



BANK-OWNED LIFE INSURANCE (BOLI) – SURVEY RESULTS 2017

2017-Q4

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INTRODUCTION & EXECUTIVE SUMMARY

INTRODUCTION

After conducting a “mini-survey” of selected bank clients in 2015 to identify issues of concern regarding BOLI risk management, we were impelled to expand the endeavor to encompass additional topics and a wider stratum of banks. This inaugural survey is the outcome.

While we are pleased with the level of participation in this initial tally (demographics follow), and hope you share our view that the findings include valuable insights, we hope, over the succeeding years, to achieve broader participation, increasing the value of each yearly installment. We’ve done our best to present the results without bias. Your candid feedback is essential if we are to make it increasingly germane and useful to your needs, so please let us know your unvarnished views. Some respondents asked for an opportunity to have input regarding future topics; a proposition we welcome and will incorporate in 2018.

Sincere thanks for taking time out of your demanding schedules to participate!

EXECUTIVE SUMMARY

Distribution

- Survey Links were shared with 82 banking institutions, both with and without existing BOLI, and spanning a wide range of size
- 15 full responses were received, representing 14 banks, all of which own BOLI

Highlights & Reflections

- Measurement of Performance: Yield/ROA was the most prevalent for BOLI assets
- Views regarding BOLI yield attractiveness:
 - GA yields are deemed relatively more attractive than SA yields at present
 - Both GA and SA yields were deemed to be relatively more attractive in rising rate scenarios than at current rates
 - SA yields were deemed most attractive in an environment of gradual rate increases of 300 bps
- Concerns: Of all topics, COI increases, lapse risk, and restrictions on investment flexibility showed the highest levels of concern
- Redirection of vendor comp: Only three respondents said they knew if and to what extent vendor compensation is redirectable
- Impact of 20% tax rate: Moderate to significant impact on new BOLI activity; little consensus on impact to existing holdings
- Basel III: General concern was low; a majority of banks use the full look-through approach

BANK PROFILES

■ State



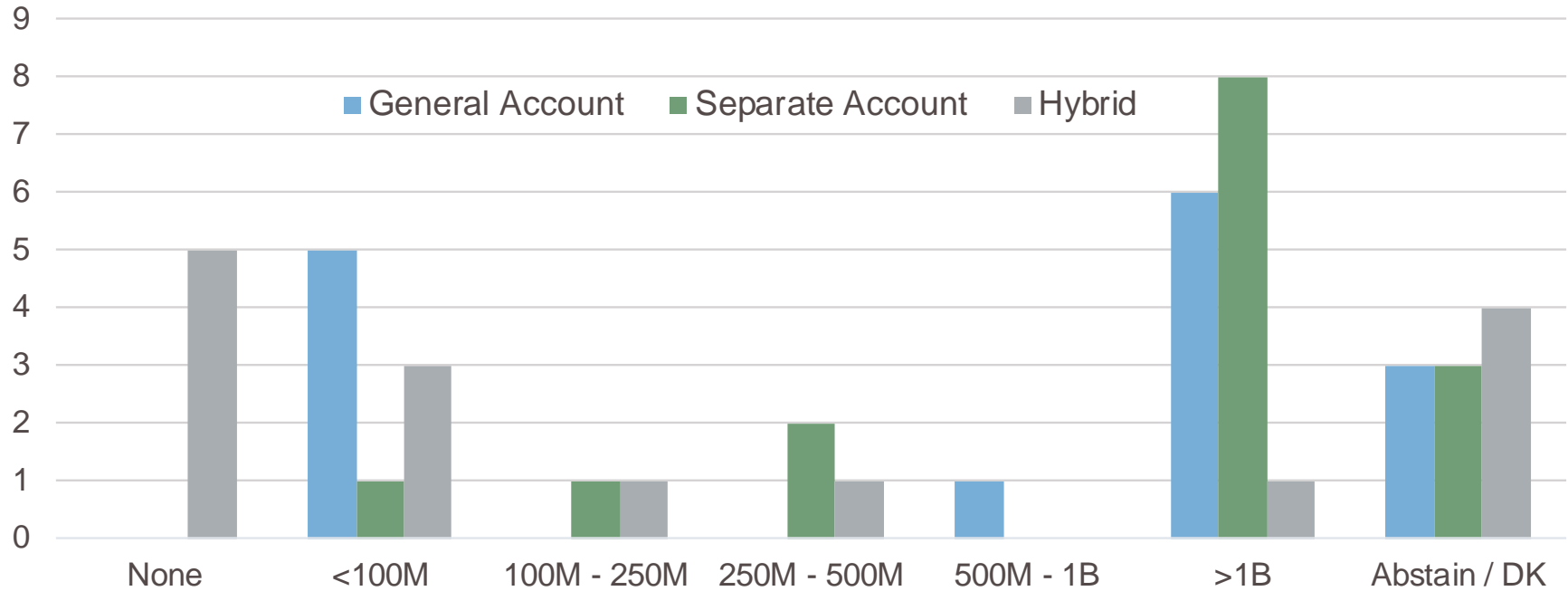
■ National



■ (Abstain)

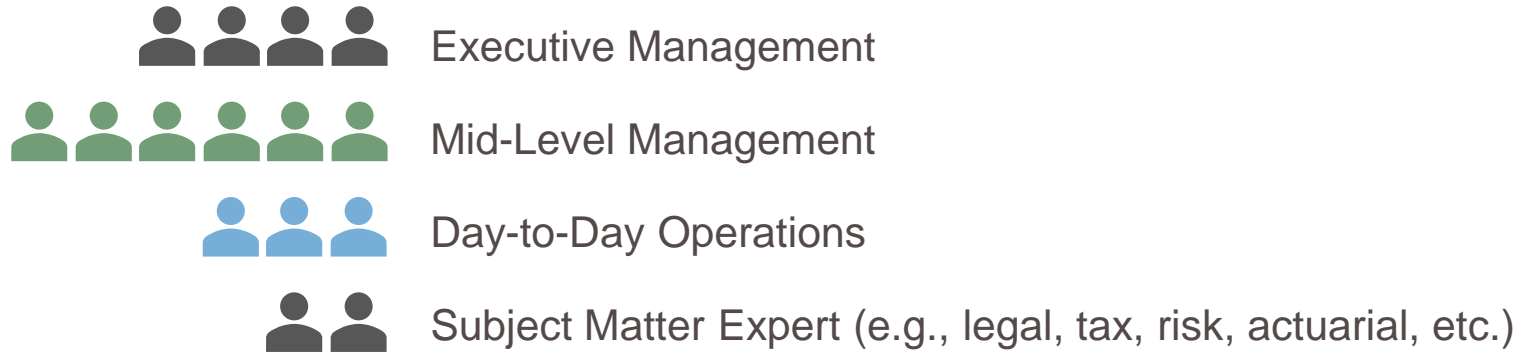


■ BOLI Assets

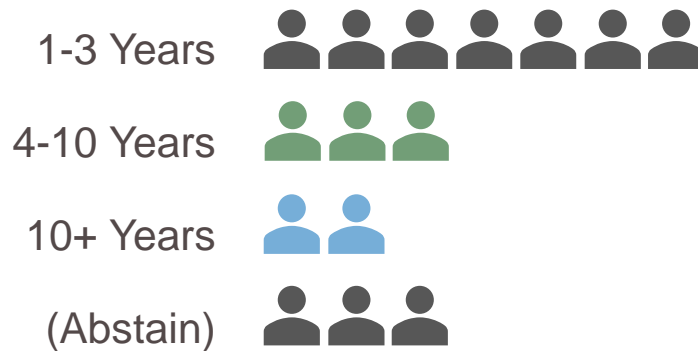


OWNER PROFILES

■ BOLI Program Role



■ BOLI Program Tenure



OWNER PROFILES

■ BOLI Program Responsibilities

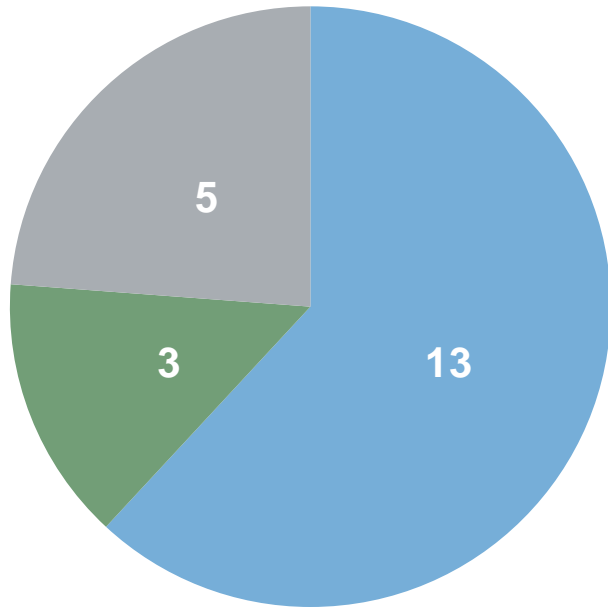
■ Day-to-Day Program Management	12
■ Monitoring Investment Performance	12
■ Monitoring Administration and/or Third Party Administrators	10
■ Senior Management – Oversight	9
■ Monitoring Legal/Compliance Risk	9
■ Monitoring Tax Risk and Issues	9
■ Monitoring Credit Risk	8
■ Primary Decision Maker for New BOLI Transactions	7
■ Primary Decision Maker for Reallocations	5
■ Accounting / Record keeping	0
■ Abstain	1

The average, and most frequent number of roles indicated, was 6

BOLI ECONOMIC FACTORS

BOLI PERFORMANCE

- How do you measure the performance of your BOLI assets? If multiple, select top 2.



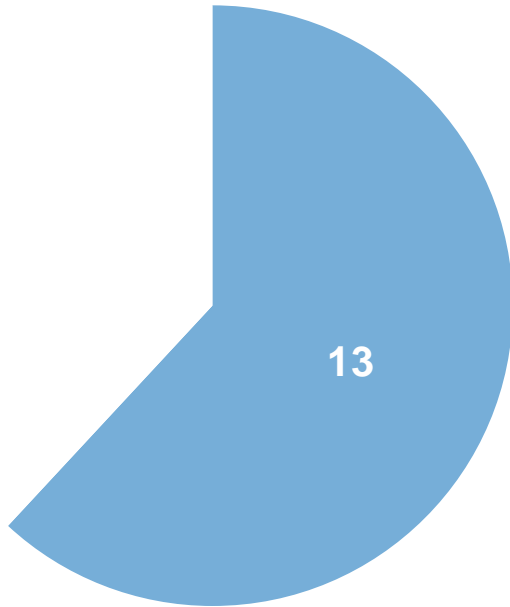
Yield/ROA (Pre-Tax/After Tax)

Return On Capital

Risk-Adjusted Returns

BOLI PERFORMANCE

- How do you measure the performance of your BOLI assets?

