

THE DEFINITIVE BOOK ON PREMIUM FINANCING

THE GOOD, BAD, UGLY & INSANE PRACTICES USED IN A CONTROVERSIAL INDUSTRY

DARREN SUGIYAMA & JEFF FAINE

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This book and the contents within are not be used as a sales aid to convince a client to purchase a premium financed life insurance policy, or to suggest that any other financial investment should be replaced with a life insurance policy. Every decision regarding such topics should be discussed with a licensed insurance professional that you trust.

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DARREN SUGIYAMA & JEFF FAINE

Chapter 1 The Power of Leverage

Nearly every financial empire was built using *leverage*. Real estate empires have been built using *leverage* in the form of *mortgage loans*. Business empires have used *leverage* in the form of *business loans* to invest in the expansion of their empires. In addition, most people have used *leverage* to finance their college education in the form of *student loans*.

Generally speaking, most financially successful people have utilized leverage in some capacity to build and grow their wealth. Leveraged Index ArbitrageTM is a strategy that utilizes a similar type of leverage to compound a person's wealth – a proprietary method of premium financing.

Premium financing is a method of accumulating wealth within a life insurance chassis using a lender's capital to fund the life insurance premiums.

The client pays the lender interest-only payments for an extended period of time, with the intention of exiting the loan (usually somewhere between years 15-20) using the policy's accumulated cash value to pay off the third party lender.

While typically used as a way to purchase a large death benefit in the most cash flow efficient way, premium financing can also be used as a way to build a tax-advantaged asset class correlated with the S&P 500, but also protected from market volatility.

By using the lender's capital to heavily frontload the premiums into the life insurance policy, the cash value accumulation reaps the benefits of compound interest based on the index's return.

The goal in a premium financing arrangement is to create a *Positive Arbitrage* scenario wherein the life insurance policy's annual *cash value gain* is greater than the annual *interest charged* on the premium financing loan.

There are two unique elements of premium financing that make this is a reasonable expectation:

- 1. If the policy is an *Indexed Universal Life (IUL)* insurance policy with a 0.00% protective floor, this crediting method insulates the policy from receiving negative index returns.
- 2. The life insurance policy cash value grows based on *compound interest*, whereas the premium financing loan is being charged *simple interest*.

Positive Interest Arbitrage

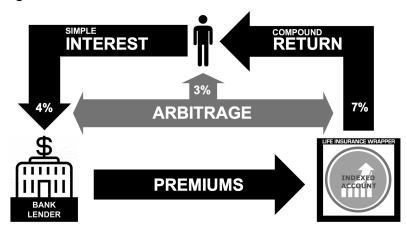
If the client borrows the premiums from a lender at an interest rate of 4.00%, and the policy cash value receives a 7.00% net credit, there would be a *Positive Interest Arbitrage* of 3.00%.

7.00% net cash value crediting rate

-4.00% borrowing interest rate

3.00% positive interest arbitrage

Below is a diagram that explains this *Positive Interest Arbitrage* concept that can exist in a premium financing arrangement.



But in addition to the *Positive Interest Arbitrage*, another key component to understand is the difference between *Simple Interest* and *Compound Interest*.

Simple Interest vs. Compound Interest

For example, if the client borrowed a total of \$2,000,000 at a borrowing interest rate of 4.00%, the client's annual interest-only payment would be \$80,000.

\$2,000,000 loan <u>x 4.00% borrowing rate</u> **\$80,000 interest payment**

However, if the borrowing interest rate increased from 4.00% to 7.00%, the client's annual interest payment would increase from \$80,000 to \$140,000. The interest payment would be limited to the borrowing rate multiplied by the non-growing principal loan balance of \$2,000,000.

\$2,000,000 loan <u>x 7.00% borrowing rate</u> **\$140,000 interest payment**

If the policy cash value only received a 4.00% net compounded annual credit (after policy charges), over a 20-year period, the cash value would grow to \$4,382,246. Assuming another paltry 4.00% net credit in the next policy year (year 21), a \$175,290 cash value gain would be credited to the policy.

\$4,382,246 policy cash value x 4.00% net cash value credit \$175,290 policy interest credit

In this isolated one-year scenario, even with *Negative Interest Arbitrage* (the 4.00% net cash value crediting rate is less than the 7.00% borrowing interest rate), the client would still experience *Positive Dollar Arbitrage* (the \$175,290 policy interest credit is greater than the \$140,000 interest payment in that year) resulting in a \$35,290 *Positive Dollar Arbitrage* (a net gain).

4.00% net cash value crediting rate
-7.00% borrowing interest rate
-3.00% negative interest arbitrage

\$175,290 policy interest credit
-\$140,000 interest payment
\$35,290 positive dollar arbitrage

Thus far, we have merely discussed arbitrage *theory* and *Positive Dollar Arbitrage* occurring within a *Negative Interest Arbitrage* environment. In *theory*, the 0.00% protective floor of the IUL along with the potential *Positive Dollar Arbitrage* created

by the *simple interest* being offset by *compound interest*, the concept of premium financing *should* work.

But what *should* happen is irrelevant.

High net worth clients want reassurance that the strategy being used to employ their 7-to-9 figure allocation is backed by empirical evidence.

They want indisputable mathematical proof.

The problem is that instead of being shown the required indisputable mathematical proof, they are often times shown premium financing scenarios wherein the borrowing rate is always lower than the static IRR in the policy.

There are no static returns in reality.

Market volatility and a poor sequence of returns can result in several 0.00% policy index credits during the early years, which can be extremely detrimental to a premium financing arrangement.

This is not my *opinion*. It is an *indisputable fact*.

There are no opinions allowed in math.

Math is either correct or it is incorrect.

At my firm, we pride ourselves in having proprietary software that has the capability of showing our clients the indisputable mathematical truth regarding premium financing.

But it's not *just* our software.

We have an innate desire to *expose* the truth, transparently articulating every risk involved in premium financing – risks that most premium financing *so-called experts* rarely ever discuss.

In this book, we will discuss the concept of premium financing at a conceptual level, and at a granular level.

We will discuss economic *theory*, but we will also calculate the indisputable math with full transparency, and show you how our program mitigates (and in some cases, completely eliminates) these risks.

Chapter 2

The Genesis of Lionsmark Capital

My business partner Jeff Faine had a very successful 10-year NFL career. A graduate of Notre Dame, Jeff was the first-round draft pick of the Cleveland Browns. He went on to play for the New Orleans Saints, the Cincinnati Bengals, and the Tampa Bay Buccaneers.

Jeff was the highest paid center in the NFL at one point, but what makes Jeff incredibly unique is that he entered entrepreneurship quite early. He began investing in restaurants and real estate, and by his fifth year in the NFL, he was living off of his business income and reinvesting his NFL income. He built his restaurant empire up to 29 restaurant units and employed over 400 employees.

Jeff even convinced the team's trainer to let him set up a makeshift office in the training room to run his business from, equipped with a computer, printer and fax machine.

As you can see, Jeff was not your typical ballplayer.

With all of his restaurant and real estate endeavors, he realized it only made sense to start a property and casualty insurance agency to write the insurance on all of his restaurants and real estate properties, which is how he entered the insurance business. Jeff's introduction to premium financing also happened during his NFL career, but as a premium financing *client*.

He bought a premium financed indexed universal life insurance policy on himself in 2009 and hit the cap five out of the first six years. Talk about great timing.

When Jeff retired from his NFL career, he joined forces with the agent that sold him his premium financed life insurance policy which is how he learned the premium financing business.

This was a great learning experience because he understood premium financing from a client's perspective, and now he was learning it from an advisor's perspective.

But one day the agent came to Jeff and told him that he was on the *back nine* of his career and wanted to take 6-month sabbaticals in Argentina and drink Malbec.

Jeff on the other hand was driven to build yet another empire in the premium financing business, and realized he needed a business partner on the *front nine* of his career instead of the *back nine*

That person was me.

When Jeff and I first met, he was attending a seminar I was hosting in Newport Beach, California. He had read one of my books – *How I Built A \$37 Million Insurance Agency In Less Than 7 Years* – wherein I explain how entered the insurance business in 2003, working out of hotel lobbies and coffee shops (because I couldn't afford a real office).

By 2008, I had built an employee benefits firm that was the #1 producing firm in the country for *Kaiser Permanente*, #1 in the country for *Health Net*, #2 in the state of California for *Aetna*, and the list goes on and on.

By 2012, my firm was responsible for over 58% of the new business written for *Colonial Life* in both Orange County and San Bernardino County combined, and in 2017, we produced over 25% of the life insurance policy sales for *Pacific Life* in Orange County, California. In 2018, my firm helped pioneer *Penn Mutual*'s new technology-based *ACE* program, selling more life insurance policies through their new platform than any other firm in the country.

In addition to building several insurance agencies, I am also an internationally acclaimed author, having published five books (this book is my sixth), several of which are in circulation worldwide in Australia, Brazil, Canada, Croatia, Czechoslovakia, Denmark, India, Italy, Japan, the Netherlands, New Zealand, Singapore, Sweden, the United Kingdom and obviously, The United States.

About a year after we met, Jeff and I started talking more seriously about doing business together in the premium financing

arena. He had negotiated a lending arrangement with a bank that agreed to a very unique set of lending parameters:

- ✓ No outside collateral.
- ✓ No personal guaranty requirements.
- ✓ Sole recourse limited to the policy asset.

Jeff is one of the most humble guys you will ever meet.

He essentially used his NFL celebrity status and business banking relationships to secure premium financing lending terms that are unheard of.

Jeff would never tell you just how much power and influence he has in some circles, nor would he tell you how successful he has been in multiple business ventures.

But with his connections and acute business acumen, along with my track record in the insurance industry, we have created the foundation of a budding empire that is currently disrupting the premium financing industry in a way that is revolutionary.

And the best part is, this unique combination of our attributes benefits everyone involved, including financial advisors, insurance agents, insurance carriers, and most importantly, our clients

Fast forward to today, Jeff and I have built a platform that consists of five publicly traded banks, one privately-held bank and eleven life insurance carriers.

We are exposing everything *wrong* with the industry, including the mathematically unsound construction of several popular gimmicky strategies.

Our platform is built on three pillars:

- ✓ Conservatism.
- ✓ Transparency.
- ✓ Indisputable Math.

Our proprietary software not only stress-tests our own premium financing program, but it also stress-tests every other

premium financing program in the market, transparently showing the client the risk exposure involved in these other programs.

It can backtest historical index returns, showing each of these risks, individually and compounded concurrently:

- ✓ Market Volatility.
- ✓ Poor Sequence of Market Returns.
- ✓ Hyper-Inflated Borrowing Interest Rates.

When vetted properly, the client should understand every single one of these risk factors, because if the premium financing program is built properly, it will withstand this *doomsday* stresstested scenario.

In this book, we will model these adverse scenarios and articulate what makes a properly designed premium financing program withstand these types of adversities.

Chapter 3

Risk #1: Collateral Calls

Most people would agree that everything in life comes with *some* risk. Premium financing is no different.

When an advisor designs a policy illustration/proposal, they manually input a hypothetical gross index rate of return the policy *might* receive, say 6% or 7% for example.

This is merely speculation based on historical averages.

The National Association of Insurance Commissioners (NAIC) has established a maximum rate of return a life insurance company may use in calculating expected cash values when illustrating Indexed Universal Life (IUL) insurance policies.

Known as AG49 (Actuarial Guideline 49), each carrier is limited to the average of each 25-year rolling period of the S&P 500 for the last 65 years, based on each of the carrier's crediting methods.

This maximum allowable rate is typically what agents use when illustrating *IUL* insurance policies, however showing a static rate (a rate that does not fluctuate whatsoever over a 20, 30 or 40-year period) with no volatility is not realistic.

If an agent shows a policy illustrated using a static 5.76% annual index credit *every year*, there's one thing we know. The S&P 500 will never produce a 5.76% return every single year, year after year. There will always be *some* volatility.

Though the policy index credit may *average* 5.76% over a 40-year period for example, there will be some years where the index will credit 0.00%, and some years where it will credit significantly more than 5.76%. This is incredibly important to understand in a premium financing arrangement.

For simplicity purposes, in order to articulate the basic concept of premium financing, we will begin by showing this type of 5.76% static return scenario, but we will definitely address volatility and a poor sequence of returns later in this chapter.

