting it as collateral on the premium financing loan.

But perhaps the biggest reason I am not a fan of *HECVRs* has nothing to do with how the drag of the additional charges erode cash value accumulation. It isn't the chargeback liability for the agent either.

The biggest concern I have regarding *HECVRs* is the message it sends to the client, which is, "You can exit this arrangement with little or no penalty."

In theory, this flexibility sounds like a good thing. However using this flexibility as a selling tactic sends the wrong message to the client. Any financial strategy that uses a cash value life insurance policy – financed or not – should be a long-term strategy. If the client enters the arrangement under the wrong premise – focusing on early exit options as an example – a life insurance-based solution is probably not appropriate for this particular type of client.

Though this analogy may be a crass one, if a single person just won the lottery and walked into a bar with a t-shirt that said, "I'm a $100,000,000 lottery winner, and I'll buy you anything you want," I'm not so sure they are going to attract the right person. Now, there is nothing wrong with being a $100,000,000 lottery winner, and there is nothing wrong with buying someone you love anything they want, but if that is the message a person leads with when engaging in a new relationship, it is harder to know what the other person's true intentions are.

As a *Premium Financed Life Insurance* intermediary, I believe it is my duty to identify whether or not the client's true intentions are to utilize this strategy for what was designed to do – to provide a long-term wealth building solution, or to be used as an effective estate planning tool. This is not a get-rich-quick scheme, a get-something-for-nothing ploy, or a short-term investment.

I want to know that the client is committed to this as a long-term strategy and that they have the liquidity and emotional fortitude to stay the course and weather any short-term financial storms should they come.

Yes, there is an element of risk in premium financing, but if designed properly, it is no more risky that buying a home with a mortgage loan. In fact, I could make the argument that a well-designed *Premium Financed Life Insurance* arrangement is far less risky because the likelihood of the policy value deteriorating as drastically as the housing market can is infinitesimally smaller.

But as I repeatedly stated over and over in this book, the only way to really understand whether or not a premium financing arrangement is mathematically sound is to create a proxy for the *IUL*, build in pessimistic assumptions, and backtest the design throughout different historical periods of time wherein the index experienced volatility.

My firm, *Lionsmark Capital*, is the only premium financing intermediary that has the ability to do this. In my humble opinion, this is the only true test of whether or not a *Premium Financed Life Insurance* arrangement is a prudent financial strategy.

In closing, I will reiterate the importance of not only understanding *The Probability Of Risk*, but more importantly, *The Consequence Of Risk*. If you are a client that is considering *Premium Financed Life Insurance* as a wealth building or generational wealth preservation strategy, you owe it to your family to insist that the premium financing intermediary you decide to work with is able to do the due diligence I have described in this book and model a range of scenarios with volatility and pessimistic assumptions.

And if you are a life insurance agent or financial advisor that is considering recommending *Premium Financed Life Insurance* to your clients, I cannot emphasize enough the importance of working with an intermediary that truly understands these concepts and can articulately communicate these variables to your clients.

Making a big life insurance sale is great, but it is far more important to make sure you are doing the right thing for the client, and if you can mathematically prove that your recommendation is not only appropriate, but superior to all other available alternative options, you are providing an invaluable service to your clients.

For more information about Darren Sugiyama, visit:
www.DarrenSugiyama.com

For more information about Lionsmark Capital, visit:
www.LionsmarkCapital.com

WWW.DARRENSUGIYAMA.COM