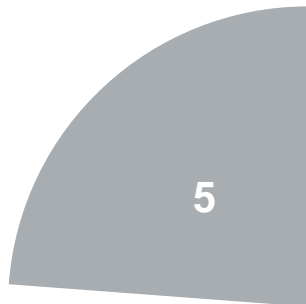


If Yield/ROA (Pre-Tax/After Tax)

What do you identify as an appropriate yield benchmark?	GA	SA
Corporate Bonds with credit qualities commensurate with our carriers' financial strength	5	1
Fixed Income Index (E.g., Bloomberg Barclays Agg or MBS)	5	10
Internally derived hurdle rate	1	1
Other*	1	0

BOLI PERFORMANCE

- How do you measure the performance of your BOLI assets?



If Return on Capital

What do you identify as the capital requirement for BOLI?

Basel III RWA	2
Leverage Ratio	
Greater of Basel III or Leverage Ratio	
Risk Capital	
Internally Derived Fixed Percentage (e.g., 10%)	2
Other*	1

* Submitted Response: "Multi-Metric"

What do you consider the most conceptually appropriate way of viewing BOLI funding cost?

LIBOR	
LIBOR plus a spread	
5-year swap rates	2
Don't know / N/A	1
Other*	1

* Submitted Responses: "Tractor funding"; "Longer term funding cost more in line with the long duration nature of the programs' death benefits"

BOLI PERFORMANCE

- How do you measure the performance of your BOLI assets?

If Risk-Adjusted Returns

What do you identify as the measurement of risk for BOLI?

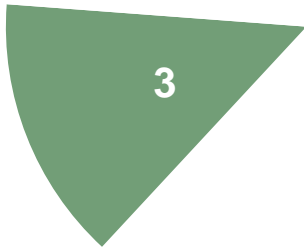
Variability of Returns

Effective Basel III RWA % 2

Duration

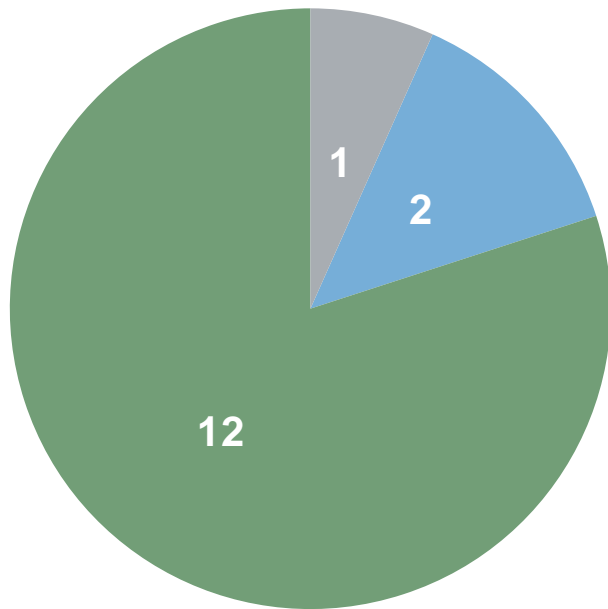
Weighted Average Credit Quality

Other 1



BOLI PERFORMANCE

- When evaluating the performance and attractiveness of BOLI, does your firm apply quantitative risk premia for factors such as illiquidity, compliance risk, or loss of control over investment decisions and administrative complexity? Or are such factors considered only on a qualitative basis?



N/A Don't Know

Yes; we apply quantitative risk premia (or both)

No; these factors are considered on a qualitative basis

ATTRACTIVENESS OF BOLI YIELDS

Participants were asked to rate the attractiveness of both general and separate account BOLI yields under 6 scenarios

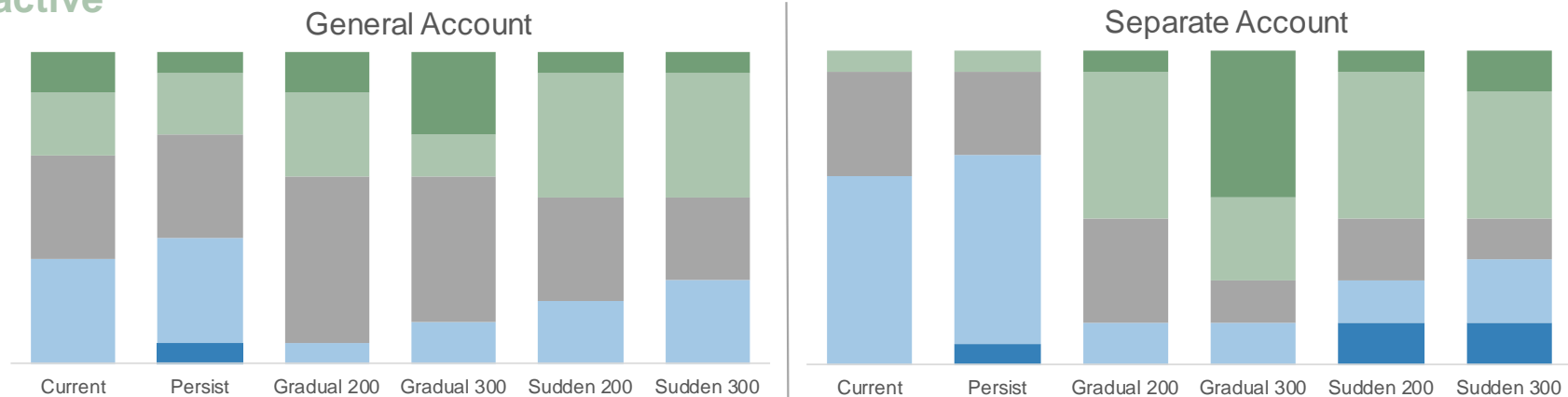
- Current = Current BOLI Yields
- Persist = Longer-term BOLI yields if interest rates persist in a range similar to current
- Gradual 200 / 300 = Longer-term BOLI yields if interest rates *gradually* rise ~200 bps / ~300 bps
- Sudden 200 / 300 = Longer-term BOLI yields if interest rates *suddenly* rise ~200 bps / ~300 bps

Response Frequencies

Very Attractive

Neutral

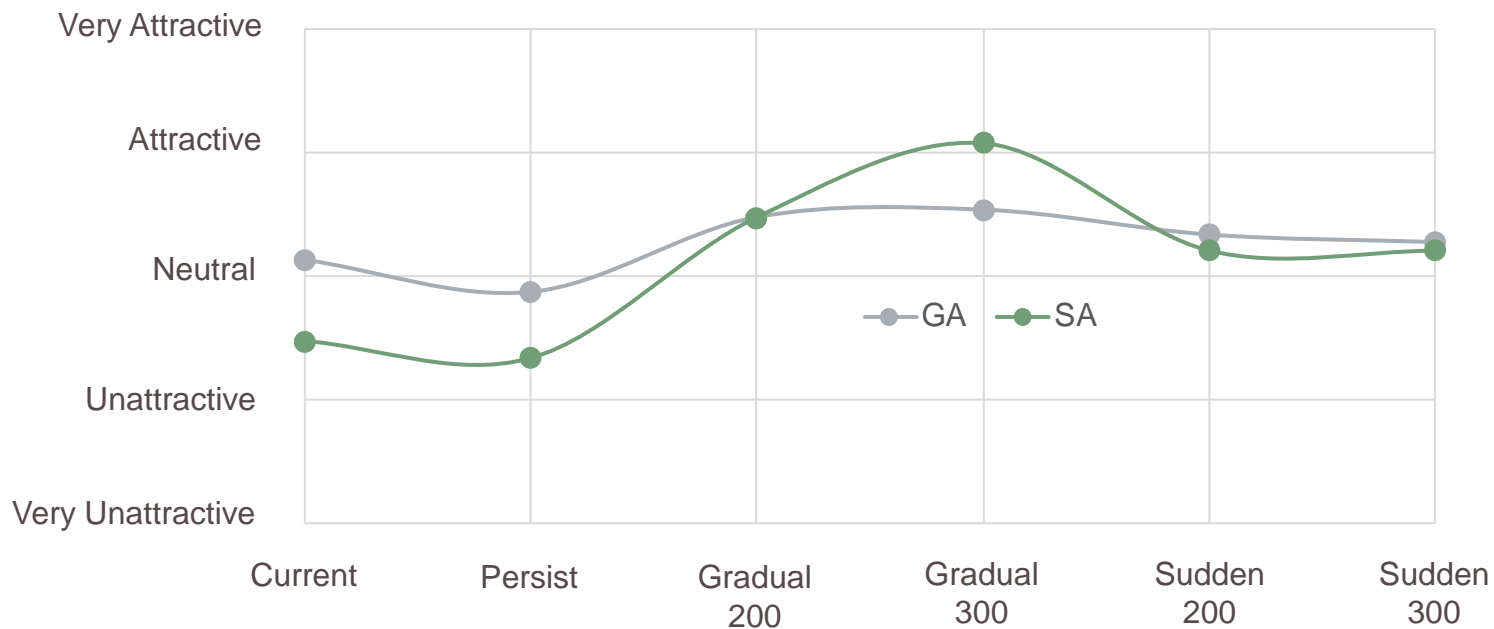
Very Unattractive



ATTRACTIVENESS OF BOLI YIELDS

Response Averages

- General account attractiveness was higher than separate account for current and persisting rates
- Separate account became more attractive than general account as rates climbed
- GA and SA were equally attractive in sudden rate increase scenarios

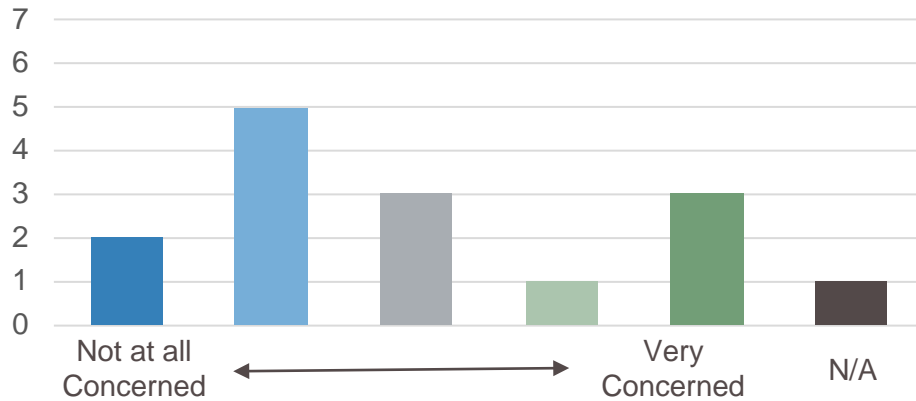


BOLI CONCERNS

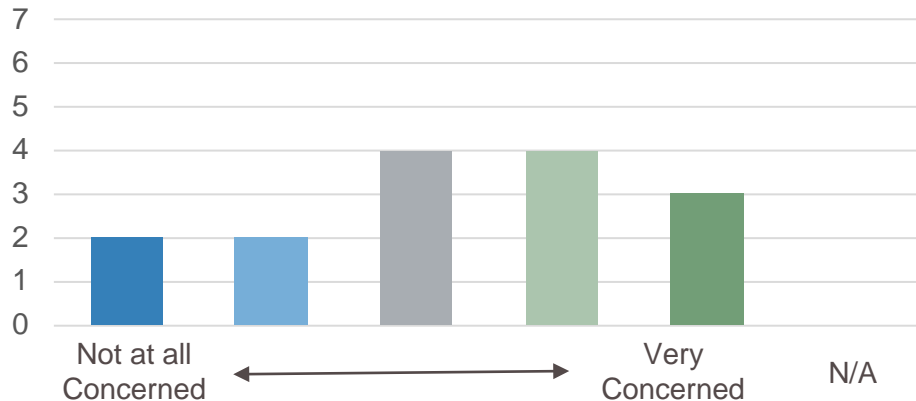
INCREASING COI

How concerned are you about increasing Cost of Insurance (COI) rates?