As a case study, we will take a look at a 55-year old male client in need of \$10,000,000 in net death benefit. The client is borrowing \$588,546 per year for seven years, and making annual interest-only payments each year for the first 15 years.

| 1 55 \$588,546 \$588,546 4.50% \$26,485 2 56 \$588,546 \$1,177,092 4.50% \$52,969 3 57 \$588,546 \$1,765,638 4.50% \$79,454 4 58 \$588,546 \$2,354,184 4.50% \$105,938 5 59 \$588,546 \$2,942,730 4.50% \$132,423 6 60 \$588,546 \$3,531,276 4.50% \$158,907 | # | 405 | PREMIUMS | CUMULATIVE PF | BORROWING | INTEREST |
|--|------|-----|-----------|---------------|-----------|-----------|
| 2 56 \$588,546 \$1,177,092 4.50% \$52,969 3 57 \$588,546 \$1,765,638 4.50% \$79,454 4 58 \$588,546 \$2,354,184 4.50% \$105,938 5 59 \$588,546 \$2,942,730 4.50% \$132,423 6 60 \$588,546 \$3,531,276 4.50% \$158,907 | YEAR | AGE | BORROWED | LOAN BALANCE | RATE | PAYMENTS |
| 3 57 \$588,546 \$1,765,638 4.50% \$79,454 4 58 \$588,546 \$2,354,184 4.50% \$105,938 5 59 \$588,546 \$2,942,730 4.50% \$132,423 6 60 \$588,546 \$3,531,276 4.50% \$158,907 | | | | • | | |
| 4 58 \$588,546 \$2,354,184 4.50% \$105,938 5 59 \$588,546 \$2,942,730 4.50% \$132,423 6 60 \$588,546 \$3,531,276 4.50% \$158,907 | | | | | | |
| 5 59 \$588,546 \$2,942,730 4.50% \$132,423 6 60 \$588,546 \$3,531,276 4.50% \$158,907 | | | | | | |
| 6 60 \$588,546 \$3,531,276 4.50% \$158,907 | | | . , | . , , | | • |
| | | | | | | |
| 7 61 \$588 546 \$4 119 822 4 50% \$185 392 | | | | | | |
| · · · · · · · · · · · · · · · · · · · | | 61 | \$588,546 | \$4,119,822 | 4.50% | \$185,392 |
| 8 62 \$0 \$4,119,822 4.50% \$185,392 | | | • | | | . , |
| 9 63 \$0 \$4,119,822 4.50% \$185,392 | | | | | | |
| 10 64 \$0 \$4,119,822 4.50% \$185,392 | | | · | | | |
| 11 65 \$0 \$4,119,822 4.50% \$185,392 | 11 | 65 | | | 4.50% | \$185,392 |
| 12 66 \$0 \$4,119,822 4.50% \$185,392 | 12 | 66 | · | | 4.50% | \$185,392 |
| 13 67 \$0 \$4,119,822 4.50% \$185,392 | 13 | 67 | \$0 | | 4.50% | \$185,392 |
| 14 68 \$0 \$4,119,822 4.50% \$185,392 | 14 | 68 | \$0 | \$4,119,822 | 4.50% | \$185,392 |
| 15 69 \$0 \$4,119,822 4.50% \$185,392 | 15 | 69 | \$0 | \$4,119,822 | 4.50% | \$185,392 |
| 16 70 \$0 \$0 4.50% \$0 | 16 | 70 | \$0 | \$0 | 4.50% | \$0 |
| 17 71 \$0 \$0 4.50% \$0 | 17 | 71 | \$0 | \$0 | 4.50% | \$0 |
| 18 72 \$0 \$0 4.50% \$0 | 18 | 72 | \$0 | \$0 | 4.50% | \$0 |
| 19 73 \$0 \$0 4.50% \$0 | 19 | 73 | \$0 | \$0 | 4.50% | \$0 |
| 20 74 \$0 \$0 4.50% \$0 | 20 | 74 | \$0 | \$0 | 4.50% | \$0 |
| 21 75 \$0 \$0 4.50% \$0 | 21 | 75 | \$0 | \$0 | 4.50% | \$0 |
| 22 76 \$0 \$0 4.50% \$0 | 22 | 76 | \$0 | \$0 | 4.50% | \$0 |
| 23 77 \$0 \$0 4.50% \$0 | 23 | 77 | \$0 | \$0 | 4.50% | \$0 |
| 24 78 \$0 \$0 4.50% \$0 | 24 | 78 | \$0 | \$0 | 4.50% | \$0 |
| 25 79 \$0 \$0 4.50% \$0 | 25 | 79 | \$0 | \$0 | 4.50% | \$0 |
| 26 80 \$0 \$0 4.50% \$0 | 26 | 80 | \$0 | \$0 | 4.50% | \$0 |
| 27 81 \$0 \$0 4.50% \$0 | 27 | 81 | \$0 | \$0 | 4.50% | \$0 |
| 28 82 \$0 \$0 4.50% \$0 | 28 | 82 | \$0 | \$0 | 4.50% | \$0 |
| 29 83 \$0 \$0 4.50% \$0 | 29 | 83 | \$0 | \$0 | 4.50% | \$0 |
| 30 84 \$0 \$0 4.50% \$0 | 30 | 84 | \$0 | \$0 | 4.50% | \$0 |
| 31 85 \$0 \$0 4.50% \$0 | 31 | 85 | \$0 | \$0 | 4.50% | \$0 |
| 32 86 \$0 \$0 4.50% \$0 | 32 | 86 | \$0 | \$0 | 4.50% | \$0 |
| 33 87 \$0 \$0 4.50% \$0 | 33 | 87 | \$0 | \$0 | 4.50% | \$0 |
| 34 88 \$0 \$0 4.50% \$0 | 34 | 88 | \$0 | \$0 | 4.50% | \$0 |
| 35 89 \$0 \$0 4.50% \$0 | 35 | | | | 4.50% | |
| 36 90 \$0 \$0 4.50% \$0 | | | · | | | |
| 37 91 \$0 \$0 4.50% \$0 | | | | | | |
| 38 92 \$0 \$0 4.50% \$0 | | | · | • | | • |
| 39 93 \$0 \$0 4.50% \$0 | | | | | | |
| 40 94 \$0 \$0 4.50% \$0 | | | | | | |

The borrowing interest rate shown is a static 4.50%.

The illustration is showing a static policy index credit of 5.76% (shown on the next page), which we know will never happen, and we also know that the static borrowing rate will never happen in reality either.

Later in this book, we will stress-test the model by showing volatility in both the borrowing rate and policy performance, but for the sake of articulating the general concept of premium financing, we will keep them static for now.

In a premium financing arrangement, the policy often serves as *part* of the collateral needed to secure the loan, but there will be a shortfall in collateral based on the loan-to-value ratio between the cumulative funds borrowed and the *Cash Surrender Value*

In the example shown on the next page, the *Gross Policy Cash Surrender Value* is less than the *Cumulative Loan Balance* in each of the first six years, resulting in the *Policy Cash Surrender Value Net Of Loans* having a negative value. Hence, the client will be required to post collateral in addition to the policy asset.

Notice the collateral requirement increases in year two and again in year three, even with a static positive policy index credit of 5.76%.

Posting additional collateral outside of the policy is not necessarily a bad thing, however often times the client will have *collateral amnesia* and will have forgotten about the initial discussion that additional collateral requirements were expected in those subsequent years.

Remember, this discussion would have happened over a year ago in most cases.

This explains why the issue of collateral can be so problematic. The client will need to submit an entire new set of financial statements, brokerage account updates, cash balance reports and several other documents to justify their credit worthiness. The client must requalify for the premium financing loan each year, which can be quite cumbersome.

| .,, | | INDEX | CDOO | POLICY COV | COLLATERA | DEATH BENEFIT |
|-----------|-----|-----------------|---------------------|----------------------------|------------------------|-------------------------------|
| # YEAR | AGE | INDEX CREDIT | GROSS POLICY CSV | POLICY CSV NET OF LOANS | COLLATERAL REQUIRED | DEATH BENEFIT NET OF LOANS |
| 1 | 55 | 5.76% | \$232,738 | -\$355,808 | \$391,389 | \$9,855,933 |
| 2 | 56 | 5.76% | \$836,648 | -\$340,444 | \$374,488 | \$9,765,398 |
| 3 | 57 | 5.76% | \$1,399,170 | -\$366,468 | \$403,115 | \$9,728,792 |
| 4 | 58 | 5.76% | \$2,016,912 | -\$337,272 | \$370,999 | \$9,747,413 |
| 5 | 59 | 5.76% | \$2,697,728 | -\$245,002 | \$269,502 | \$9,829,101 |
| 6 | 60 | 5.76% | \$3,429,700 | -\$101,576 | \$111,734 | \$9,961,952 |
| 7 | 61 | 5.76% | \$4,215,712 | \$95,890 | \$0 | \$10,148,843 |
| 8 | 62 | 5.76% | \$4,465,742 | \$345,920 | \$0 | \$10,148,843 |
| 9 | 63 | 5.76% | \$4,745,191 | \$625,369 | \$0 | \$10,148,843 |
| 10 | 64 | 5.76% | \$5,037,449 | \$917,627 | \$0 | \$10,148,843 |
| 11 | 65 | 5.76% | \$5,368,515 | \$1,248,693 | \$0 | \$10,148,843 |
| 12 | 66 | 5.76% | \$5,730,864 | \$1,611,042 | \$0 | \$10,148,843 |
| 13 | 67 | 5.76% | \$6,126,406 | \$2,006,584 | \$0 | \$10,148,843 |
| 14 | 68 | 5.76% | \$6,558,482 | \$2,438,660 | \$0 | \$10,148,843 |
| 15 | 69 | 5.76% | \$7,029,724 | \$2,909,902 | \$0 | \$10,148,843 |
| 16 | 70 | 5.76% | \$7,541,787 | \$3,127,180 | \$0 | \$10,148,843 |
| 17 | 71 | 5.76% | \$8,108,082 | \$3,373,674 | \$0 | \$10,148,843 |
| 18 | 72 | 5.76% | \$8,735,324 | \$3,653,174 | \$0 | \$10,148,843 |
| 19 | 73 | 5.76% | \$9,431,137 | \$3,969,930 | \$0 | \$10,148,843 |
| 20 | 74 | 5.76% | \$10,202,787 | \$4,328,775 | \$0 | \$10,148,843 |
| 21 | 75 | 5.76% | \$11,047,912 | \$4,728,500 | \$0 | \$10,148,843 |
| 22 | 76 | 5.76% | \$11,953,006 | \$5,154,479 | \$0 | \$10,148,843 |
| 23 | 77 | 5.76% | \$12,922,573 | \$5,607,232 | \$0 | \$10,148,843 |
| 24 | 78 | 5.76% | \$13,964,051 | \$6,089,196 | \$0 | \$10,148,843 |
| 25 | 79 | 5.76% | \$15,075,102 | \$6,603,315 | \$0 | \$10,148,843 |
| 26 | 80 | 5.76% | \$16,262,888 | \$7,161,068 | \$0 | \$10,148,843 |
| 27 | 81 | 5.76% | \$17,525,068 | \$7,754,985 | \$0 | \$10,148,843 |
| 28 | 82 | 5.76% | \$18,864,540 | \$8,396,030 | \$0 | \$10,148,843 |
| 29 | 83 | 5.76% | \$20,287,169 | \$9,101,309 | \$0 | \$10,148,843 |
| 30 | 84 | 5.76% | \$21,796,429 | \$9,887,888 | \$0 | \$10,382,283 |
| 31 | 85 | 5.76% | \$23,395,773 | \$10,769,004 | \$0 | \$11,307,454 |
| 32 | 86 | 5.76% | \$25,032,317 | \$11,648,473 | \$0 | \$12,230,897 |
| 33 | 87 | 5.76% | \$26,701,608 | \$12,520,572 | \$0 | \$13,146,601 |
| 34 | 88 | 5.76% | \$28,403,660 | \$13,382,925 | \$0 | \$14,052,071 |
| 35 | 89 | 5.76% | \$30,139,782 | \$14,233,082 | \$0 | \$14,944,736 |
| 36 | 90 | 5.76% | \$31,903,077 | \$15,065,707 | \$0 | \$15,818,993 |
| 37 | 91 | 5.76% | \$33,785,300 | \$15,954,491 | \$0 | \$16,592,670 |
| 38 | 92 | 5.76% | \$35,805,600 | \$16,908,475 | \$0 | \$17,415,729 |
| 39 | 93 | 5.76% | \$37,985,048 | \$17,937,610 | \$0 | \$18,296,362 |
| 40 | 94 | 5.76% | \$40,350,290 | \$19,054,478 | \$0 | \$19,245,023 |

There is, however, a much cleaner and mathematically superior way to finance a life insurance policy's premiums.

Our proprietary program, Leveraged Index ArbitrageTM produces an outcome that is of greater benefit to the client and incurs substantially less risk. It also includes some very unique features, including:

- ✓ No Outside Collateral Requirements
- ✓ No Personal Guaranty Requirements
- ✓ No Corporate Guaranty Requirements
- ✓ Sole Recourse Limited to the Policy

The policy asset is the sole collateral in this program.

The reason these benefits exist is based on our unique policy design, our proprietary lending parameters, and the overall construction of our program.

In this arrangement, the client pays the first-year premium payment out-of-pocket. Think of it like making a down payment on a piece of real estate.

As we see in this example on the following page, the client pays the first year premium payment of \$575,000.

Then, the client borrows \$590,804 per year in years 2-7.

Due to the *Gross Policy Cash Surrender Value* being greater than the *Cumulative Loan Balance*, the *Policy Cash Surrender Value Net of Loans* is always in a positive position.

Based on this unique loan-to-value ratio in the *Leveraged Index Arbitrage*TM program, the client is not required to post any outside collateral whatsoever, as long as the *Gross Policy Cash Surrender Value* is greater than the *Cumulative Loan Balance*.

With the policy as the sole collateral (and the loan being more than 100% collateralized by the *Gross Policy Cash Surrender Value*), the client is not required to sign a personal guaranty on the loan.