Existing Policies that have already been impacted



Exposure to similar actions from other carriers



9/15 Expressed elevated concern for increasing COIs

Length of concern

More than 5 years	
2-5 Years	6
1-2 Years	1
Recently arose	1
Don't know / N/A	1

Taken action to address it?

No	4
No, but actively deliberating	3
Yes, internally	1
Yes, external assistance	1
Don't know / N/A	

Did those actions work?

Fully resolved	
Improved, but still a concern	
No improvement	1
Too early to tell	1
Don't know / N/A	

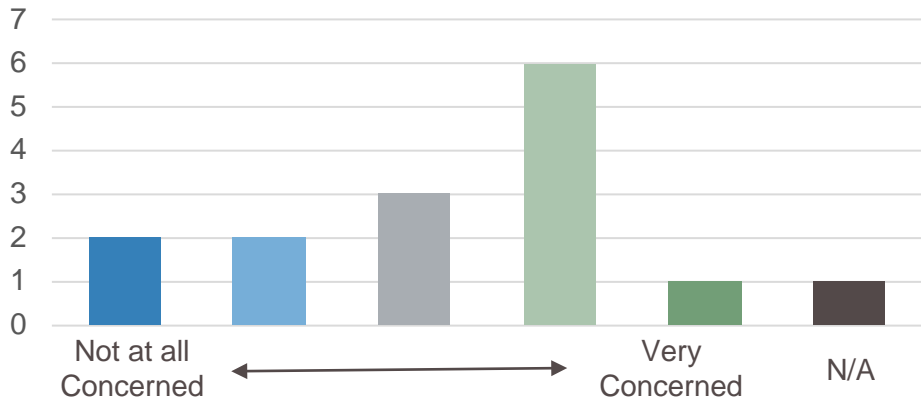
How significant is the impact if left unresolved?

	No Impact	Some Impact	Significant Impact	N/A
Financial	2	4	3	
Regulatory	5	3		1
Administrative/Other	4	4		1

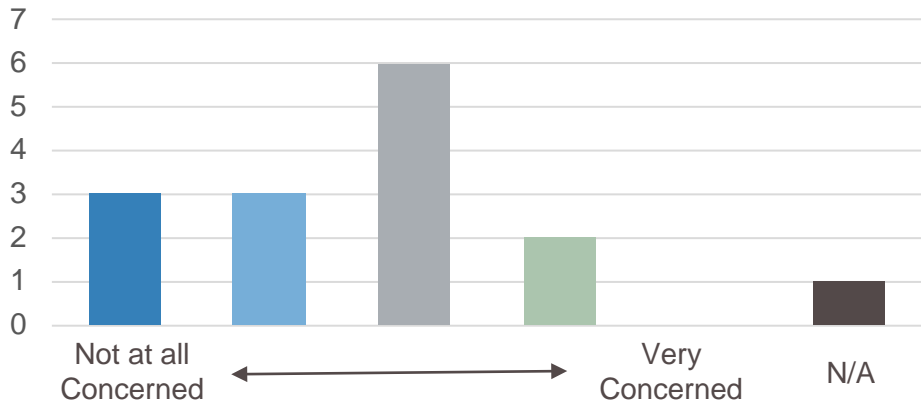
POLICY LAPSES

How concerned are you about the risk that policies will lapse?

If low interest rate environment persists another 5-10 years



If interest rates rise to more historical norms within 5 years



9/15 Expressed elevated concern for policy lapses

Length of concern

More than 5 years	
2-5 Years	3
1-2 Years	3
Recently arose	1
Don't know / N/A	2

Taken action to address it?

No	1
No, but actively deliberating	2
Yes, internally	1
Yes, external assistance	4
Don't know / N/A	1

Did those actions work?

Fully resolved	
Improved, but still a concern	4
No improvement	
Too early to tell	1
Don't know / N/A	

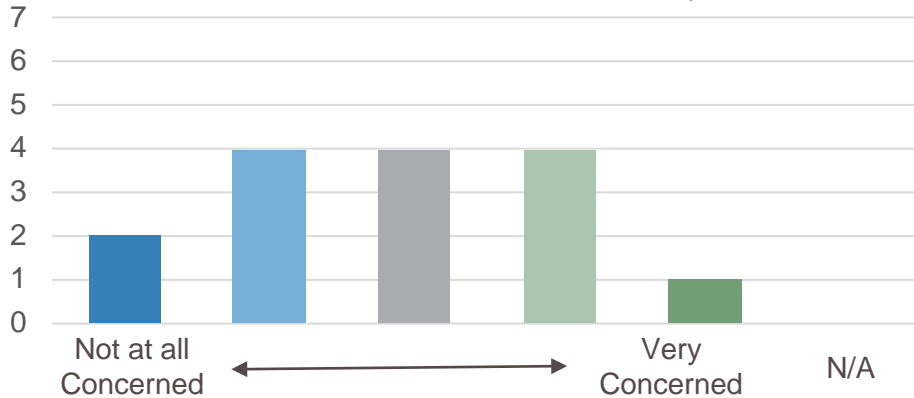
How significant is the impact if left unresolved?

	No Impact	Some Impact	Significant Impact	N/A
Financial	1	5	2	
Regulatory	3	5		1
Administrative/Other	2	6	1	

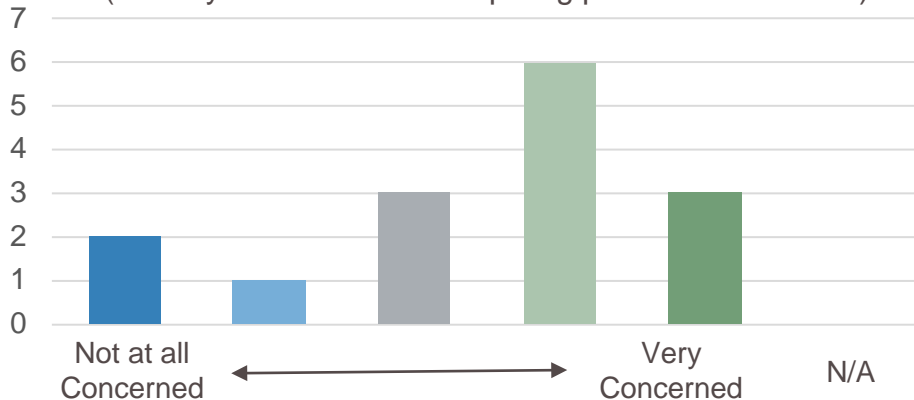
INVESTMENT FLEXIBILITY

How concerned are you about Separate Account BOLI Investment flexibility and/or restrictions?

- Arising from regulatory considerations (e.g., permissibility or restrictions of certain classes of assets)



- Arising from stable value agreement (SVA) considerations (inability to reallocate or requiring permission to do so)



9/15 Expressed elevated concern for SA flexibility

Length of concern	
More than 5 years	1
2-5 Years	3
1-2 Years	2
Recently arose	2
Don't know / N/A	1

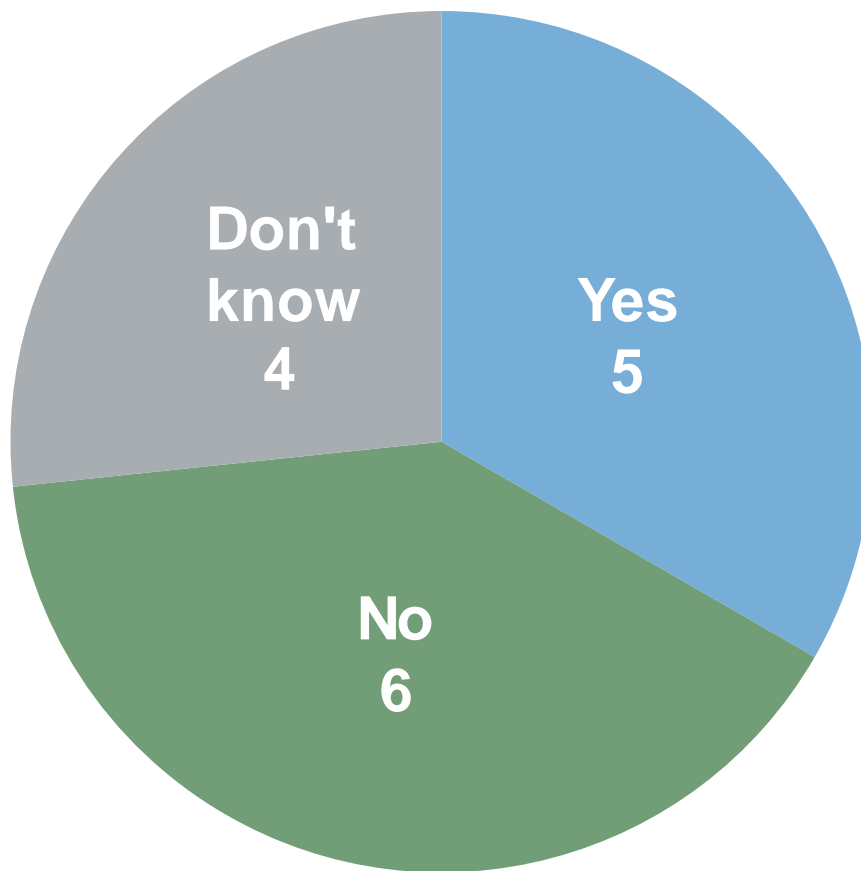
Taken action to address it?		Did those actions work?	
No	1	Fully resolved	1
No, but actively deliberating	4	Improved, but still a concern	2
Yes, internally	1	No improvement	
Yes, external assistance	2	Too early to tell	
Don't know / N/A	1	Don't know / N/A	

	How significant is the impact if left unresolved?			N/A
	No Impact	Some Impact	Significant Impact	
Financial	1	6	2	
Regulatory	4	5		
Administrative/Other	3	6		

IMPACT OF TAX REFORM

TAX REDUCTION

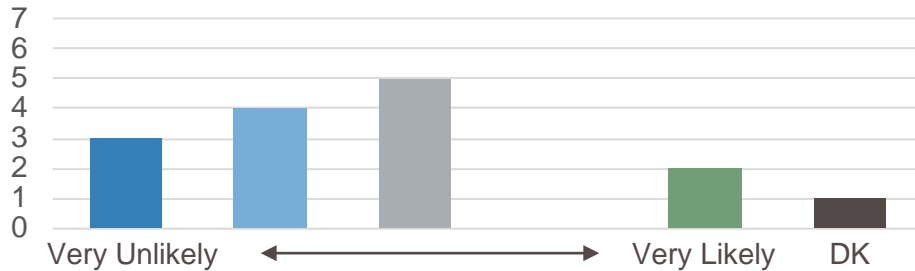
- Do you expect a material reduction in business tax rates during the present administration?