In addition, if the policy is owned by a corporation, there is no corporate guaranty requirement either, hence the loan is nonrecourse to the borrower with the sole recourse being the policy asset. These elements are unheard of in the premium financing industry.

| # YEAR | AGE | PREMIUMS BORROWED | PREMIUMS BORROWED | CUMULATIVE PF LOAN BALANCE | BORROWING RATE | INTEREST PAYMENTS |
|-----------|-----|----------------------|----------------------|-------------------------------|-------------------|----------------------|
| 1 | 55 | \$575,000 | \$0 | \$0 | 4.50% | \$0 |
| 2 | 56 | \$0 | \$590,804 | \$590,804 | 4.50% | \$26,586 |
| 3 | 57 | \$0 | \$590,804 | \$1,181,608 | 4.50% | \$53,172 |
| 4 | 58 | \$0 | \$590,804 | \$1,772,412 | 4.50% | \$79,759 |
| 5 | 59 | \$0 | \$590,804 | \$2,363,216 | 4.50% | \$106,345 |
| 6 | 60 | \$0 | \$590,804 | \$2,954,020 | 4.50% | \$132,931 |
| 7 | 61 | \$0 | \$590,804 | \$3,544,824 | 4.50% | \$159,517 |
| 8 | 62 | \$0 | \$0 | \$3,544,824 | 4.50% | \$159,517 |
| 9 | 63 | \$0 | \$0 | \$3,544,824 | 4.50% | \$159,517 |
| 10 | 64 | \$0 | \$0 | \$3,544,824 | 4.50% | \$159,517 |
| 11 | 65 | \$0 | \$0 | \$3,544,824 | 4.50% | \$159,517 |
| 12 | 66 | \$0 | \$0 | \$3,544,824 | 4.50% | \$159,517 |
| 13 | 67 | \$0 | \$0 | \$3,544,824 | 4.50% | \$159,517 |
| 14 | 68 | \$0 | \$0 | \$3,544,824 | 4.50% | \$159,517 |
| 15 | 69 | \$0 | \$0 | \$3,544,824 | 4.50% | \$159,517 |
| 16 | 70 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 17 | 71 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 18 | 72 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 19 | 73 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 20 | 74 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 21 | 75 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 22 | 76 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 23 | 77 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 24 | 78 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 25 | 79 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 26 | 80 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 27 | 81 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 28 | 82 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 29 | 83 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 30 | 84 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 31 | 85 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 32 | 86 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 33 | 87 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 34 | 88 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 35 | 89 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 36 | 90 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 37 | 91 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 38 | 92 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 39 | 93 | \$0 | \$0 | \$0 | 4.50% | \$0 |
| 40 | 94 | \$0 | \$0 | \$0 | 4.50% | \$0 |

| INDEX | GROSS | POLICY CSV | COLLATERAL | DEATH BENEFIT |
|--------|--------------|--------------|------------|---------------|
| CREDIT | POLICY CSV | NET OF LOANS | REQUIRED | NET OF LOANS |
| 5.76% | \$219,257 | \$219,257 | \$0 | \$10,430,998 |
| 5.76% | \$824,479 | \$233,675 | \$0 | \$10,339,517 |
| 5.76% | \$1,388,406 | \$206,798 | \$0 | \$10,302,058 |
| 5.76% | \$2,007,654 | \$235,242 | \$0 | \$10,319,927 |
| 5.76% | \$2,690,084 | \$326,868 | \$0 | \$10,400,971 |
| 5.76% | \$3,423,786 | \$469,766 | \$0 | \$10,533,294 |
| 5.76% | \$4,211,651 | \$666,827 | \$0 | \$10,719,780 |
| 5.76% | \$4,461,391 | \$916,567 | \$0 | \$10,719,780 |
| 5.76% | \$4,740,527 | \$1,195,703 | \$0 | \$10,719,780 |
| 5.76% | \$5,032,449 | \$1,487,625 | \$0 | \$10,719,780 |
| 5.76% | \$5,363,141 | \$1,818,317 | \$0 | \$10,719,780 |
| 5.76% | \$5,725,071 | \$2,180,247 | \$0 | \$10,719,780 |
| 5.76% | \$6,120,145 | \$2,575,321 | \$0 | \$10,719,780 |
| 5.76% | \$6,551,695 | \$3,006,871 | \$0 | \$10,719,780 |
| 5.76% | \$7,022,347 | \$3,477,523 | \$0 | \$10,719,780 |
| 5.76% | \$7,533,744 | \$3,735,486 | \$0 | \$10,719,780 |
| 5.76% | \$8,099,290 | \$4,026,220 | \$0 | \$10,719,780 |
| 5.76% | \$8,725,689 | \$4,354,183 | \$0 | \$10,719,780 |
| 5.76% | \$9,420,550 | \$4,723,768 | \$0 | \$10,719,780 |
| 5.76% | \$10,192,608 | \$5,139,889 | \$0 | \$10,719,780 |
| 5.76% | \$11,036,695 | \$5,601,541 | \$0 | \$10,719,780 |
| 5.76% | \$11,940,652 | \$6,093,265 | \$0 | \$10,719,780 |
| 5.76% | \$12,908,969 | \$6,617,862 | \$0 | \$10,719,780 |
| 5.76% | \$13,949,072 | \$7,177,003 | \$0 | \$10,719,780 |
| 5.76% | \$15,061,171 | \$7,774,380 | \$0 | \$10,719,780 |
| 5.76% | \$16,247,860 | \$8,425,589 | \$0 | \$10,719,780 |
| 5.76% | \$17,508,873 | \$9,126,331 | \$0 | \$10,719,780 |
| 5.76% | \$18,849,918 | \$9,893,334 | \$0 | \$10,719,780 |
| 5.76% | \$20,271,444 | \$10,744,033 | \$0 | \$11,281,234 |
| 5.76% | \$21,779,534 | \$11,674,455 | \$0 | \$12,258,178 |
| 5.76% | \$23,377,638 | \$12,664,163 | \$0 | \$13,297,371 |
| 5.76% | \$25,012,914 | \$13,657,751 | \$0 | \$14,340,639 |
| 5.76% | \$26,680,910 | \$14,649,603 | \$0 | \$15,382,083 |
| 5.76% | \$28,381,643 | \$15,639,798 | \$0 | \$16,421,788 |
| 5.76% | \$30,116,420 | \$16,623,309 | \$0 | \$17,454,474 |
| 5.76% | \$31,878,347 | \$17,595,781 | \$0 | \$18,475,571 |
| 5.76% | \$33,759,111 | \$18,633,845 | \$0 | \$19,379,199 |
| 5.76% | \$35,777,846 | \$19,748,060 | \$0 | \$20,340,501 |
| 5.76% | \$37,955,603 | \$20,950,046 | \$0 | \$21,369,047 |
| 5.76% | \$40,319,012 | \$22,254,502 | \$0 | \$22,477,047 |

But as I mentioned earlier, both of this illustration on the previous page has two fundamental flaws:

- 1. The borrowing interest rate assumption is a static 4.50%.
- 2. The policy index credit assumption is a static 5.76%.

Whether or not the borrowing interest rate and policy index crediting rate is realistic is *not* the point.

The fundamental flaw is that they are both *static* rates.

Sure, these are just *hypothetical* percentages, but will *Positive Interest Arbitrage* ever happen year after year, in perpetuity?

Of course not.

In the real world, borrowing interest rates and policy index crediting rates experience volatility.

When a premium financing illustration shows a policy index crediting rate that is *always* greater than the borrowing interest rate, the *puppet master* behind the curtain has manipulated the spreadsheet to show a static *Positive Interest Arbitrage* in perpetuity.

Just about anyone can manipulate the interest rates on a spreadsheet to make the numbers work in favor of a premium financing arrangement.

But what if the S&P 500 experiences a negative return and the policy index credits 0.00% in the first few years of the policy?

The *First-Dollar Financing* arrangement illustrated on the previous page was illustrated assuming a static 5.76% index credit every year. Under this assumption, there were certain collateral requirements in the first several years.

However, if the policy index credited 0.00% in the first three years of the policy (due to negative S&P 500 returns), the collateral requirements would be drastically greater.

In the third year, the collateral requirement would jump from \$403,115 to \$698,650 as illustrated on the next page.

| COLL | COLLATERAL REQUIREMENTS BASED ON: | | | | | |
|----------------|--|--|--|--|--|--|
| POLICY YEAR | 5.76% INDEX CREDIT FOR FIRST 3 YEARS | 0.00% INDEX CREDIT FOR FIRST 3 YEARS | | | | |
| 1 | \$391,389 | \$448,263 | | | | |
| 2 | \$374,488 | \$530,660 | | | | |
| 3 | \$403,115 | \$698,650 | | | | |

In the third year, the advisor would have to call the client and explain why the lender is requiring them to post \$295,535 *more* collateral than what was originally illustrated. Think about how this unexpected surprise would make the client feel.

This is the reason why so many premium financed policies are surrendered, lawsuits are filed, and skepticism is amplified.

But *premium financing* is not the problem.

The real problem is two-fold:

- 1. The agent's lack of transparency in communicating increasing collateral requirements.
- 2. The client's inability to recall the conversation regarding increasing collateral liability potential.

All plausible excuses aside, if the advisor informs the client that their collateral requirement is now \$295,535 greater than was originally expected (a 73.31% increase above expected), the client will begin to distrust both the advisor and the entire premium financing arrangement.

Quite frankly, I don't blame the client for feeling this way.

In a traditional *First-Dollar Financing* arrangement where the client borrows all the premiums starting in year one, there will most likely be a collateral requirement for the first 6-12 years of the policy.

However, by having the client pay the first-year premium out-of-pocket in our proprietary *Leveraged Index Arbitrage*TM program, the need for outside collateral becomes a non-issue.

However to be fair, the *Leveraged Index Arbitrage*TM illustration was run at a static 5.76% policy index credit, which as we mentioned, is not realistic due to the absence of volatility.

Our proprietary software stress-tests the IUL by backtesting historical returns of the S&P 500 (not including dividends), and then applies an IUL's crediting method. Obviously, we also apply the policy charges to the calculation.

We illustrate the performance of this hypothetical index account during several different 40-year periods using historical S&P 500 performance.

One of these 40-year periods is called *The Sandwich*.

In *The Sandwich* 40-year run, we start and end with the lost decade – the 10-year period 2000-2009 – and *sandwiched* in between these two decades is the last 20-year period.

Equally as important to note, during the first three years of this period, the S&P 500 produced negative returns, where the IUL's policy index credit would have been 0.00%.

| YEAR | S&P 500 RETURN | POLICY INDEX CREDIT |
|------|-------------------|------------------------|
| 2000 | -10.14% | 0.00% |
| 2001 | -13.04% | 0.00% |
| 2002 | -23.37% | 0.00% |

This is also during the time where an IUL's policy charges would be the highest.

This is an important scenario to consider in a premium financing arrangement because the intent is to pay off the third-party loan with the accumulated cash value, usually somewhere between the 12^{th} and 20^{th} year of the policy.

If the policy happens to experience poor performance in the first 1-10 years, there may or may not be enough cash value in the policy to pay off the premium financing loan.

When a policy is illustrated using a static index credit (which is the norm in the life insurance industry), there is no way for the client to know if the premium financing loan exit strategy will work if the policy experiences poor performance in the beginning years of the policy.

Even if there is enough *Cash Surrender Value* in the policy to exit the loan using such funds, the *Net Amount At Risk* may be too great.

The Net Amount At Risk is the difference between the policy Cash Surrender Value and the Death Benefit.

For example, if the *Death Benefit* started out at \$10,000,000 and the cash value grew to \$10,000,000, the death benefit would most likely increase to approximately \$10,500,000 (assuming a 5.00% corridor).

In this example, the *Net Amount At Risk* is very low at only \$500,000 (the difference between the \$10,500,000 of *Death Benefit* and the \$10,000,000 of *Cash Surrender Value*). There would be plenty of cash value to support the relatively low *Cost Of Insurance (COI)* charges.

Conversely, if the policy *Cash Surrender Value* is stripped down to the bone to pay off the premium financing loan, this may create *Net Amount At Risk* problems in the form of higher *COI* charges.

If the policy was illustrated assuming the *Cash Surrender Value* was going to be \$7,000,000 in the 16th year to facilitate the loan payoff, but the poor policy performance resulted in only \$4,000,000 in *Cash Surrender Value*, and the premium financing loan payoff was made with \$3,500,000 withdrawal, the remaining *Cash Surrender Value* would only be \$500,000.

The *Net Amount At Risk* would then be \$9,500,000 (95% of the death benefit being at risk) as shown in the table below.

This creates a major problem because the *COI* charges would very rapidly eat up the remaining *Cash Surrender Value* and the policy would most likely lapse early.

\$ 4,000,000 policy cash value
-\$ 3,500,000 premium financing loan payoff
\$ 500,000 cash value after loan payoff

\$10,000,000 death benefit
-\$ 500,000 cash value after loan payoff
\$ 9,500,000 net amount at risk
95.00% death benefit liability at risk

In our *Sandwich* stress-tested model on the next page, we show the first 10 years and the last 10 years of a 40-year run using historical S&P 500 returns (not including dividends) from 2000-2009, and *sandwiched* in between these two decades is the 20-year run of 1999-2018.

In this 40-year constructed period, the *Compounded Annual Growth Rate (CAGR)* of the S&P 500 was 2.25% with dividends and 0.41% without dividends.

Using a 0.00% floor and a 9.25% cap in the IUL crediting method during this sequence of returns would have generated a 4.78% gross compounded annual policy index crediting rate (before policy charges). This is a testament to the IUL chassis and crediting method.

But what is so impressive about this stress test is that the sequence of returns is so poor, leading off with three 0.00% policy index credits in the first three years of the policy, which is an extremely adverse scenario for a premium financing program.

In this sequence, there are seven 0.00% policy index credits in the first fifteen years of the policy, and fourteen 0.00% policy index credits in the entire 40-year run, and the policy remains in force with healthy policy *Cash Surrender Values*.

In a traditional premium financing design, it is incredibly important to address the potential of a poor sequence of returns because if cash value suffers, the lender will require additional outside collateral if the policy cash surrender value falls below a certain threshold.

As a result of the client paying the first-year premium outof-pocket in our proprietary *Leveraged Index Arbitrage*TM program, even with this extremely adverse sequence of returns, you will notice that the client does not have to post any additional outside collateral because the *Policy Cash Surrender Value Net Of Loans* is always in a positive position.

| # YEAR | AGE | CAL YEAR | S&P 500 RETURN | INDEX CREDIT | GROSS POLICY CSV | LOAN BALANCE | COLLATERAL REQUIRED |
|-----------|-----|-------------|-------------------|-----------------|---------------------|-----------------|------------------------|
| 1 | 55 | 2000 | -10.14% | 0.00% | \$192,365 | \$0 | \$0 |
| 2 | 56 | 2001 | -13.04% | 0.00% | \$657,588 | \$590,804 | \$0 |
| 3 | 57 | 2002 | -23.37% | 0.00% | \$1,018,049 | \$1,181,608 | \$0 |
| 4 | 58 | 2003 | 26.38% | 9.25% | \$2,268,198 | \$1,772,412 | \$0 |
| 5 | 59 | 2004 | 8.99% | 8.99% | \$2,840,939 | \$2,363,216 | \$0 |
| 6 | 60 | 2005 | 3.00% | 3.00% | \$3,076,877 | \$2,954,020 | \$0 |
| 7 | 61 | 2006 | 13.60% | 9.25% | \$4,116,406 | \$3,544,824 | \$0 |
| 8 | 62 | 2007 | 3.52% | 3.52% | \$3,750,801 | \$3,544,824 | \$0 |
| 9 | 63 | 2008 | -38.49% | 0.00% | \$3,425,615 | \$3,544,824 | \$0 |
| 10 | 64 | 2009 | 23.65% | 9.25% | \$4,774,539 | \$3,544,824 | \$0 |
| 11 | 65 | 1999 | 19.53% | 9.25% | \$6,170,710 | \$3,544,824 | \$0 |
| 12 | 66 | 2000 | -10.14% | 0.00% | \$5,660,768 | \$3,544,824 | \$0 |
| 13 | 67 | 2001 | -13.04% | 0.00% | \$5,181,295 | \$3,544,824 | \$0 |
| 14 | 68 | 2002 | -23.37% | 0.00% | \$4,729,909 | \$3,544,824 | \$0 |
| 15 | 69 | 2003 | 26.38% | 9.25% | \$6,910,725 | \$3,544,824 | \$0 |
| 16 | 70 | 2004 | 8.99% | 8.99% | \$3,094,909 | \$0 | \$0 |
| 17 | 71 | 2005 | 3.00% | 3.00% | \$2,777,516 | \$0 | \$0 |
| 18 | 72 | 2006 | 13.60% | 9.25% | \$3,093,631 | \$0 | \$0 |
| 19 | 73 | 2007 | 3.52% | 3.52% | \$2,775,888 | \$0 | \$0 |
| 20 | 74 | 2008 | -38.49% | 0.00% | \$2,484,630 | \$0 | \$0 |
| 21 | 75 | 2009 | 23.65% | 9.25% | \$3,345,613 | \$0 | \$0 |
| 22 | 76 | 2010 | 12.63% | 9.25% | \$3,651,372 | \$0 | \$0 |
| 23 | 77 | 2011 | 0.10% | 0.10% | \$3,421,464 | \$0 | \$0 |
| 24 | 78 | 2012 | 13.29% | 9.25% | \$3,777,398 | \$0 | \$0 |
| 25 | 79 | 2013 | 29.43% | 9.25% | \$5,178,917 | \$0 | \$0 |
| 26 | 80 | 2014 | 11.54% | 9.25% | \$5,565,244 | \$0 | \$0 |
| 27 | 81 | 2015 | -0.73% | 0.00% | \$5,369,819 | \$0 | \$0 |
| 28 | 82 | 2016 | 9.54% | 9.25% | \$5,576,154 | \$0 | \$0 |
| 29 | 83 | 2017 | 19.42% | 9.25% | \$6,695,114 | \$0 | \$0 |
| 30 | 84 | 2018 | -6.24% | 0.00% | \$6,436,862 | \$0 | \$0 |
| 31 | 85 | 2000 | -10.14% | 0.00% | \$6,174,252 | \$0 | \$0 |
| 32 | 86 | 2001 | -13.04% | 0.00% | \$5,906,014 | \$0 | \$0 |
| 33 | 87 | 2002 | -23.37% | 0.00% | \$5,631,025 | \$0 | \$0 |
| 34 | 88 | 2003 | 26.38% | 9.25% | \$7,331,686 | \$0 | \$0 |
| 35 | 89 | 2004 | 8.99% | 8.99% | \$7,462,893 | \$0 | \$0 |
| 36 | 90 | 2005 | 3.00% | 3.00% | \$7,088,777 | \$0 | \$0 |
| 37 | 91 | 2006 | 13.60% | 9.25% | \$7,736,675 | \$0 | \$0 |
| 38 | 92 | 2007 | 3.52% | 3.52% | \$7,378,331 | \$0 | \$0 |
| 39 | 93 | 2008 | -38.49% | 0.00% | \$7,060,149 | \$0 | \$0 |
| 40 | 94 | 2009 | 23.65% | 9.25% | \$8,980,605 | \$0 | \$0 |

In the Leveraged Index ArbitrageTM program, if the Policy Cash Surrender Value Net Of Loans is in a positive position the policy is the sole collateral.

Due to this arrangement, the client is not required to post any additional collateral outside of the policy asset, hence no personal guaranty is required.

Now think about this for just one moment.

No personal guaranty requirements.

No outside collateral requirements.

The loan recourse is limited to the policy asset.

We have now stress-tested the *Leveraged Index* $Arbitrage^{TM}$ program during a 40-year run with terrible S&P performance – *The Sandwich* – and still, no outside collateral needed, no personal guarantor requirements, with recourse limited to the policy asset.

But there is still one more risk we have not addressed: Borrowing interest rate increases.

We will address this risk in the next chapter.

Chapter 4

Risk #2: Borrowing Rate Increases

Most premium financing programs depict a scenario using extremely low borrowing rate increases that have clearly been chosen to illustrate the positive arbitrage theory favorably.

In my opinion, if the client is making their ultimate decision based on this unrealistic scenario, they are blindly entering an arrangement without understanding the actual *Probability Of Risk*, nor the true *Consequence Of Risk*.

Unfortunately, this is commonplace in the premium financing arena. I have found that most premium financing clients have never been shown an adequately stress-tested scenario where enough *Negative Interest Arbitrage* years have been modeled.

The pace at which borrowing rates increase (assuming they are poised to increase) is certainly debatable, but when entering a premium financing arrangement, we believe the client should be transparently shown scenarios that depict extremely unfavorable borrowing rate conditions so they are aware of the larger interest payments they would potentially be responsible for paying.

When modeling the borrowing interest rates in our premium financing software, we run several projection models that are significantly more adverse than historical rates.

The reason we do this is to transparently show the client what happens in these different borrowing rate environments, so they fully understand this risk.

We also show them how our *Leveraged Index Arbitrage*TM program mitigates this risk, which no other premium financing firm does.

As we examine the *1-Year U.S. Treasury Daily Yield Curve (USTDYC)* rates over the last 21 years, the rate has decreased at a compounded annual rate of 5.31% from 1998-2018.

We will often times use this as the benchmark and show our base borrowing rate increase at 5.31% per year, but more often than not, we will model that rate increasing at 8.00% per year as our standard, default rate assumption. Our software can model whatever rate increase assumption the client wants to see in real time, immediately at the point of sale.

This is an incredibly valuable feature because we are able to address the client's concerns right there on the spot, modeling hyper-rate increases.

In addition, we will also let the client pick the type of schedule they want to see that increase based on. Some clients want to see the rate increase for the first ten years, then decrease for ten years, then increase for ten years, then decrease for ten years.

Some want to see the rate increase for twenty years, then decrease for twenty years.

And some want to see the rate increase every year for the next forty years in a row.

Our software can model all of these options with a simple click of a mouse button.

In our *Ultimate Stress Test*, we show *The Sandwich* 40-year run. Again, this is an S&P CAGR environment of 2.25% with dividends (0.41% without dividends). During this period, the policy index credit is 0.00% for 4 of the first 10 years, and 7 of the first 15 years.

From a borrowing interest rate perspective, we show the current 1-Year USTDYC increase 8.00% per year, every year for 40 years in a row.

We also model the client taking withdrawals to subsidize the higher interest payments. This is the interest payment increase (above what the payment would have been had the borrowing interest rate never increased).

It is important to note that taking withdrawals to subsidize the higher interest payments is NOT the plan. We merely model this scenario to show the client an alternative to surrendering the policy should they experience economic hardship due to unexpected (and substantially) higher interest payments. From a client cash flow perspective, this modeled environment *feels* like the client has a fixed borrowing interest rate.

Despite the compounded adverse effects of all of these stresses, the policy *Cash Surrender Value Net Of Loans* remains healthy. At this point, the client has run out of reasons to not do this

Again, I want to reiterate just how adverse this *Sandwich* scenario model is.

Our *Ultimate Stress Test* included:

- ✓ An S&P 500 40-year environment with a Compounded Annual Growth Rate of 2.25% including dividends (0.40% without dividends).
- ✓ Volatility and poor Sequence Of Returns that included a 0.00% index credit during 4 of the first 10 years of the policy, and 7 of the first 15 years of the policy.
- ✓ Hyper-increasing borrowing interest rates, modeling the 1-Year USTDYC rate increasing 8.00% per year, compounding for 40 years in a row.
- ✓ The *Policy Cash Surrender Value* subsidizing the increased interest payment amounts each year, using withdrawals up to basis, thus creating a simulated fixed borrowing interest rate (from a client cash flow perspective).
- ✓ No *High Early Cash Value Riders* used whatsoever.
- ✓ No Participating Loan Arbitrage Mirage.

...and it still works with the policy endowing at age 121.

As I said earlier, this is the most conservative and most heavily stress tested premium financing program in the industry.

DARREN SUGIYAMA & JEFF FAINE

Chapter 5 The Math Doesn't Lie

There are so many different premium financing programs being marketed right now. Some are antiquated, while some are new, gimmicky, and over-hyped.

We'll take a look at some of the overly-aggressive, *pie-in-the-sky* programs later in this book (Chapter 6), but in this chapter, we'll compare a traditional *First-Dollar Financing* program to our proprietary *Leveraged Index ArbitrageTM* program.

As discussed earlier, there are some distinct advantages to the *Leveraged Index Arbitrage*TM program where the client pays the first-year premium out-of-pocket from a *loan features* standpoint, summarized again below.

| | FIRST-DOLLAR FINANCING (With Collateral) | LEVERAGED INDEX ARBITRAGE (No Collateral) |
|--|--|---|
| Outside Collateral Requirement: | Yes | No |
| Personal Guarantor Requirement: | Yes | No |
| Corporate Guarantor Requirement: | Yes | No |
| Recourse To The Borrower: | Yes | No |
| Affects Client's Debt-To-Income Ratio: | Yes | No |

Below is a comparison from a premium design standpoint. Virtually the same cumulative premium is being loaded into the policy, with the same target premium.

| | | POLICY PREMIUMS | | | |
|----------------|---------------|---------------------------|------------------------------|--|--|
| POLICY YEAR | CLIENT AGE | FIRST-DOLLAR FINANCING | LEVERAGED INDEX ARBITRAGE | | |
| 1 | 55 | \$664,762 (BORROWED) | \$575,000 (PAID) | | |
| 2 | 56 | \$664,762 (BORROWED) | \$679,722 (BORROWED) | | |
| 3 | 57 | \$664,762 (BORROWED) | \$679,722 (BORROWED) | | |
| 4 | 58 | \$664,762 (BORROWED) | \$679,722 (BORROWED) | | |
| 5 | 59 | \$664,762 (BORROWED) | \$679,722 (BORROWED) | | |
| 6 | 60 | \$664,762 (BORROWED) | \$679,722 (BORROWED) | | |
| 7 | 61 | \$664,762 (BORROWED) | \$679,722 (BORROWED) | | |
| | | \$4,653,334 | \$4,653,332 | | |
| | | Total Premiums Loaded | Total Premiums Loaded | | |

In this scenario, the annual (and cumulative) interest payments are obviously less with the *Leveraged Index Arbitrage*TM program because less premium was borrowed due to the client paying the first year premium out-of-pocket.

| POLICY YEAR | CLIENT AGE | FIRST-DOLLAR FINANCING | LEVERAGED INDEX ARBITRAGE |
|----------------|---------------|--|--|
| 1 | 55 | \$33,504 | \$0 |
| 2 | 56 | \$69,710 | \$35,639 |
| 3 | 57 | \$108,941 | \$74,262 |
| 4 | 58 | \$151,557 | \$116,226 |
| 5 | 59 | \$197,954 | \$161,927 |
| 6 | 60 | \$248,572 | \$211,805 |
| 7 | 61 | \$303,893 | \$266,342 |
| 8 | 62 | \$318,898 | \$279,493 |
| 9 | 63 | \$335,103 | \$293,695 |
| 10 | 64 | \$352,605 | \$309,034 |
| 11 | 65 | \$333,703 | \$292,468 |
| 12 | 66 | \$316,314 | \$277,228 |
| 13 | 67 | \$300,315 | \$263,206 |
| 14 | 68 | \$285,597 | \$250,306 |
| 15 | 69 | \$272,056 | \$238,438 |
| | • | \$3,628,722 Cumulative Interest Paid | \$3,070,070 Cumulative Interest Paid |

Despite the first-year premium being paid out-of-pocket in the *Leveraged Index Arbitrage*TM program, the cumulative outlay is very similar due to the smaller annual interest payments.