TAX REFORM IMPLICATIONS

How likely do you think it is that tax reform will impact the following?

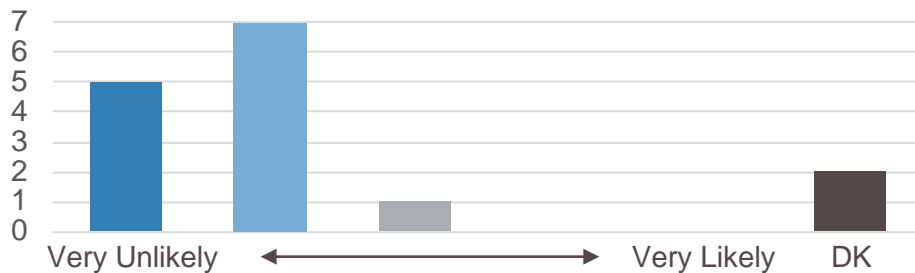
Tax deferral of inside build up



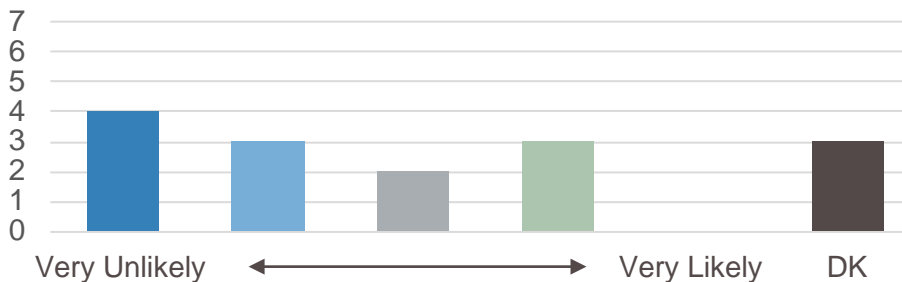
If Likely, Do you think the impact will:

Be prospective only	
Apply to existing contracts	2
Don't know	

Tax free treatment of death proceeds received by employers



Loss of existing exemption from loan interest expense disallowance for policies covering active employees



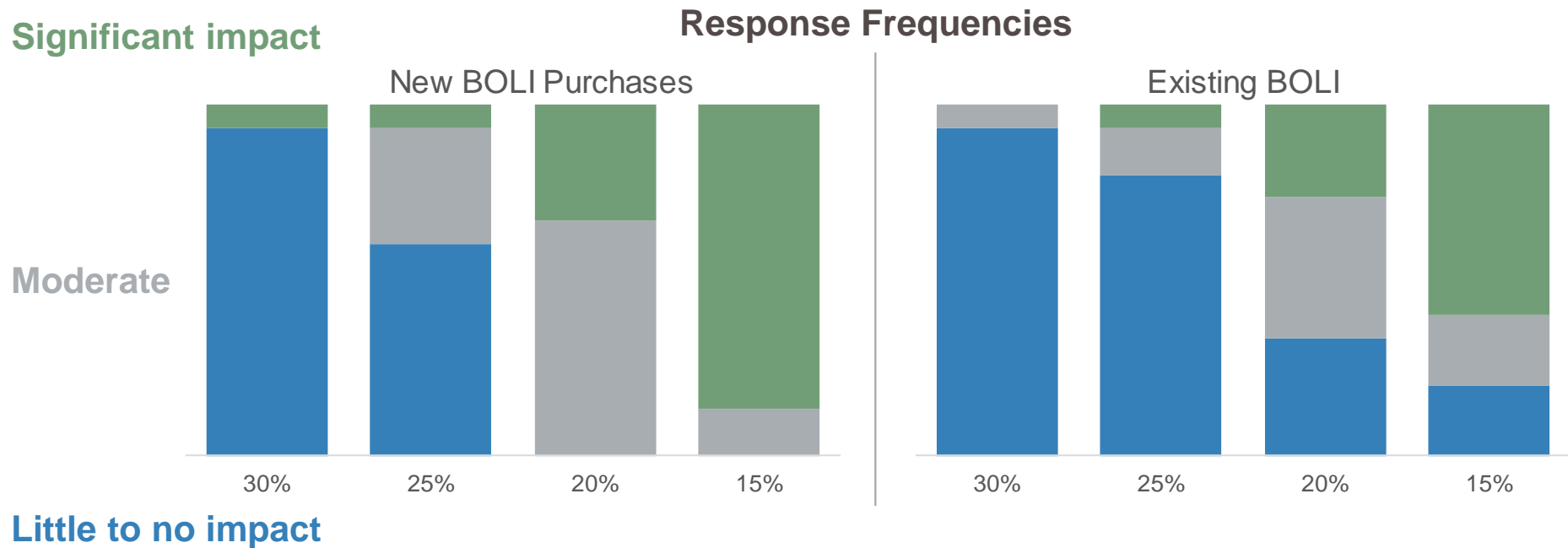
If Likely, Do you think the impact will:

Be prospective only	
Apply to existing contracts	1
Don't know	2

TAX REFORM IMPLICATIONS

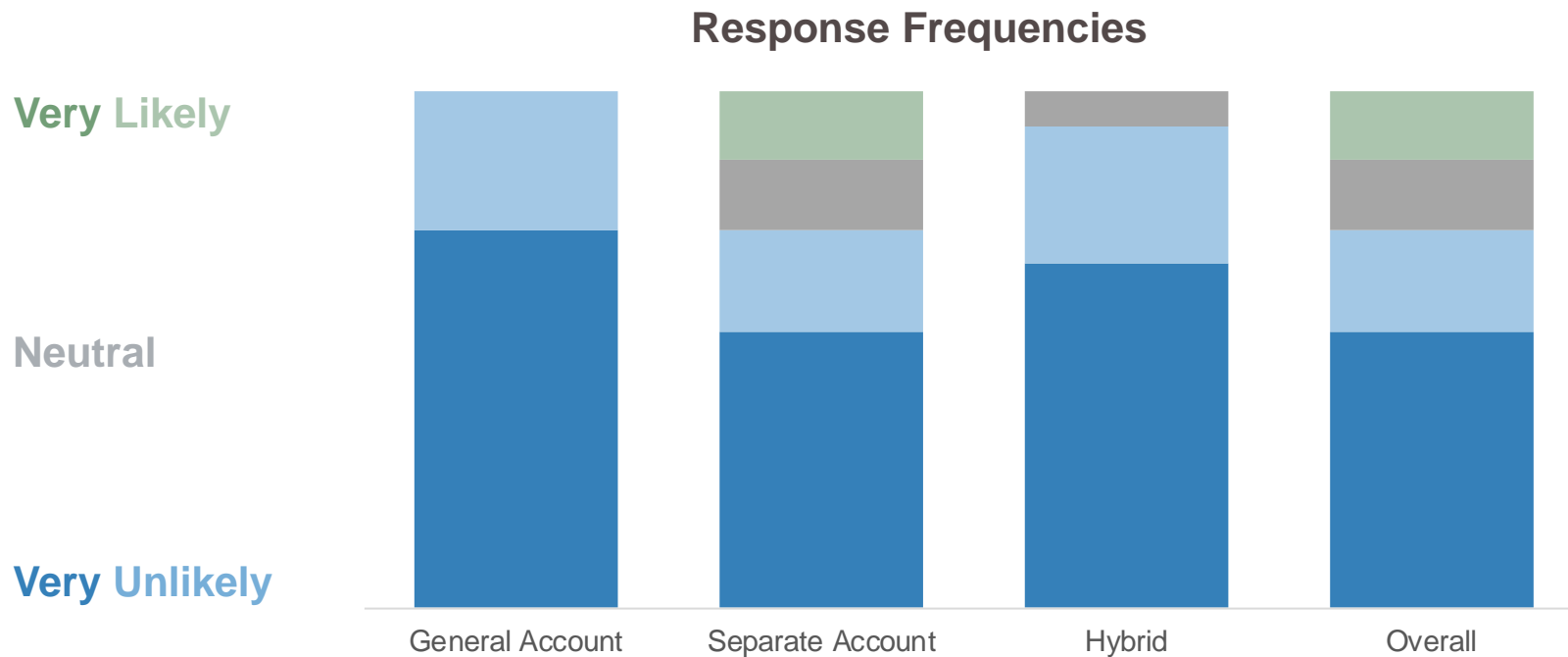
How would BOLI be impacted if corporate tax rates were reduced to the following levels?