| POLICY YEAR | CLIENT AGE | FIRST-DOLLAR FINANCING | LEVERAGED INDEX ARBITRAGE |
|----------------|---------------|-------------------------------------|-------------------------------------|
| 1 | 55 | \$33,504 | \$575,000 |
| 2 | 56 | \$69,710 | \$35,639 |
| 3 | 57 | \$108,941 | \$74,262 |
| 4 | 58 | \$151,557 | \$116,226 |
| 5 | 59 | \$197,954 | \$161,927 |
| 6 | 60 | \$248,572 | \$211,805 |
| 7 | 61 | \$303,893 | \$266,342 |
| 8 | 62 | \$318,898 | \$279,493 |
| 9 | 63 | \$335,103 | \$293,695 |
| 10 | 64 | \$352,605 | \$309,034 |
| 11 | 65 | \$333,703 | \$292,468 |
| 12 | 66 | \$316,314 | \$277,228 |
| 13 | 67 | \$300,315 | \$263,206 |
| 14 | 68 | \$285,597 | \$250,306 |
| 15 | 69 | \$272,056 | \$238,438 |
| | • | \$3,628,722 Cumulative Outlay | \$3,645,070 Cumulative Outlay |

But the cumulative outlay is where the similarities stop. Due to the different methods of funding and loan payoff amounts, the *Leveraged Index Arbitrage*TM program produces a significantly greater *Cash Surrender Value Net Of Loans*.

| CASH SURRENDER VALUE NET OF LOANS | | | | |
|-----------------------------------|---------------|---------------------------|------------------------------|--|
| POLICY YEAR | CLIENT AGE | FIRST-DOLLAR FINANCING | LEVERAGED INDEX ARBITRAGE | |
| 16 | 62 | \$3,915,026 | \$4,489,120 | |
| 17 | 63 | \$4,183,299 | \$4,799,721 | |
| 18 | 64 | \$4,472,476 | \$5,135,799 | |
| 19 | 65 | \$4,785,309 | \$5,501,042 | |
| 20 | 66 | \$5,124,341 | \$5,898,103 | |
| 21 | 67 | \$5,493,314 | \$6,330,861 | |
| 22 | 68 | \$5,895,141 | \$6,805,080 | |
| 23 | 69 | \$6,334,108 | \$7,325,636 | |
| 24 | 70 | \$6,815,582 | \$7,898,430 | |
| 25 | 71 | \$7,346,737 | \$8,533,608 | |
| 26 | 72 | \$7,935,275 | \$9,240,045 | |
| 27 | 73 | \$8,591,124 | \$10,030,396 | |
| 28 | 74 | \$9,325,382 | \$10,918,886 | |
| 29 | 75 | \$10,153,280 | \$11,904,802 | |
| 30 | 76 | \$11,083,177 | \$12,981,442 | |
| 31 | 77 | \$12,025,727 | \$14,072,699 | |
| 32 | 78 | \$12,973,860 | \$15,169,175 | |
| 33 | 79 | \$13,916,955 | \$16,259,229 | |
| 34 | 80 | \$14,846,526 | \$17,333,855 | |
| 35 | 81 | \$15,754,884 | \$18,379,252 | |
| 36 | 82 | \$16,706,335 | \$19,476,591 | |
| 37 | 83 | \$17,716,892 | \$20,638,784 | |
| 38 | 84 | \$18,792,453 | \$21,879,113 | |
| 39 | 85 | \$19,940,421 | \$23,203,362 | |
| 40 | 86 | \$21,173,351 | \$24,626,362 | |
| | | | | |

Similar to the Cash Surrender Value Net Of Loans performing substantially better in the Leveraged Index $Arbitrage^{TM}$ program, the Death Benefit Net Of Loans is also substantially greater.

The initial net death benefit in the traditional *First-Dollar Financing* program is \$9,856,093 compared to \$10,431,523 in the *Leveraged Index Arbitrage*TM program.

By the 40^{th} year (at age 86), it is \$3,487,540 greater – \$24,872,625 versus only \$21,385,085 in the *First-Dollar Financing* program – a 16.31% increase.

| DEATH | BENEFIT | COMPARISON | |
|----------------|---------------|---------------------------|------------------------------|
| POLICY YEAR | CLIENT AGE | FIRST-DOLLAR FINANCING | LEVERAGED INDEX ARBITRAGE |
| 16 | 62 | \$10,300,033 | \$10,851,444 |
| 17 | 63 | \$10,300,033 | \$10,851,444 |
| 18 | 64 | \$10,300,033 | \$10,851,444 |
| 19 | 65 | \$10,300,033 | \$10,851,444 |
| 20 | 66 | \$10,300,033 | \$10,851,444 |
| 21 | 67 | \$10,300,033 | \$10,851,444 |
| 22 | 68 | \$10,300,033 | \$10,851,444 |
| 23 | 69 | \$10,300,033 | \$10,851,444 |
| 24 | 70 | \$10,300,033 | \$10,851,444 |
| 25 | 71 | \$10,300,033 | \$10,851,444 |
| 26 | 72 | \$10,300,033 | \$10,851,444 |
| 27 | 73 | \$10,300,033 | \$10,851,444 |
| 28 | 74 | \$10,300,033 | \$11,464,830 |
| 29 | 75 | \$10,660,944 | \$12,500,042 |
| 30 | 76 | \$11,637,336 | \$13,630,514 |
| 31 | 77 | \$12,627,014 | \$14,776,334 |
| 32 | 78 | \$13,622,554 | \$15,927,634 |
| 33 | 79 | \$14,612,802 | \$17,072,191 |
| 34 | 80 | \$15,588,852 | \$18,200,548 |
| 35 | 81 | \$16,542,628 | \$19,298,214 |
| 36 | 82 | \$17,541,652 | \$20,450,421 |
| 37 | 83 | \$18,425,568 | \$21,464,335 |
| 38 | 84 | \$19,356,227 | \$22,535,486 |
| 39 | 85 | \$20,339,229 | \$23,667,429 |
| 40 | 86 | \$21,385,085 | \$24,872,625 |
| | | | |

The reason for this drastic discrepancy is that the *First-Dollar Financing* program incurred greater debt (premiums borrowed in years 1-7 instead of only years 2-7).

When the cash value is used to payoff the premium financing loan, a greater drawdown amount (\$4,653,334) is required in the *First-Dollar Financing* program compared to only \$4,078,332 in the *Leveraged Index Arbitrage*TM program).

It is also important to note that in these two premium financing models, we used:

- 1. The exact same products from the exact same carriers.
- 2. The exact same target premiums.

It is difficult to believe, but this level of mathematical transparency is unique to Lionsmark Capital.

No other firm has the ability to model a true apples-toapples comparison between life insurance funding options.

In fact, the majority of the premium financing firms use *smoke & mirrors gimmicks* in their illustrations, which is extremely misleading to clients.

In the next chapter, we will expose the dirty little secrets of some of these misleading premium financing programs and address where the holes are (and where the bodies are buried).

DARREN SUGIYAMA & JEFF FAINE

Chapter 6 Smoke & Mirrors Gimmicks

HBO recently aired a documentary called *The Inventor:* Out For Blood In Silicon Valley about Elizabeth Holmes, founder of self-proclaimed revolutionary healthcare company *Theranos*.

Her story is quite bizarre.

Elizabeth Holmes dropped out of *Stanford University* in 2004 to start *Theranos* and was referred to by some as *The Next Steve Jobs*.

By 2014, *Theranos* was valued at \$9 billion, which made Holmes the youngest self-made female billionaire in the world.

Her claim was that instead of traditional phlebotomy, her technology could run a series of over 200 health-related reports from a simple finger-prick blood test.

This revolutionary claim would radically change the world of healthcare forever.

Holmes had the ability to charm some of the most powerful and influential people in this country to sit on her board as well as invest hundreds of millions of dollars.

Her Board Of Directors included:

- ➤ Former Secretary of State Henry Kissinger
- > Former Secretary of Defense Bill Perry
- ➤ Former Secretary of State George Shultz
- Former Senator Sam Nunn
- Former Senator Bill Frist
- Former Navy Admiral Gary Roughead
- > Former Marine Corps General James Mattis
- ➤ Former CEO of Wells Fargo Dick Kovacevich
- ➤ Former CEO of Bechtel Riley Bechtel

Her roster of early investors were equally impressive which included:

- ➤ The Walton Family (founders of Walmart): \$150 million
- Rupert Murdoch: \$125 million
- > Betsy DeVos (U.S. Secretary of Education): \$110 million
- ➤ The Cox Family (Atlanta Billionaires)
- > Members of a South African diamond dynasty
- Carlos Slim (Billionaire Mexican TelCom tycoon)

Theranos not only caught fire with the Silicon Valley community of investors, but it also signed a contract with Walgreens that put Theranos blood test centers inside Walgreens stores. Holmes graced the covers of respected magazines including Inc, Forbes and Fortune. All of this hype, and yet the technology was never actually proven to work.

It was all *theory*. What makes this theoretically-based company even more scandalous was that not only was the technology never *proven* – it was actually *disproven*.

Not only was it disproven – it was covered up.

Once disproven, the *Theranos* centers inside *Walgreens* stores actually stopped using the *Theranos* technology. They started secretly using standard blood draws using old school phlebotomy methods and sent off the blood samples to *Siemens* to process the test results. Eventually the scam was made public, and everything came crashing down. Just two years after its \$9 billion valuation, *Theranos* had a market value less than zero and was cited as a massive fraud by the *Securities Exchange Commission* (SEC).

So why am I telling you about the fraudulent claims of *Theranos* and Elizabeth Holmes?

The reason is that I see premium financing programs that are being sold all over the country using similar deceptive tactics.

The *smoke & mirrors gimmicks* they use to manipulate their spreadsheets are so obvious to the *trained eye*, however to the *untrained eye*, these misleading details go undetected.

These premium financing programs look like *the best investments ever*, illustrating huge income streams with concurrent cash value increases, despite the massive income drawdowns.

I'm assuming the Walton Family, Rupert Murdoch, Betsy DeVos and Carlos Slim felt the same way about *Theranos* and Elizabeth Holmes. I'm also sure the majority of premium financing clients felt the same about the charlatan that sold them their *fugazi* program.

The first of many *too-good-to-be-true* premium financing arrangements is based on the manipulated façade of *Interest Accrual Arbitrage*.

The Façade Of Interest Accrual Arbitrage

Several premium financing firms sell a *semi-free insurance* program where the client accrues the interest (instead of legitimately paying the interest due). Essentially, here's how this scheme works. They'll tell the client,

"You don't have to make the interest payments. We'll just roll the interest payments back into the principal loan balance. Why would you make the interest payments if you don't have to? Just let the growth of the cash value of the policy pay it off later?"

This *kick-the-can-down-the-road* philosophy is exactly what caused people who opted for over-leveraged negative amortization mortgages to lose their homes during the mortgage crisis of 2008

When a client accrues the interest in a premium financing program, their debt compounds and compounds and compounds. Compounding debt is one of the most dangerous traps to fall into if you don't truly understand the math.

I'm going to break down the math for you by showing you an actual client case study. What you are about to witness will make you cringe.

If you're a life insurance agent reading this book, and you've sold an interest accrual-based premium financed life insurance policy, this will forever change your perspective.

In this model on the next page, the client is scheduled to borrow \$721,169 in annual premium in years 1-10, totaling \$7,211,690 in premium.

We see the client paying roughly \$86,000 for the first 10 years, but these are not true interest payments. They are *black box numbers* that the premium financier is claiming to be partial interest payments plus ambiguous fees.

But look at the *Interest Owed* column. These are the actual speculated interest payments due, however the client is not actually paying these interest payments. The interest is being accrued and rolled back into the principal loan balance in the *Accrued Loan* column.

Each year, the client is falling deeper and deeper into debt. They're not robbing Peter to pay Paul. They're avoiding paying Paul (the lender) altogether, hoping that the cash value growth will outpace the compounding loan debt.

In the 13th year, this program is speculating that the policy cash value will be \$10,488,641 (in the *Policy CSV* column) and the accrued, compounded loan debt will only be \$9,445,921 (in the *Accrued Loan Balance* column).

The proposal shows the cash value paying off the \$9,445,921 in the 14th year (in the *Annual Drawdowns* column) which according to the illustration shows a *Net Cash Surrender Value* of \$1,348,018 (in the *Policy CSV* column, year 14).

Clearly, \$10.4 million minus \$9.4 million does not equal \$1.3 million.

So how is the policy illustration showing \$1.3 million in *Cash Surrender Value*?

Does that mean that the illustration is showing a 30% cash value gain in the 14th year?

Obviously not.

I will explain how they arrived at this *Cash Surrender Value* on page 42.

INTEREST ACCRUAL PROPOSAL (not a Lionsmark Capital proposal)

| POLICY YEAR | CLIENT AGE | BORROWED PREMIUM | ACCRUED LOAN BAL | LOAN RATE | INTEREST OWED | "INTEREST" PAID | ANNUAL DRAWDOWNS | POLICY CSV |
|----------------|---------------|---------------------|---------------------|--------------|------------------|--------------------|---------------------|---------------|
| 1 | 56 | \$721,169 | \$760,833 | 3.97% | \$30,625 | \$85,716 | \$0 | \$189,249 |
| 2 | 57 | \$721,169 | \$1,485,608 | 4.00% | \$60,028 | \$86,412 | \$0 | \$844,442 |
| 3 | 58 | \$721,169 | \$2,210,383 | 4.02% | \$89,945 | \$86,269 | \$0 | \$1,583,458 |
| 4 | 59 | \$721,169 | \$2,935,158 | 4.04% | \$120,228 | \$86,010 | \$0 | \$2,334,191 |
| 5 | 60 | \$721,169 | \$3,713,863 | 4.07% | \$153,104 | \$85,374 | \$0 | \$3,176,510 |
| 6 | 61 | \$721,169 | \$4,547,285 | 4.10% | \$188,648 | \$84,616 | \$0 | \$4,085,648 |
| 7 | 62 | \$721,169 | \$5,418,241 | 4.12% | \$265,181 | \$83,539 | \$0 | \$5,064,382 |
| 8 | 63 | \$721,169 | \$6,328,838 | 4.14% | \$265,822 | \$82,114 | \$0 | \$6,117,440 |
| 9 | 64 | \$721,169 | \$7,281,308 | 4.17% | \$307,695 | \$80,190 | \$0 | \$7,262,341 |
| 10 | 65 | \$721,169 | \$8,278,015 | 4.20% | \$351,932 | \$80,000 | \$0 | \$8,470,127 |
| 11 | 66 | \$0 | \$8,648,031 | 4.22% | \$370,016 | \$0 | \$0 | \$9,089,190 |
| 12 | 67 | \$0 | \$9,036,979 | 4.24% | \$388,948 | \$0 | \$0 | \$9,760,663 |
| 13 | 68 | \$0 | \$9,445,921 | 4.27% | \$408,942 | \$0 | \$0 | \$10,488,641 |
| 14 | 69 | \$0 | \$0 | 4.30% | \$0 | \$0 | -\$9,445,921 | \$1,348,018 |
| 15 | 70 | \$0 | \$0 | 4.32% | \$0 | \$0 | -\$319,151 | \$1,367,702 |
| 16 | 71 | \$0 | \$0 | 4.34% | \$0 | \$0 | -\$319,151 | \$1,387,570 |
| 17 | 72 | \$0 | \$0 | 4.37% | \$0 | \$0 | -\$319,151 | \$1,454,468 |
| 18 | 73 | \$0 | \$0 | 4.40% | \$0 | \$0 | -\$319,151 | \$1,580,797 |
| 19 | 74 | \$0 | \$0 | 4.42% | \$0 | \$0 | -\$319,151 | \$1,779,093 |
| 20 | 75 | \$0 | \$0 | 4.44% | \$0 | \$0 | -\$319,151 | \$2,064,532 |
| 21 | 76 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$2,455,674 |
| 22 | 77 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$2,944,430 |
| 23 | 78 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$3,532,496 |
| 24 | 79 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$4,235,249 |
| 25 | 80 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$5,065,760 |
| 26 | 81 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$6,043,194 |
| 27 | 82 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$7,179,170 |
| 28 | 83 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$8,496,475 |
| 29 | 84 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$10,021,389 |
| 30 | 85 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$11,770,185 |
| 31 | 86 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$13,471,486 |
| 32 | 87 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$15,095,383 |
| 33 | 88 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$16,587,538 |
| 34 | 89 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$17,917,501 |
| 35 | 90 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$19,031,088 |
| 36 | 91 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$20,258,230 |
| 37 | 92 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$21,608,777 |
| 38 | 93 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$23,119,837 |
| 39 | 94 | \$0 ©0 | \$0 ©0 | 5.50% | \$0 ©0 | \$0 ©0 | -\$319,151 | \$24,825,174 |
| 40 | 95 | \$0 | \$0 | 5.50% | \$0 | \$0 | -\$319,151 | \$26,654,586 |

There are several mathematically incorrect elements shown above.

First of all, the *Accured Loan Balance* column, multiplied by the *Loan Rate* does not equal the *Interest Owed* column.

Secondly, the "Interest" Paid column is an ambiguous number whose calculation is not disclosed in the proposal. The figure changes each year and is not truly tied to the actual interest owed whatsoever. The proposal from the premium financing firm that created this claims that it is a combination of interest and fees.

In this *Interest Accrual* model, the illustration is showing the client only borrowing \$7.2 million in premium, but owing \$9.4 million in accrued debt. That \$9.4 million in debt assumes the borrowing interest rate is only increasing 0.02%-0.03% per year (in the *Loan Rate* column).

To put that in perspective, it would take 33 years for the borrowing rate to increase from 4.00% to 5.00%. This extremely low borrowing rate increase has clearly been chosen to illustrate a minimal debt accrual scenario. The reason this interest accrual program appears to work is quite simple. It assumes a static policy crediting rate of 6.17%, and a premium financing borrowing interest rate that starts at only 3.97%, and never increases to a rate greater 4.27%. This scenario is modeling perpetual positive interest arbitrage, year after year.

This is not a realistic scenario because the S&P 500 will never produce a positive return every year, and it is unlikely that the premium financing borrowing rate will never increase greater than 4.27%.

As an example, 1-Month LIBOR opened at 5.32% in 2007, and 9.25% in 1989. The lender would then add a spread on top of the base LIBOR rate. Clients should absolutely be shown what happens to the premium financing program in high borrowing interest rate environments, however often times, they are not.

In addition, the reason the illustration is able to show an annual drawdown of \$319,151 every year after the premium financing loan is paid off is due to them illustrating participating loans, wherein the participating policy loan rate is a static 4.65% and the policy crediting rate is the same static 6.17% as we mentioned earlier. The reason this *fantasy land* number exists in

the illustration is they are illustrating *participating policy loans* instead of *fixed policy loans*. Let's discuss the difference between the two types of policy loans.

Fixed Loans

Fixed Loans tend to be the simplest and most conservative of policy loan options. Let's say the client took a \$100,000 fixed policy loan. In a fixed policy loan, that \$100,000 would technically be *charged* a *Fixed Loan Rate (FLR)*, say 2.25% for example. However it would also be *credited* a fixed interest rate – the same 2.25%

\$100,000 Policy Loan

x 2.25% Fixed Loan Rate

\$2,250 Interest Charged

\$100,000 Cash Value <u>x 2.25% Crediting Rate</u> **\$2,250 Cash Value Earned**

The fixed interest *charged* (2.25%) is the same rate as the fixed interest *credited* (2.25%) and would produce a net zero interest charge.

Participating Loans

The second type of loan rate is called a *Participating Loan Rate (PLR)*. Some insurance companies will refer to the *PLR* as an *Indexed Loan Rate* or an *Alternate Loan Rate*. For example, if the insurance carrier's *Participating Loan Rate* was 4.65% in a given year, and the policy's index credit was 6.17% in that same year, then the cash value would experience a 1.52% positive arbitrage gain.

6.17% Policy Index Credit
- 4.65% Participating Loan Rate
1.52% Positive Arbitrage

Using the \$100,000 example we just used, the client would receive a \$6,170 credit in policy cash value (6.17% return on the \$100,000 that still exists in the policy), and be charged \$4,650 in policy loan interest (4.65% interest on the \$100,000 policy loan), netting the client a \$1,520 gain.

\$6,170 Policy Index Credit
- \$4,650 Participating Loan Interest Charge
\$1,520 Positive Arbitrage Cash Value Gain

In this scenario, the client would put \$100,000 in their own pocket (tax-free), yet their policy cash value would still grow \$1,520 in that year. The \$100,000 policy loan would be later netted against the death benefit at the time of the client's passing.

Remember how this scenario pencils out because I'm about to explain how these *smoke & mirrors* premium financiers use this manufactured positive arbitrage to their deceptive advantage. What they don't illustrate is the *Consequence Of Risk*.

If the S&P 500 produces a negative return in a given year, assuming the IUL has a 0.00% protective floor, the policy's index would credit 0.00% in that year (instead of 6.17%). The *Participating Loan Rate* is still 4.65%. In this scenario, the loan amount would experience a -4.65% drag/loss.

0.00% Policy Index Credit
- 4.65% Participating Loan Rate
-4.65% Drag/Loss

Using the \$100,000 example again, the policy cash value would receive a \$0 credit (0.00% return on the \$100,000), and be charged \$4,650 in policy loan interest (4.65% interest on the \$100,000 policy loan), netting the client a \$4,650 loss (not including the policy charges).

\$ 0 Policy Index Credit
- \$4,650 Participating Loan Interest Charge
-\$4,650 Negative Arbitrage Cash Value Loss

This doesn't sound that bad when we use units of only \$100,000 and limit that scenario to only one year, but what happens when the numbers are larger?

I've seen premium financing programs that only show *Policy Participating Loans*, and they always illustrate a policy *Index Credit* greater than the *Participating Loan Rate*, creating positive interest arbitrage gains EVERY year.

In my opinion, this is truly manipulative because it assumes that the *Index Credit* will ALWAYS be greater the *Participating Loan Rate* every year, which nearly impossible.

In the case study we just discussed, notice that despite the illustration showing annual income drawdowns of \$319,151 for 26

years in a row, the policy cash surrender value magically continues to increase each year, despite the \$319,151 drawdowns.

This is the *smoke & mirrors* trick many premium financing firms use, showing a carrier illustration where:

- 1. The *Policy Index Credit* is positive every year.
- 2. The illustrated *Participating Loan Rate* is perpetually lower than the *Policy Index Credit*.

In this case study, the premium financing firm shows the policy earning 6.17% every year, and a *Participating Loan Rate* of only 4.65%. This is intentionally leading the client to believe something that will never happen in reality.

In the *Annual Drawdowns* column below, we see the \$9,445,921 premium financing loan balance paid off in the 14th year using a *Participating Loan* (instead of a true withdrawal), and \$319,151 income drawdowns that continue for the next 26 years.

| POLICY YEAR | CLIENT AGE | ANNUAL DRAWDOWNS | CASH SURRENDER VALUE |
|----------------|---------------|---------------------|-------------------------|
| 13 | 67 | \$0 | \$10,488,641 |
| 14 | 68 | -\$9,445,921 | \$1,348,018 |
| 15 | 69 | -\$319,151 | \$1,367,702 |
| 16 | 70 | -\$319,151 | \$1,387,570 |
| 17 | 71 | -\$319,151 | \$1,454,468 |
| 18 | 72 | -\$319,151 | \$1,580,797 |
| 19 | 73 | -\$319,151 | \$1,779,093 |
| 20 | 74 | -\$319,151 | \$2,064,532 |
| 21 | 75 | -\$319,151 | \$2,455,674 |
| 22 | 76 | -\$319,151 | \$2,944,430 |
| 23 | 77 | -\$319,151 | \$3,532,496 |
| 24 | 78 | -\$319,151 | \$4,235,249 |
| 25 | 79 | -\$319,151 | \$5,065,760 |
| 26 | 80 | -\$319,151 | \$6,043,194 |
| 27 | 81 | -\$319,151 | \$7,179,170 |
| 28 | 82 | -\$319,151 | \$8,496,475 |
| 29 | 83 | -\$319,151 | \$10,021,389 |
| 30 | 84 | -\$319,151 | \$11,770,185 |
| 31 | 85 | -\$319,151 | \$13,471,486 |
| 32 | 86 | -\$319,151 | \$15,095,383 |
| 33 | 87 | -\$319,151 | \$16,587,538 |
| 34 | 88 | -\$319,151 | \$17,917,501 |
| 35 | 89 | -\$319,151 | \$19,031,088 |
| 36 | 90 | -\$319,151 | \$20,258,230 |
| 37 | 91 | -\$319,151 | \$21,608,777 |
| 38 | 92 | -\$319,151 | \$23,119,837 |
| 39 | 93 | -\$319,151 | \$24,825,174 |
| 40 | 94 | -\$319,151 | \$26,654,586 |
| | | | |

Notice the *Cash Surrender Value* continues to grow every year after the premium financing loan payoff in 14, despite the \$319,151 additional annual drawdowns.

So how is this even possible?

Let me break down the magical illusion of how this premium financing firm conveniently illustrated *Participating Policy Loans*, manipulating the numbers to create their *fairy tale*.

It is important to note that this magic trick ONLY works when the illusion of perpetual positive arbitrage is mischievously created, where the *Policy Index Crediting Rate* (policy performance) is greater than the *Participating Loan Rate* (*PLR*) every single year.

This is so misleading, I literally can't believe anyone falls for this magic trick, but plenty of clients do.

To be blunt, plenty of agents fall for this trick as well.

Premium financing firms that utilize this trick are stacking the deck in their favor, creating a fantasy land scenario that will never happen in reality.

Here's the math behind the illusion.

With a Start Of Year 14 Cash Value of \$10,488,641 (line **A**) and Policy Charges of \$416,250 (line **B**), the Accumulatd Value Minus Charges becomes \$10,072,391 (line **C**).

| С | Accumulated Value Minus Charges: | \$10,072,391 |
|---|----------------------------------|--------------|
| В | Policy Charges: | - \$416,250 |
| Α | Start Of Year 14 Cash Value: | \$10,488,641 |

Assuming the client takes a \$9,445,921 *Participating Policy Loan* in the 14th year to pay off the premium financing loan (**line D**), a *Participating Loan Rate* of 4.65% (**line E**) would create an interest due amount of \$439,235 (**line F**).

| F | Participating Loan Interest Due/Accrued: | | -\$439,235 | |
|---|---|-----|-------------|---|
| Е | Participating Loan Rate: | X | 4.65% | _ |
| D | Participating Policy Loan To Pay Off PF Loan: | -\$ | \$9,445,921 | |

This proposal assumed the interest amount due would be accrued and rolled back into the policy loan debt.

This would cause additional compounding debt, of which the client would owe additional interest on the larger accrued debt the following year.

Essentially, they would be charged interest on their accrued interest, which compounds year after year after year.