- Significant impact (virtually no new contracts will be purchased)
- Moderate impact (only extremely efficient contracts will be purchased)
- Little to no Impact



NEW PURCHASE

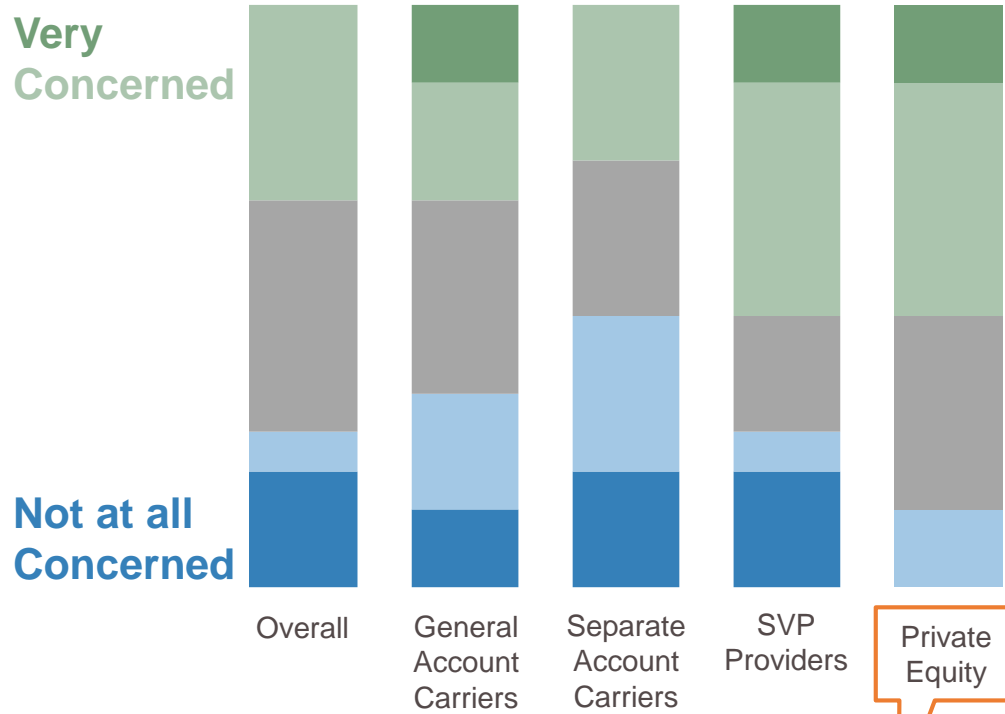
- How likely is your institution to purchase NEW BOLI in the next 2 years?



ADDITIONAL BOLI CONCERNS

RUN OFF BUSINESSES

- How concerned are you about exposure to businesses in run-off?



4/15 Expressed elevated concern for overall run-off exposure

Length of concern	
More than 5 years	1
2-5 Years	2
1-2 Years	
Recently arose	1
Don't know / N/A	

Taken action to address it?	
No	1
No, but actively deliberating	2
Yes, internally	
Yes, external assistance	1
Don't know / N/A	

Did those actions work?	
Fully resolved	
Improved, but still a concern	1
No improvement	
Too early to tell	
Don't know / N/A	

	How significant is the impact if left unresolved?			N/A
	No Impact	Some Impact	Significant Impact	
Financial	1	3		
Regulatory	2	2		
Administrative/Other	1	3		

- How concerned would you be if a private equity investment group acquired a run-off block of business that included BOLI policies you owned?

DEATH CLAIMS

How concerned are you about death claim processing?

- Overall
- Ability to effectively monitor for claims
- Social Security's Death Master File restrictions – impact on claim identification
- Ability to process claims without procuring death certificates



1/15 Expressed elevated concern for death claim processing

Length of concern

More than 5 years	
2-5 Years	1
1-2 Years	
Recently arose	
Don't know / N/A	

Taken action to address it?

No	
No, but actively deliberating	
Yes, internally	
Yes, external assistance	1
Don't know / N/A	

Did those actions work?

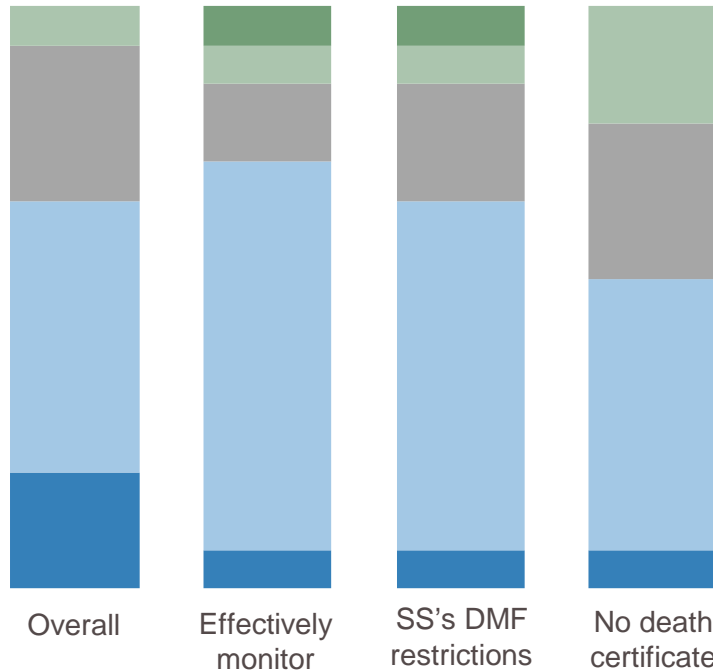
Fully resolved	
Improved, but still a concern	1
No improvement	
Too early to tell	
Don't know / N/A	

How significant is the impact if left unresolved?

	No Impact	Some Impact	Significant Impact	N/A
Financial		1		
Regulatory		1		
Administrative/Other		1		

Very Concerned

Not at all Concerned



RANGE OF RISK CONCERN

- How concerned are you about the overall complexity of managing your BOLI program's range of potential risk areas?

Very Concerned



Not at all Concerned



1/15 Expressed elevated concern for managing BOLI risk areas

Length of concern	
More than 5 years	1
2-5 Years	
1-2 Years	
Recently arose	
Don't know / N/A	

Taken action to address it?		Did those actions work?	
No		Fully resolved	
No, but actively deliberating		Improved, but still a concern	1
Yes, internally		No improvement	
Yes, external assistance	1	Too early to tell	
Don't know / N/A		Don't know / N/A	

	How significant is the impact if left unresolved?			
	No Impact	Some Impact	Significant Impact	N/A
Financial		1		
Regulatory		1		
Administrative/Other		1		

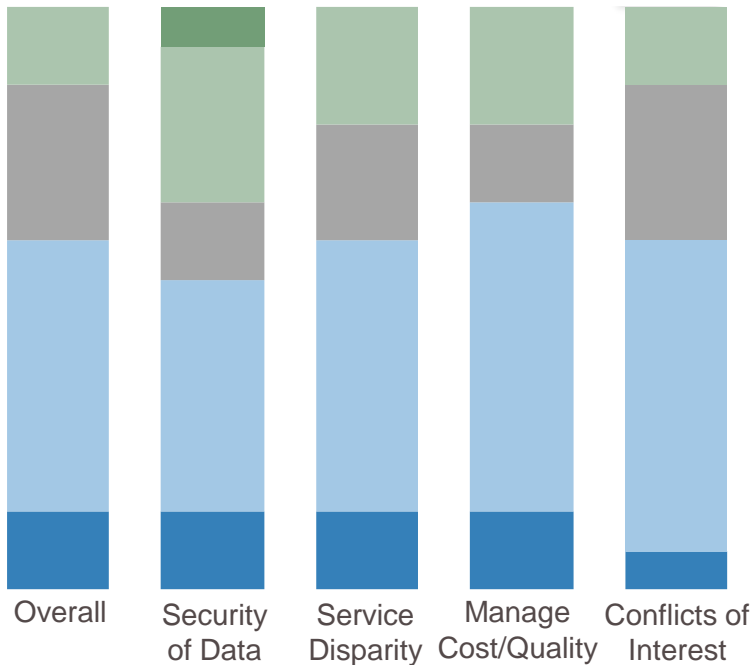
VENDOR MANAGEMENT

How concerned are you about third-party vendor management?

- Overall
- Security of sensitive data
- Disparity in services and expertise of existing BOLI vendors
- Ability to effectively manage cost/quality of work provided
- Conflicts of interest

Very Concerned

Not at all Concerned



2/15 Expressed elevated concern for third-party vendor management

Length of concern	
More than 5 years	1
2-5 Years	
1-2 Years	1
Recently arose	
Don't know / N/A	

Taken action to address it?	
No	
No, but actively deliberating	
Yes, internally	1
Yes, external assistance	1
Don't know / N/A	

Did those actions work?	
Fully resolved	
Improved, but still a concern	2
No improvement	
Too early to tell	
Don't know / N/A	

	How significant is the impact if left unresolved?			
	No Impact	Some Impact	Significant Impact	N/A
Financial		2		
Regulatory		1	1	
Administrative/Other		2		

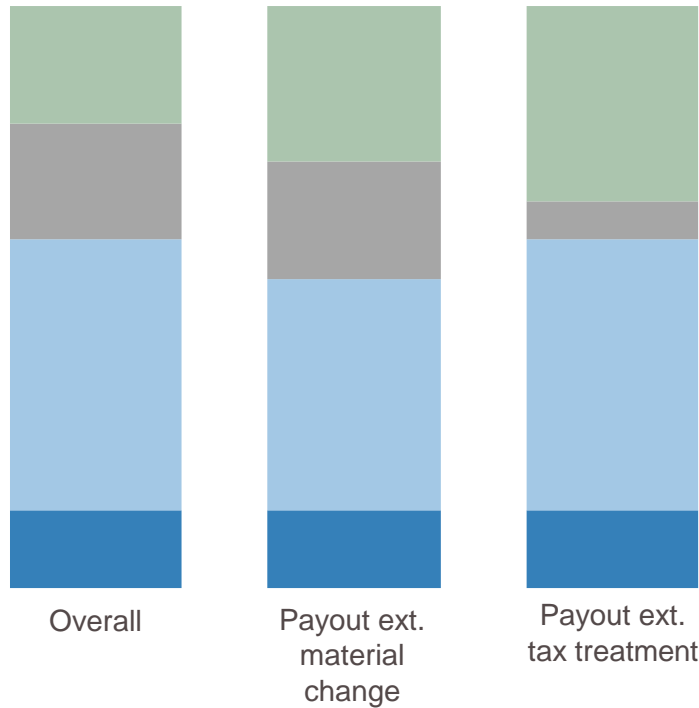
MATURITIES

How concerned are you about policies maturing/ending prior to death?

- Overall
- Uncertainty of tax treatment of adding payout extension riders (e.g., "material change" considerations)
- Uncertainty of tax treatment of payout extension riders

Very Concerned

Not at all Concerned



3/15 Expressed elevated concern for policies maturing before death

Length of concern

More than 5 years	
2-5 Years	1
1-2 Years	
Recently arose	
Don't know / N/A	

Taken action to address it?

No	
No, but actively deliberating	
Yes, internally	
Yes, external assistance	1
Don't know / N/A	

Did those actions work?