The policy was illustrated assuming a 6.17% *Policy Index Credit* (**line G**). In this particular IUL policy, a 1.83 multiplier bonus would be applied in year 14 (**line H**), resulting in an 11.29% *Cash Value Credit* (**line I**).

| ı | Cash Value Credit With Multiplier Bonus: | 11.29% |
|---|--|--------|
| Н | Multiplier Bonus: | x 1.83 |
| G | Illustrated Policy Index Credit: | 6.17% |

This 11.29% would be applied to the \$10,280,516 Average Monthly Accumulated Value, resulting in a \$1,160,783 Policy Interest Credit (line L).

| L | Policy Interest Credit: | \$1,160,783 |
|---|--|--------------|
| K | Cash Value Credit With Multiplier Bonus: | 11.29% |
| J | Average Monthly Accumulated Value: | \$10,280,516 |

This interest credit would then be added to the \$10,072,391 *Accumulated Value Minus Charges*.

The \$9,445,921 participating loan would be backed out, as would the \$439,235 participating loan interest due/accrued.

The result would be an *End Of Year 14 Net Cash Surrender Value* of \$1,348,018 (**line M**).

| М | End Of Year 14 Net Cash Surrender Value: | \$1,348,018 |
|---|---|--------------|
| L | Policy Interest Credit: | \$1,160,783 |
| F | Participating Loan Interest Due/Accrued: | -\$439,235 |
| D | Participating Policy Loan To Pay Off PF Loan: | -\$9,445,921 |
| С | Accumulated Value Minus Charges: | \$10,072,391 |

Next is the summary ledger of this entire depiction, as illustrated by the premium financing firm that originally sold this case using this mischievously manipulated scenario.

| | YEAR 14: 6.17% INDEX CREDIT (PARTICIPATING LOAN TO | PAY OFF PF LOAN) |
|---|--|------------------|
| Α | Start Of Year 14: Policy Cash Surrender Value: | \$10,488,641 |
| В | Policy Charges: | -\$416,250 |
| С | Accumulated Value Minus Charges: | \$10,072,391 |
| | | |
| D | Participating Loan: | -\$9,445,921 |
| E | Participating Loan Rate: | 4.65% |
| F | Participating Loan Interest Due/Accrued: | -\$439,235 |
| | | |
| G | Illustrated Policy Index Credit: | 6.17% |
| Н | Multiplier Bonus: | 1.83 |
| I | Cash Value Credit With Multiplier Bonus: | 11.29% |
| | | |
| J | Average Monthly Accumulated Value: | \$10,280,516 |
| K | Cash Value Credit With Multiplier Bonus: | 11.29% |
| L | Policy Interest Credit: | \$1,160,783 |
| | Accumulated Value Minus Charges: | \$10,072,391 |
| | Participating Loan: | -\$9,445,921 |
| | Participating Loan Interest Due/Accrued: | -\$439,235 |
| М | End Of Year 14: Net Cash Surrender Value: | \$1,348,018 |

Remember, this scenario above assumes that the policy will receive an index credit of 6.17% every single year. It also assumes that the policy will receive the multiplier credit every year as well, which only exists when the index credit is greater than 0.00%.

If the policy receives a 0.00% index credit, there is no multiplier bonus credit. Additionally, a poor *sequence of returns* could worsen things exponentially. But even if the policy *does* perform at 6.17% every year in years 1-13, then receives just one 0.00% policy index credit in the 14th year, this policy falls apart.

Year 14: 0.00% Index Credit (Participating Loans)

If the policy receives the illustrated 6.17% index credit every year, but then in the 14th year, receives a 0.00% index credit, everything falls apart.

Just ONE year of a 0.00% index credit.

The *Participating Loan* interest charge would remain the same at \$439,235 (**line F**). With a 0.00% policy index credit, the cash value would receive a \$0 *Policy Interest Credit* (**line L**).

Add this \$0 credit to the *Accumulated Value Minus Charges*, then back out the \$9,445,921 *Participating Loan*, then back out the \$439,235 in *Participating Loan Interest Due/Accrued*, and the *End Of Year 14 Policy Cash Surrender Value* is only \$187,235 (**line M**).

| | YEAR 14: 0.00% INDEX CREDIT | |
|---|--|--------------|
| Α | Start Of Year 14: Policy Cash Surrender Value: | \$10,488,641 |
| В | Policy Charges: | -\$416,250 |
| С | Accumulated Value Minus Charges: | \$10,072,391 |
| D | Participating Loan: | -\$9,445,921 |
| Е | Participating Loan Rate: | 4.65% |
| F | Participating Loan Interest Due/Accrued: | -\$439,235 |
| G | Illustrated Policy Index Credit: | 0.00% |
| Н | Multiplier Bonus: | 1.00 |
| I | Cash Value Credit With Multiplier Bonus: | 0.00% |
| J | Average Monthly Accumulated Value: | \$10,280,516 |
| K | Cash Value Credit With Multiplier Bonus: | 0.00% |
| L | Policy Interest Credit: | \$0 |
| | Accumulated Value Minus Charges: | \$10,072,391 |
| | Participating Loan: | -\$9,445,921 |
| | Participating Loan Interest Due/Accrued: | -\$439,235 |
| М | End Of Year 14: Net Cash Surrender Value: | \$187,235 |

Just ONE year of a 0.00% index credit dramatically affects the viability of this premium financing arrangement, as <u>a mere</u> \$187,235 Cash Surrender Value will most likely lapse this policy due to the Net Amount At Risk being too high.

Again, look at the difference in outcome just ONE year of the policy receiving a 6.17% index credit versus of 0.00% makes in that 14th year.

| End Of Year 14 Net Cash Surrender Value: | \$1,348,018 | vs. | \$187,235 |
|--|-------------|-----|-----------|
| Policy Index Credit In Year 14: | 6.17% | VS. | 0.00% |
| Policy Index Credit In Years 1-13: | 6.17% | VS. | 6.17% |

Even more disturbing, as mentioned earlier in this book, we reconstructed this exact same illustration in the carrier's software using a static index credit of 5.76% (instead of 6.17%), and the policy LAPSED in the 14th year.

Just 0.41% less in policy performance, and their entire premium financing program blows up.

This is the risk of using *Interest Accrual* programs.

This is also the risk of using *Participating Policy Loans* inappropriately, showing static positive arbitrage every year.

Now, this doesn't mean that *Participating Policy Loans* are bad. It just means that illustrating them in a scenario where the policy crediting rate (ie: 6.17%) is always greater than the *Participating Loan Rate* (ie: 4.65%) paints a very misleading picture because in the real world, volatility will exist, as will occasional negative interest arbitrage.

Sure it looks good on paper, but just like a cubic zirconia looks good on social media... just like Bernie Madoff's portfolio returns looked good on his fake fund statements... just like every get rich quick scheme promises... this fabricated and manipulated *Participating Loan* positive arbitrage doesn't exist in reality.

This is the *smoke & mirrors* game that so many premium financing programs are based on.

We call this *The Participating Loan Arbitrage Mirage*, and it's an absolute crime.

So why does everyone else illustrate a *Policy Participating Loan* to pay off the *Premium Financing* loan instead of a *Withdrawal Up To Basis*?

This is one of the dirty little secrets that premium financing firms don't want you to know.

They cheat the numbers.

Again, here's how they do it.

They illustrate a perpetual *Fabricated Positive Interest Arbitrage* (which will never happen), and they're doing it on both the premium financing side, as well as the policy loans side.

| PREMIUM FINANCING FABRICATION | |
|---|---------|
| Policy Index Crediting Rate: | 6.17% |
| Premium Financing Borrowing Rate: | - 4.50% |
| Fabricated Positive Interest Arbitrage: | 1.67% |

| PARTICIPATING LOAN FABRICATION | |
|---|---------|
| Policy Index Crediting Rate: | 6.17% |
| Policy Participating Loan Rate: | - 4.65% |
| Fabricated Positive Interest Arbitrage: | 1.52% |

This static interest *crediting rate* and *charge rate* has been manipulated to tell a great story that only exists in *Fantasy Land*.

No one in their right mind would buy this ridiculous *Participating Loan Arbitrage Mirage* if they truly understood the risk.

Just one year of a 0.00% policy index credit, and the entire program falls apart.

But it keeps getting worse (as if that wasn't bad enough).

This policy was sold last year assuming the carrier's AG49 max rate of 6.17%.

We ran the exact same unrealistic scenario of the borrowing rate only increasing 0.02%-0.03% per year using the exact same IUL product at 5.76% (which is the current AG49 max rate this year).

We modeled the exact same \$9,445,921 loan payoff in the same 14th year.

Notice, the policy lapses in the 14th year.

| POLICY YEAR | CLIENT AGE | BORROWED PREMIUM | PAY OFF LOAN FROM CSV | CASH SURRENDER VALUE | DEATH BENEFIT |
|----------------|---------------|------------------|-----------------------------|----------------------------|------------------|
| 1 | 56 | \$721,169 | \$0 | \$210,422 | \$10,998,170 |
| 2 | 57 | \$721,169 | \$0 | \$906,439 | \$11,550,315 |
| 3 | 58 | \$721,169 | \$0 | \$1,560,419 | \$12,189,910 |
| 4 | 59 | \$721,169 | \$0 | \$2,288,095 | \$12,903,196 |
| 5 | 60 | \$721,169 | \$0 | \$3,099,553 | \$13,700,269 |
| 6 | 61 | \$721,169 | \$0 | \$3,970,851 | \$14,557,176 |
| 7 | 62 | \$721,169 | \$0 | \$4,903,598 | \$15,475,539 |
| 8 | 63 | \$721,169 | \$0 | \$5,902,588 | \$16,460,139 |
| 9 | 64 | \$721,169 | \$0 | \$6,983,795 | \$17,512,570 |
| 10 | 65 | \$721,169 | \$0 | \$8,118,483 | \$18,618,483 |
| 11 | 66 | \$0 | \$0 | \$8,649,026 | \$18,618,483 |
| 12 | 67 | \$0 | \$0 | \$9,220,358 | \$18,618,483 |
| 13 | 68 | \$0 | \$0 | \$9,836,852 | \$18,618,483 |
| 14 | 69 | \$0 | -\$9,445,921 | POLICY LAPSE | POLICY LAPSE |
| | | \$7,211,690 | -\$9.445.921 | | |

Do you think the premium financing intermediary that designed this interest accrual program adequately stress tested their model?

Of course not. If they did, they would have to show the interest accrual model working at 6.17%, but lapsing at 5.76% (a mere 0.41% lower policy index crediting rate).

Can you imagine the client buying something, knowing that a slight reduction in S&P 500 performance (a mere 0.41% lesser annual return) would completely blow up their premium financing program?

No one in their right mind would buy into this strategy if the risks were transparently articulated to them.

On top of that, what if the borrowing interest rate increased more than 0.03% per year? If borrowing interest rates increased more rapidly than this amount, the accrued loan debt would be even greater, compounding year after year, and the loan payoff would be substantially greater than \$9,445,921.

Setting It Up Properly From The Beginning

There were so many things wrong with the Interest Accrual program we looked at earlier in this chapter.

The client only borrowed \$7,211,690 in premium, but their accrued loan balance was \$9,445,921 by the 14th year, and that assumed a mere 0.03% annual borrowing interest rate increase, which is so understated and misleading, it's embarrassing.

If they were to pay the interest out-of-pocket as they would have in a *First-Dollar Financing* arrangement, the loan payoff would only be \$7,211,690 (**line D**).

This would be done in the form of a Withdrawal Up To Basis, not a Participating Policy Loan.

Under this arrangement, despite a 0.00% *Policy Index Credit* in the 14th year (**line F**), the *End Of Year 14 Net Cash Surrender Value* would be \$2,860,701 (**line L**).

| | YEAR 14: 0.00% INDEX CREDIT (WITHDRAWAL TO PAY OFF | F PF LOAN) |
|---|--|--------------|
| Α | Start Of Year 14: Policy Cash Surrender Value: | \$10,488,641 |
| В | Policy Charges: | -\$416,250 |
| С | Policy Cash Surrender Value After Charges: | \$10,072,391 |
| D | Withdrawal: | -\$7,211,690 |
| Ε | End Of Year 14 Policy Accumulated Value: | \$2,860,701 |
| F | Illustrated Policy Index Credit: | 0.00% |
| G | Multiplier Bonus: | 1.00 |
| Н | Cash Value Credit With Multiplier Bonus: | 0.00% |
| | | |
| I | End Of Year 14 Policy Accumulated Value: | \$2,860,701 |
| J | Cash Value Credit With Multiplier Bonus: | 0.00% |
| K | Policy Interest Credit: | \$0 |
| L | End Of Year 14: Net Cash Surrender Value: | \$2,860,701 |

If the client were to use our proprietary *Leveraged Index Arbitrage*TM program where they would pay the first year premium out-of-pocket, they would be in an even better financial position, with no outside collateral requirements and no personal guarantor requirements either.

We can obviously facilitate both the *Leveraged Index* $Arbitrage^{TM}$ program and the *First-Dollar Financing* arrangement as illustrated above. It's completely up the client's preference.

We believe in transparently illustrating both scenarios. It boils down to the two hallmarks of Lionsmark Capital:

- 1. Transparency.
- 2. Integrity.

In addition to the lack of transparency in premium financing, there is an equally opaque view of how the IUL cash value accumulation actually works.

For example, here are some questions most agents do not know the answers to:

- 1. When are the policy charges actually taken out?
- 2. Are the premium load charges applied differently than the standard charges?
- 3. Are the multiplier charges applied to:
 - a. The Beginning Of Year Accumulated Value?
 - b. The End Of Year Accumulated Value?
 - c. The Average Monthly Accumulated Value?
- 4. How adverse is the multiplier charge when the base index credit is 0.00%?
- 5. Is the index credit applied before or after the charges?
- 6. Is the index credit applied to:
 - a. The Beginning Of Year Accumulated Value?
 - b. The End Of Year Accumulated Value?
 - c. The Average Monthly Accumulated Value?
- 7. What is a *Retention Bonus* and how is it applied to the standard index credit?