Fully resolved	
Improved, but still a concern	1
No improvement	
Too early to tell	
Don't know / N/A	

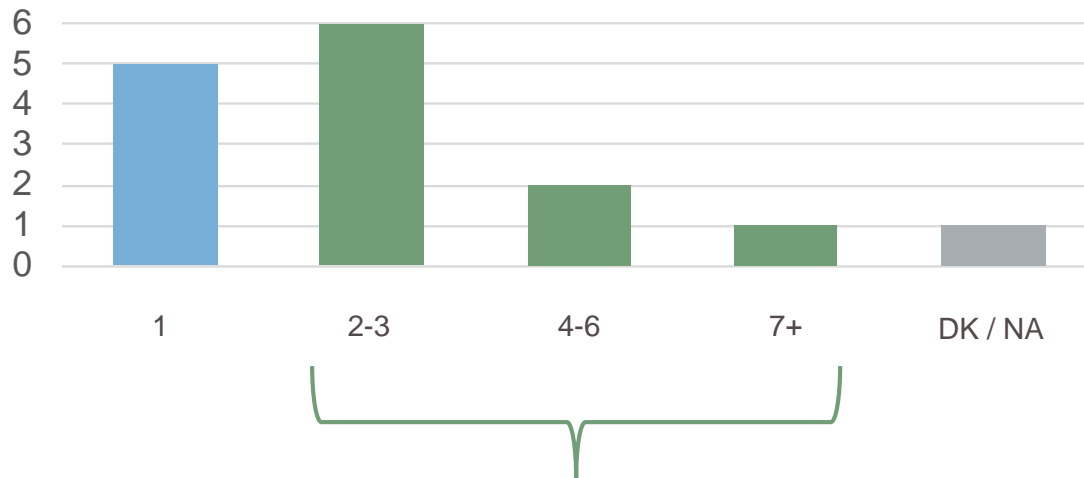
How significant is the impact if left unresolved?

	No Impact	Some Impact	Significant Impact	N/A
Financial		1		
Regulatory		1		
Administrative/Other		1		

BOLI VENDORS

BOLI VENDORS

- How many BOLI vendor businesses (brokers, agents, consultants, administrators) do you interact with in managing your BOLI program?

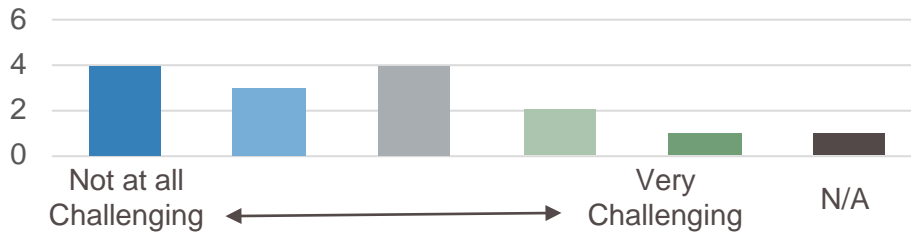


- All 9 responses of 2-7+ vendors subsequently indicated that they consider one or two of the vendors to be the primary administrative service provider(s) for their program

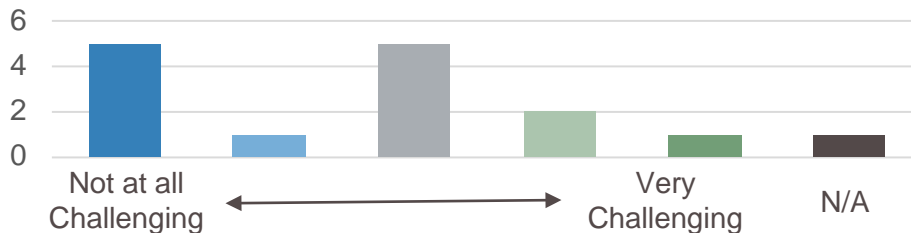
BOLI VENDOR OVERSIGHT

- With regard to BOLI vendor management oversight, how challenging is it to comply with the following aspects of OCC 2013-29?

- Ability to assess and understand the direct and indirect costs involved in the third-party relationship (i.e., have you obtained representations of full compensation transparency?)



- Effecting written contracts with all BOLI vendors that outline the rights and responsibilities of each party

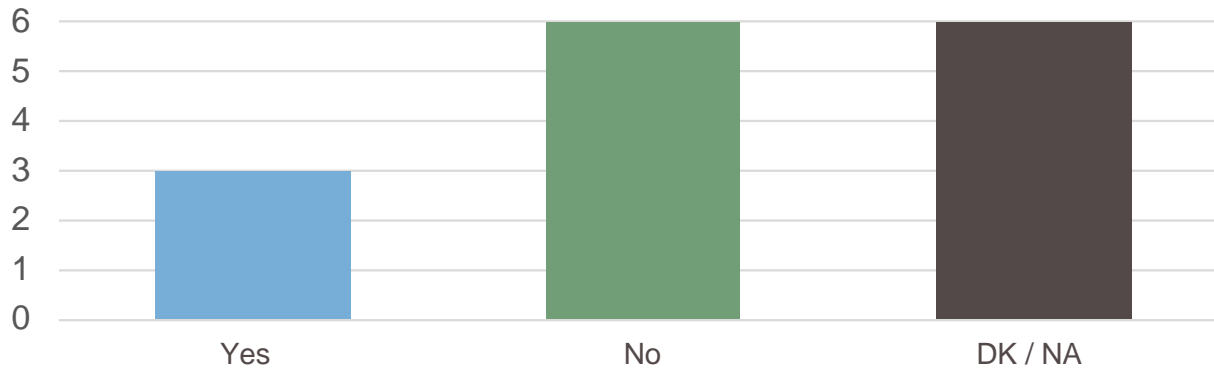


- Ongoing monitoring of the vendor's activities and performance



BOLI VENDOR COMPENSATION

- If you were to change BOLI vendors, do you know whether and to what extent compensation being paid to the previous vendor by the carrier can be eliminated or redirected?



REGULATORY / COMPLIANCE FACTORS

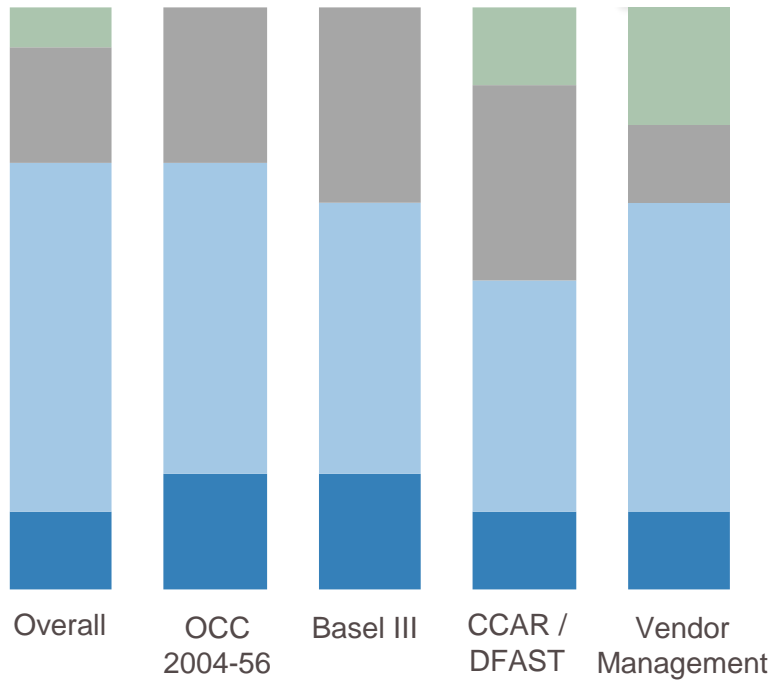
REGULATORY COMPLIANCE BURDEN

How concerned are you about BOLI bank regulatory compliance BURDEN?

- Overall
- OCC 2004-56
- Application of Basel III
- CCAR/DFAST
- Third Party Vendor Management

Very Concerned

Not at all Concerned



1/15 Expressed elevated concern for overall compliance burden

Length of concern

More than 5 years	
2-5 Years	1
1-2 Years	
Recently arose	
Don't know / N/A	

Taken action to address it?

No	
No, but actively deliberating	
Yes, internally	1
Yes, external assistance	
Don't know / N/A	

Did those actions work?

Fully resolved	
Improved, but still a concern	1
No improvement	
Too early to tell	
Don't know / N/A	

How significant is the impact if left unresolved?

	No Impact	Some Impact	Significant Impact	N/A
Financial		1		
Regulatory		1		
Administrative/Other		1		

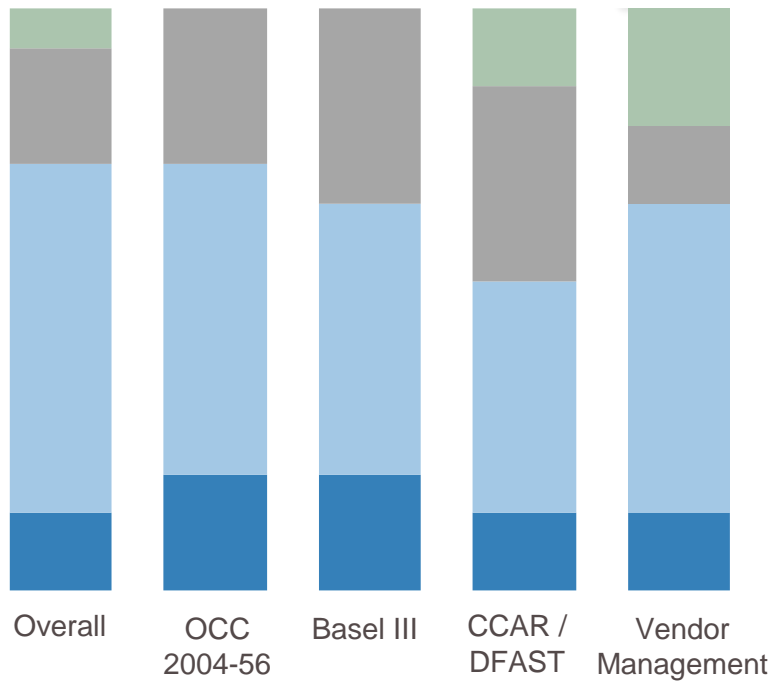
REGULATORY COMPLIANCE BURDEN

■ (Continued) How concerned are you about BOLI bank regulatory compliance BURDEN?

- Overall
- OCC 2004-56
- Application of Basel III
- CCAR/DFAST
- Third Party Vendor Management

Very Concerned

Not at all Concerned



2/15 Expressed elevated concern for CCAR/DFAST compliance burden

Length of concern

More than 5 years	
2-5 Years	1
1-2 Years	
Recently arose	1
Don't know / N/A	

Taken action to address it?

No	
No, but actively deliberating	
Yes, internally	2
Yes, external assistance	
Don't know / N/A	

Did those actions work?

Fully resolved	
Improved, but still a concern	1
No improvement	
Too early to tell	1
Don't know / N/A	

How significant is the impact if left unresolved?

	No Impact	Some Impact	Significant Impact	N/A
Financial	1		1	
Regulatory		2		
Administrative/Other		2		

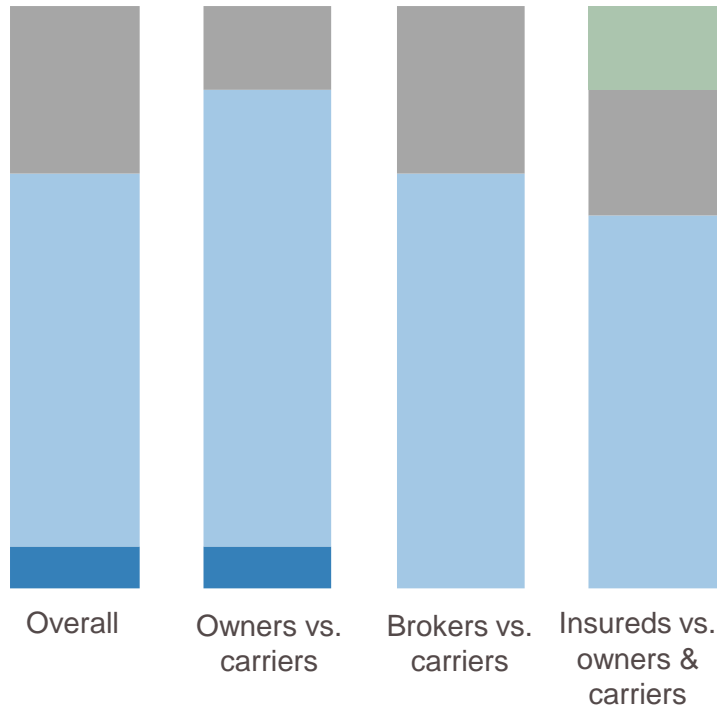
BOLI LITIGATION

How concerned are you about BOLI related litigation?

- Overall
- BOLI owners engaging in litigation against insurance carriers
- BOLI administrators/brokers engaging in litigation against insurance carriers
- Insureds engaging in litigation against owners and/or carriers

Very Concerned

Not at all Concerned



2/15 Expressed elevated concern for insureds vs. owner and carrier litigation

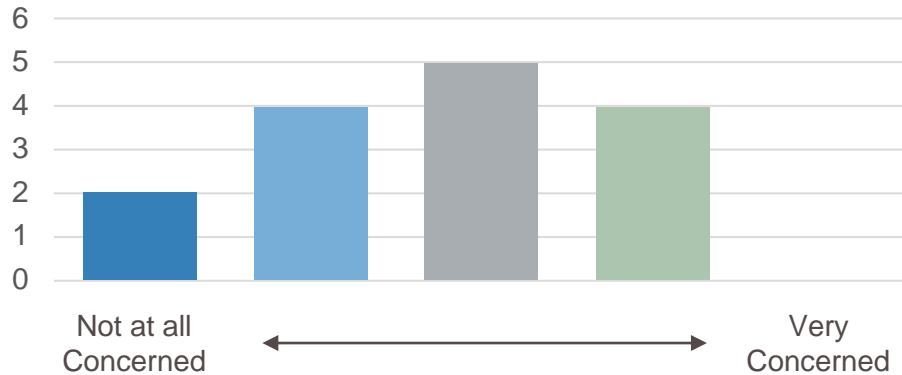
Length of concern	
More than 5 years	1
2-5 Years	
1-2 Years	1
Recently arose	
Don't know / N/A	

Taken action to address it?		Did those actions work?	
No	1	Fully resolved	
No, but actively deliberating	1	Improved, but still a concern	
Yes, internally		No improvement	
Yes, external assistance		Too early to tell	
Don't know / N/A		Don't know / N/A	

	How significant is the impact if left unresolved?			
	No Impact	Some Impact	Significant Impact	N/A
Financial	1	1		
Regulatory	1	1		
Administrative/Other		1	1	

HEADLINE RISK

- How concerned are you about headline/reputation risk stemming from public misconceptions about profiting from deaths?



4/15 Expressed elevated concern for SA flexibility

Length of concern	
More than 5 years	3
2-5 Years	
1-2 Years	1
Recently arose	
Don't know / N/A	

Taken action to address it?		Did those actions work?	
No	2	Fully resolved	
No, but actively deliberating		Improved, but still a concern	2
Yes, internally	2	No improvement	
Yes, external assistance		Too early to tell	
Don't know / N/A		Don't know / N/A	

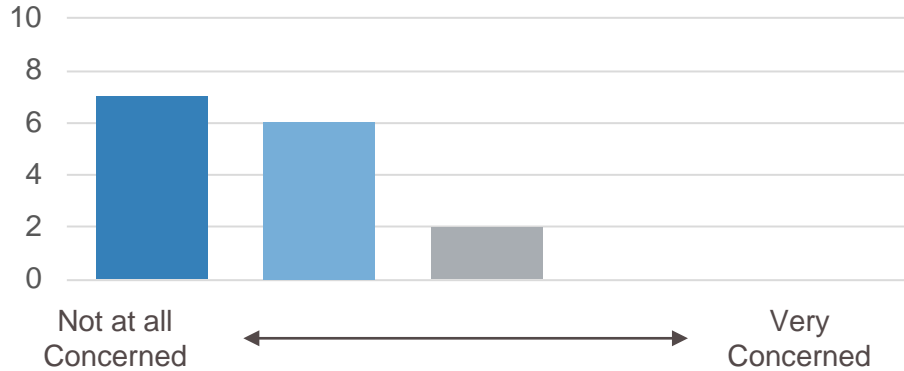
	How significant is the impact if left unresolved?			N/A
	No Impact	Some Impact	Significant Impact	
Financial	2	2		
Regulatory	2	2		
Administrative/Other	1	2	1	

BASEL III

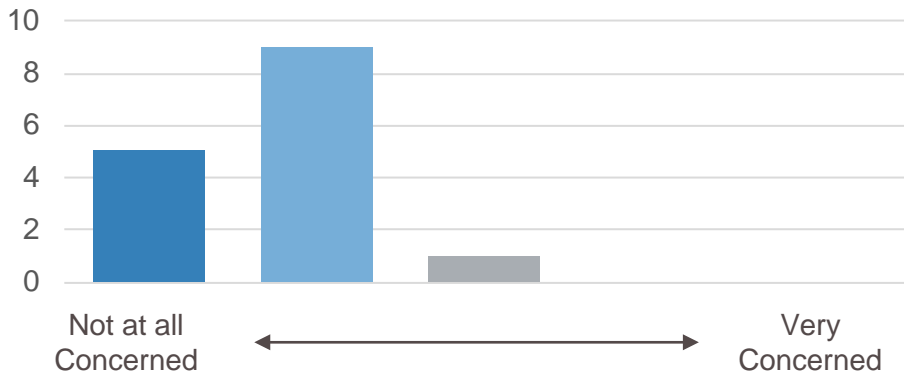
APPLICATION OF BASEL III

■ How concerned are you that your institution is NOT applying Basel III rules correctly?

■ Risk weighting the BOLI program

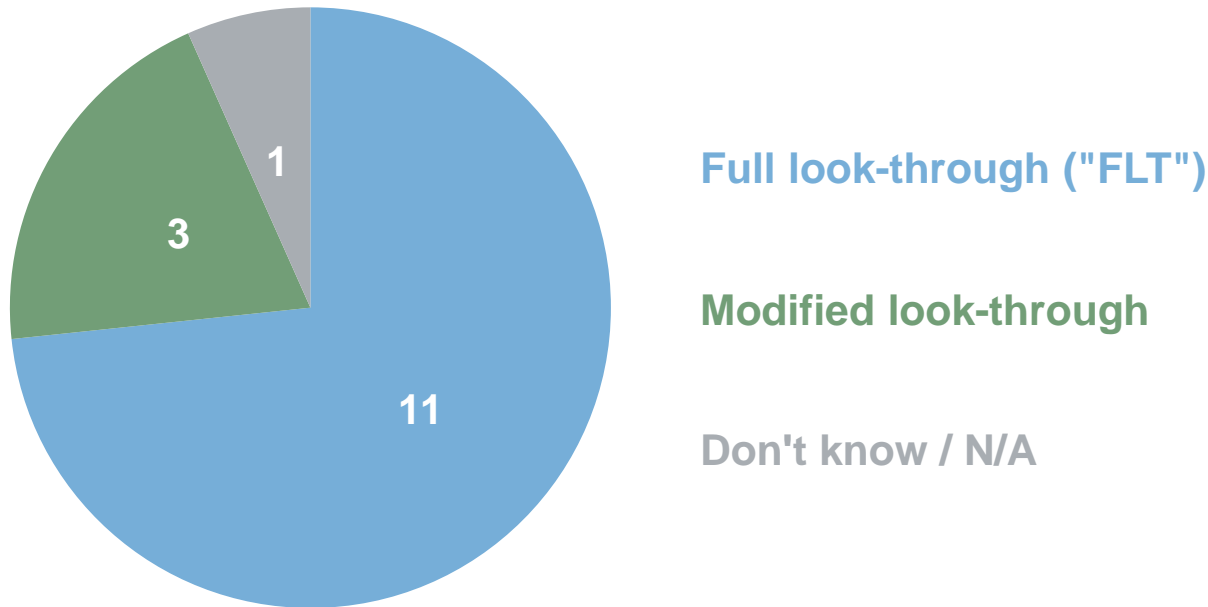


■ Reporting the values correctly on the Call Reports



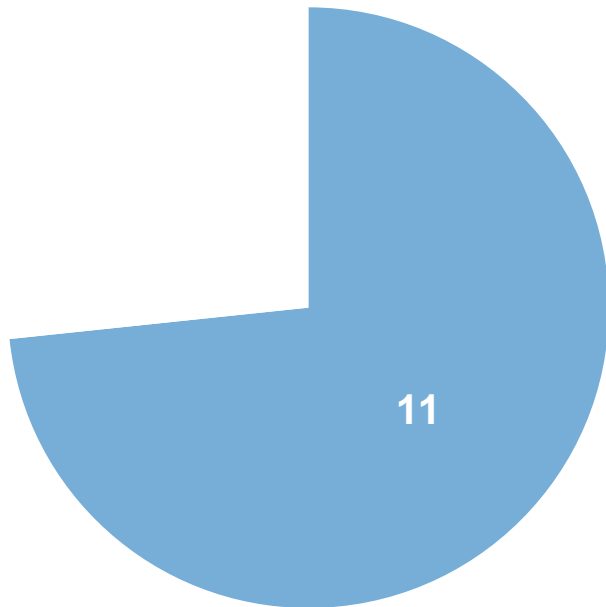
BASEL III APPROACH

- Does your institution use a full look-through (“FLT”) approach or one of the modified look-through approaches?



FULL LOOK THROUGH

- Does your institution use a full look-through (“FLT”) approach or one of the modified look-through approaches?



If Full look-through ("FLT")

How frequently does your institution perform Basel III FLT computations?

Monthly	5
Quarterly	5
Annually	
Don't know / NA	
Other*	1
* "quarterly migrating to monthly"	

What "as of" date is used for portfolio holdings and carrying values?

Carrying Value Date	5
1-Month Lag	2
2-Month Lag	1
3-Month Lag	
Don't know / NA	2
Other*	1
* "multiple holdings periods"	

What is the effective overall risk weight of your separate account investment allocations?

Less than 20% (before floor)	3
20%-30%	2
31%-50%	5
51%-100%	
Don't know / NA	1

MODIFIED LOOK-THROUGH

- Does your institution use a full look-through (“FLT”) approach or one of the modified look-through approaches?

If Modified look-through

What is the effective overall risk weight of your separate account investment allocations?

Less than 20% (before floor)

20%-30%

31%-50%

51%-100%

Don't know / NA

3

Would you employ a full-look-through (“FLT”) if it resulted in a material reduction in RWA?

Yes

No

Don't know / N/A

2

1

What are the primary reasons your institution would not apply the FLT for BOLI? (Chose all that apply)

Data availability

X

Data timing

X

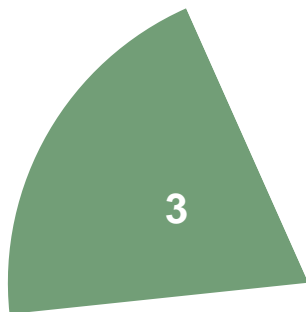
Data reliability

X

Complexity/work (i.e., disproportionate to benefit from RWA difference)

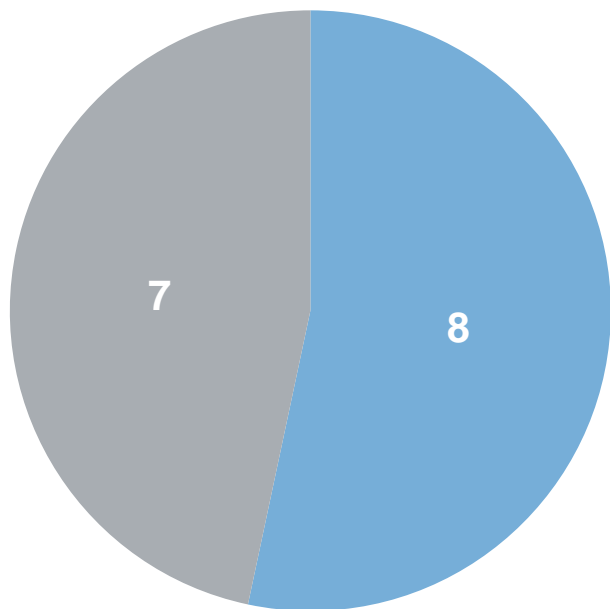
XX

Other



HYBRID TREATMENT

- How does your firm treat Hybrid BOLI exposures?



GA 100% Risk-Weight

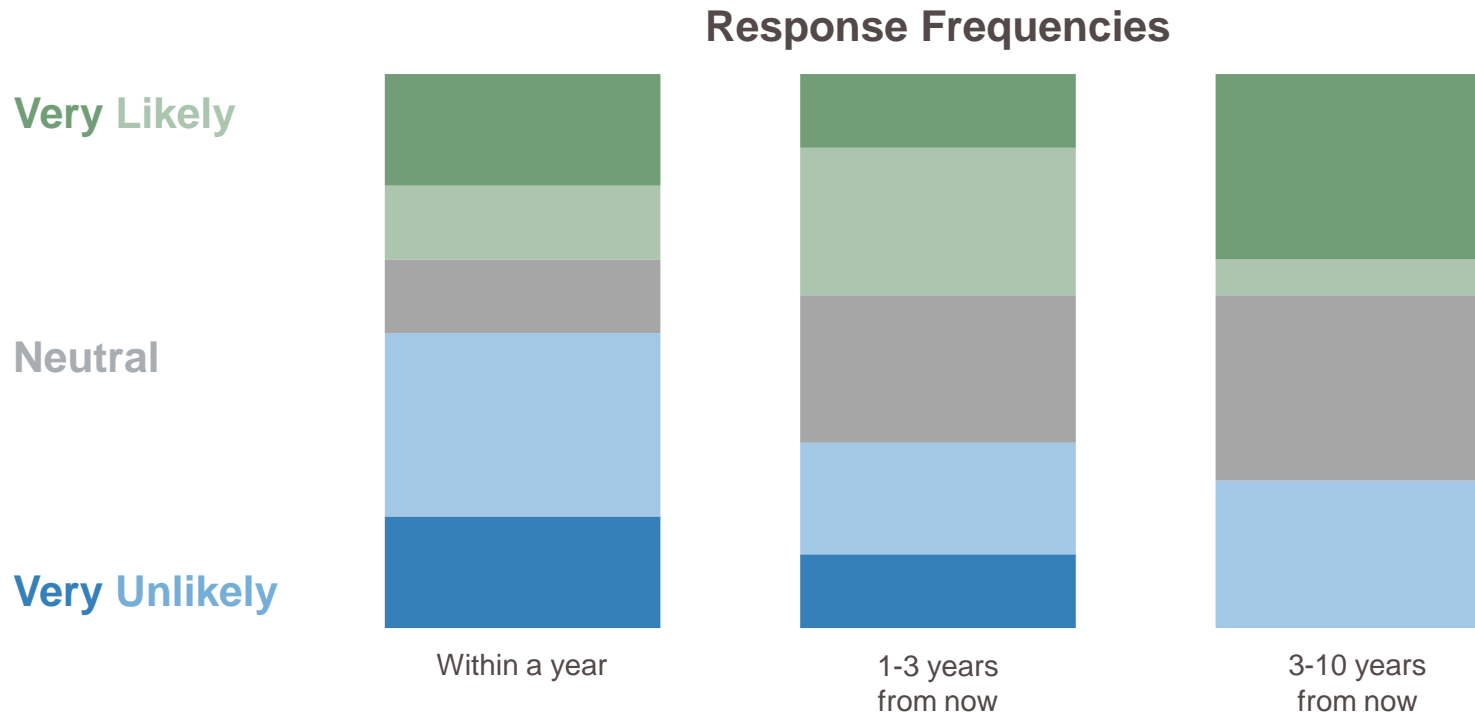
SA Investment Fund Exposure

Don't know / N/A

SEPARATE ACCOUNT ALLOCATION

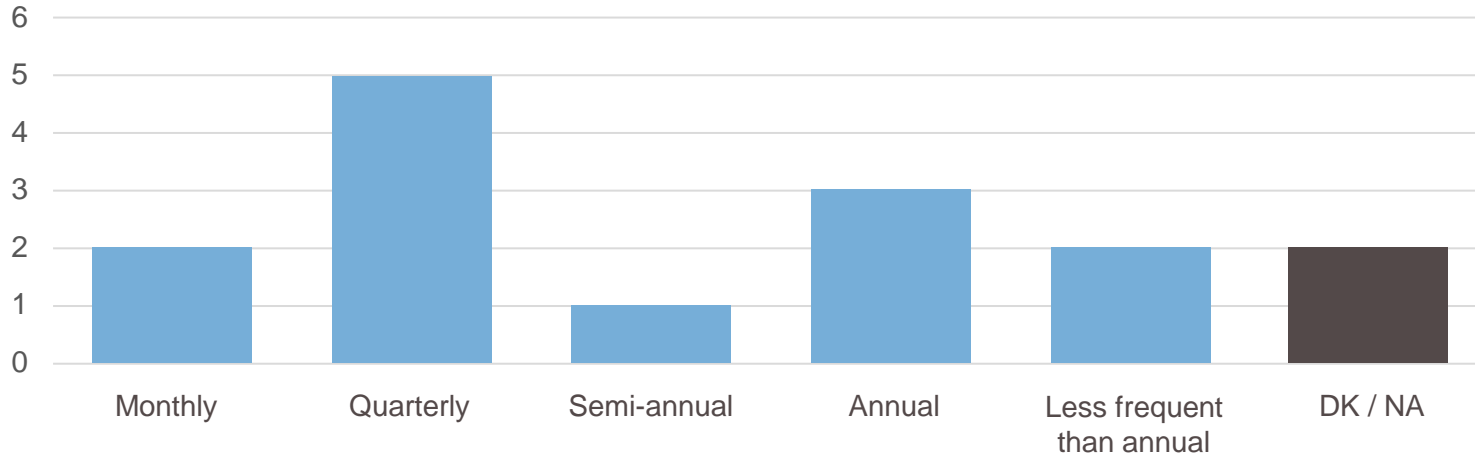
ALLOCATION CHANGES

- How likely is your firm to modify your current SA investment allocations (excluding 401(k) mirror plan related allocations)?



ALLOCATION EVALUATION

- How frequently does your firm evaluate its SA BOLI investment allocations in the context of considering changes/reallocations?



ALLOCATION CONSIDERATIONS

- Please select the **THREE** most significant considerations that impact your SA BOLI investment allocation decisions.

Consideration	Selected	Ranked 1 st (3pts)	Ranked 2 nd (2 pts)	Ranked 3 rd (1pt)	Point total
Investment guidelines or risk parameters	9	5		3	18
Investment manager's track record relative to benchmark	8	2	5	1	17
SVP Provider considerations (i.e., will SVP provider allow the allocation?)	7	4	1	2	16
Investment manager's track record relative to peers	7	1	4	2	13
Highest expected return on capital	4	3		1	10
Investment management fees	4		2	2	6
Highest expected risk-adjusted return	3		1	2	4
Lowest possible risk weight	1		1		2
Preference for passive management	1			1	1

SVP APPROVAL

- Does your SVP agreement require the approval of the SVP provider to change investment allocations?

No; our contracts generally specify a list of available investment divisions that are permissible. 5

No; our contracts specify at least one investment division that is available for reallocation without requiring the SVP provider's approval.

Yes; our contracts require the SVP provider(s) to agree to any changes in the investment allocation. 4

Combination; some of our contracts allow us to reallocate without the SVP provider's prior approval while others require SVP provider approval. 2

N/A; we do not utilize SVP agreements. 1

Don't know; I am not certain how my SVP agreements function regarding investment reallocations. 3

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