These questions are incredibly important when it comes to premium financing, and sadly, most premium financing experts cannot answer them, nor can they model how these factors affect policy performance during volatile index return years. In this next chapter, I will answer these questions and illustrate the risks and liabilities that come along with these compounded adverse factors.

Chapter 7

Index Credits, Charges & Multipliers

In addition to understanding the relationship between policy index *crediting rates* and premium financing *borrowing rates*, it is equally important to understand the relationship between:

- 1. Policy Charges (especially Multiplier Charges), and
- 2. Policy Index Credits (and *Multiplier Bonuses*)

The policy charges are calculated based on the policy's *Accumulated Value*, whereas the policy index credits are typically based on the *Average Monthly Accumulated Value*.

It is vitally important to understand the chronological order in which the policy charges and credits are applied to the policy cash value because if not properly modeled, and a credit is applied before a charge is deducted, the accumulated value would be projected much higher than reality.

In this chapter, we will discuss the sequence of charges and credits, as well as how they are calculated.

Policy Charges

There are several potential charges applied to the *Accumulated Value* of an IUL:

- ✓ Premium Load Charges
- ✓ Administrative & Rider Charges
- ✓ Non-Guaranteed Coverage Charges
- ✓ Non-Guaranteed Cost of Insurance Charges
- ✓ Index Multiplier Charges (depending on the product & crediting choice)

Premium Load Charges are typically taken out of the premiums paid into the policy at the beginning of the index segment.

The remaining policy charges (including the *Multiplier Charges*) are typically calculated, charged and deducted monthly.

If the IUL product has a *Multiplier Charge*, it is typically calculated as a percentage of the *Accumulated Value* each month of the index segment:

- 1. After any new premiums have been added,
- 2. After all of the annual *Premium Load Charges* have been deducted,
- 3. Before other monthly charges are deducted.

For example, if the annualized *Multiplier Charge* was 1.20%, and the *Accumulated Value* (as defined above) in the first month of a given segment was \$10,000,000, the total annual *Multiplier Charge* in that given month would be $1/12^{\text{th}}$ of the annualized 1.20% charge (0.10%) and applied to that \$10,000,000 *Accumulated Value* in *Month I* of that segment.

\$10,000,000 Accumulated Value In A Given Month
x 0.10% Multiplier Charge (%) In A Given Month

\$10,000 Multiplier Charge (\$) In A Given Month

After the *Multiplier Charge* is calculated, charged and deducted in each month, the remaining monthly charges would be deducted. The *Annualized Multiplier Charge* of 1.20% would be slightly less than \$120,000 in annual charges.

The reason it would be less than \$120,000 is that the remaining monthly charges would be deducted each month, making the *Accumulated Value* less than the previous month.

For example, if the *Accumulated Value* was \$10,000,000 at the beginning of *Month 1* of the segment, and the monthly charges in *Month 1* were \$40,000, the *Accumulated Value* at the beginning of *Month 2* would be \$9,960,000. The monthly *Multiplier Charge* of 0.10% would be \$9,960 in *Month 2* of the segment (versus \$10,000,000 in *Month 1* of the segment).

By Month 12 in this segment, eleven months of charges would have been deducted, making the Accumulated Value significantly less than the Accumulated Value in Month 1.

Base Policy Index Credits

The *Base Policy Index Credit* credited to an IUL's cash value is based on the crediting method of the IUL policy, which may vary from product to product, carrier to carrier.

For example, in a policy with a 0.00% floor and a 9.25% cap (assuming an S&P 500 correlated index and an annual point-to-point crediting segment), if the S&P 500 produced a 10.00% gain in a given year (not including dividends), the policy would receive a gross 9.25% *Base Policy Index Credit* (hitting the IUL's cap).

Bonus Policy Index Credits

Some IULs have *Bonus Policy Index Credits*, including:

- ✓ Multiplier Bonus Credits, and/or
- ✓ Persistency Bonus Credits

The *Multiplier Bonus* is a figure multiplied by the *Base Policy Index Credit*. In other words, if the *Multiplier Bonus* was 2.00, and the *Base Policy Index Credit* is 9.25%, the *After-Multiplier Index Credit* would be 18.50%.

| 18.50% | After-Multiplier Index Credit |
|--------|-------------------------------|
| x 2.00 | Multiplier Bonus |
| 9.25% | Base Policy Index Credit |

In addition, if the IUL product has a *Persistency Bonus* (in the form of a percentage), it would be added to the *After-Multiplier Index Credit* (assuming there was a multiplier credit).

For example, if the *Persistency Bonus* was 0.50%, it would be added to the 18.50% *After-Multiplier Index Credit*, equaling a 19.00% *Total Index Credit*

| 19.00% | Total Index Credit |
|---------|-------------------------------|
| + 0.50% | Persistency Bonus |
| 18.50% | After-Multiplier Index Credit |

Some IULs do not have a *Multiplier Bonus*, but they have a *Persistency Bonus*.

Some IULs do not have a *Persistency Bonus*, but they have a *Multiplier Bonus*.

Some IULs that have a *Multiplier Bonus* do not have an additional charge for such bonus, and some do. IULs with a *Multiplier Charge* will have a much higher *Multiplier Bonus* than those that do not have a *Multiplier Charge*.

Additionally, IULs with higher *Multiplier Charges* will typically have higher *Multiplier Bonuses*.

IULs with higher *Multiplier Bonuses/Charges* incur substantially greater risks and rewards. The risk occurs when the policy receives several consecutive years of 0.00% index credits.

In such years, there is no *Multiplier Bonus* credited, because even if the *Multiplier Bonus* was 2.00, the end result is still a 0.00% *After-Multiplier Index Credit*.

0.00% Base Policy Index Credit x 2.00 Multiplier Bonus

0.00% After-Multiplier Index Credit

If the *Annualized Multiplier Charge* was 1.20% of the *Accumulated Value* in this year, such charge would still be taken out of the policy's *Cash Value*, despite the zero benefit of the *Multiplier Bonus* in this given year.

The argument in favor of IULs with high *Multiplier Bonuses* is that despite the subsequent high charges, the *Multiplier Bonus* should overcompensate for the charges, producing a greater cash value accumulation over time.

They *should*, but do they really?

Risks vs. Rewards of Multiplier Crediting Methods

The idea of paying for a *Multiplier Bonus* credit can be very appealing to a client that is looking to maximize their potential gains in regards to cash value accumulation.

Many advisors (and carriers) will debate over the *benefits* versus the *risks* of *Multiplier Bonus* components within IUL crediting methods. As you will see later in this chapter, *Multiplier*

Charges can often times be hundreds of thousands (if not millions) of dollars in a single given year. This can look very intimidating.

Of course, the justification of such high *charges* is that they are not truly *charges* per se, but rather an increase in budget for the carrier to purchase additional options packages, which is what buys the client the *Multiplier Bonus*.

Essentially, it is the idea of doubling down on the IUL's crediting method.

Categorically speaking, it is not a *charge*, but rather a *reinvestment* in the IUL's index crediting strategy, dramatically boosting the potential of the index return's upside.

These types of philosophical debates, though entertaining, are meaningless without volatility stress-testing and risk potential modeling (to uncover the indisputable mathematical truth), which we will do in the upcoming pages of this book.

To evaluate the *Risks vs. Rewards* of *Multiplier Bonuses*, we have modeled the exact same IUL product (from the same carrier) with two different crediting methods:

- 1. A very aggressive *Multiplier Bonus* with a very high *Multiplier Charge*, *versus*
- 2. No Multiplier Bonus and no Multiplier Charge.

We modeled both IUL product designs during two very different 40-year S&P 500 historical lookback periods:

- 1. The Last 40 Years (1979-2018)
- 2. The Sandwich (2000-2009 + 1999-2018 + 2000-2009)

Last 40 Years (1978-2018)

In the *Last 40 Years (1978-2018)*, we specifically looked at *Policy Years 22-24* (2000-2002) when the policy would have received 0.00% index credits three years in a row.

During this time, the *Multiplier Bonus* would not have positively impacted the index credit (a 0.00% *Base Policy Index Credit* multiplied by any *Multiplier Bonus* still equals 0.00%).

In the chart below, both the IUL with the *Multiplier Bonus* and the IUL without any *Multiplier Bonus* would receive a 0.00% *Index Credit*.

| 2000-2003 (Policy Years 22-25) | S&P 500 RETURNS NO DIVIDENDS | INDEX CREDIT WITH MULTIPLIER | INDEX CREDIT NO MULTIPLIER |
|--------------------------------|---------------------------------|------------------------------|-------------------------------|
| 2000 (Policy Year 22): | -10.14% | 0.00% | 0.00% |
| 2001 (Policy Year 23): | -13.04% | 0.00% | 0.00% |
| 2002 (Policy Year 24): | -23.37% | 0.00% | 0.00% |

In *Policy Year 24* below, there are \$560,752 in *Total Charges* in the IUL with the *Multiplier Bonus*, compared to only \$36,185 in the IUL without the *Multiplier Bonus*.

| 2002 (Policy Year 24): | WITH MULTIPLIER | NO Multiplier |
|-------------------------------|--------------------|------------------|
| BOY Accumulated Value: | \$13,450,446 | \$8,840,339 |
| Multiplier Charges (%): | 3.90% | 0.00% |
| Multiplier Charges (\$): | -\$524,567 | \$0 |
| Standard Policy Charges (\$): | -\$36,185 | -\$36,185 |
| Total Policy Charges (\$): | -\$560,752 | -\$36,185 |

This massive difference in *Total Policy Charges* may shatter some people's confidence in IULs with *Multiplier Charges*, especially when they consider the fact that in a year where the *Base Policy Index Credit* is 0.00%, the cash value would still take a \$560,752 hit in this year (in the form of *Total Policy Charges*).

In this particular year during this 40-year lookback period, the S&P 500 produced a negative return (-23.37%). In such year, the policy would have produced a 0.00% *Total Index Credit*.

| 2002 (Policy Year 24): | WITH MULTIPLIER | NO Multiplier |
|------------------------------------|--------------------|------------------|
| S&P 500 Return (no dividends): | -23.37% | -23.37% |
| Base Policy Index Credit: | 0.00% | 0.00% |
| Multiplier Credit: | 1.90 | 1.00 |
| Total Index Credit (%): | 0.00% | 0.00% |
| Average Monthly Accumulated Value: | \$13,170,070 | \$8,822,247 |
| Total Index Credit (\$): | \$0 | \$0 |

In this particular lookback period, this negative return was the third of three consecutive negative return years (-10.14% in 2000, -13.04% in 2001, and -23.37% in 2002). This would result in three consecutive years earning 0.00% index credits

The IUL with the *Multiplier Bonus* also incurs substantial policy charges in *Policy Years 22-24* (\$2,225,877 vs. \$158,793 in the IUL with no *Multiplier Bonus*).

| 1979-1999 (Policy Years 1-21) | WITH Multiplier | NO Multiplier |
|---------------------------------|--------------------|------------------|
| 2000 Charges (Policy Year 22): | -\$929,554 | -\$67,966 |
| 2001 Charges (Policy Year 23): | -\$735,571 | -\$54,642 |
| 2002 Charges (Policy Year 24): | -\$560,752 | -\$36,185 |
| Total Policy Charges (3 Years): | -\$2,225,877 | -\$158,793 |

Despite the substantially higher policy charges in this scenario, the IUL with the *Multiplier Bonus* would have accumulated more cash value in the first 23 years than the IUL without the *Multiplier Bonus* due to strong S&P 500 returns during these first 23 years of this particular lookback period (1979-2001).

As we see in the next chart, despite the high *Multiplier Charges* and 0.00% *Total Index Credits* in *Policy Years 22-24*, the IUL with the *Multiplier Bonus* has a substantially greater *End-Of-Year Accumulated Value* than the IUL without the *Multiplier Bonus* in *Policy Year 24* (\$12,889,694 vs. \$8,804,154 in the IUL with no *Multiplier Bonus*).

| 2002 (Policy Year 24): | WITH Multiplier | NO Multiplier |
|----------------------------|--------------------|------------------|
| BOY Accumulated Value: | \$13,450,446 | \$8,840,339 |
| Total Policy Charges (\$): | -\$560,752 | -\$36,185 |
| Total Index Credits (\$): | \$0 | \$0 |
| EOY Accumulated Value: | \$12,889,694 | \$8,804,154 |

As attractive as the *Multiplier Bonus* crediting method may appear in this particular backtested period, we must also evaluate its affect during a time when the S&P 500 does not perform as well

These volatility backtesting and stress-testing capabilities of our proprietary software is something unique to Lionsmark Capital.

It is imperative to see what would actually happen in underperforming years, especially with volatility and a poor sequence of returns.

Simply running a low static IRR in the carrier illustration software does not address the risk of several consecutive 0.00% index crediting years during high *Multiplier Charge* years.

The Sandwich Lookback Period

The Sandwich Lookback period is an ideal 40-year period to evaluate the *Multiplier Bonus* crediting method due to its terrible sequence of returns.

Years 1-10: 2000-2009 (S&P 500 CAGR: - 0.99%)
Years 11-30: 1999-2018 (S&P 500 CAGR: 5.59%)
Years 31-40: 2000-2009 (S&P 500 CAGR: - 0.99%)

The *Compounded Annual Growth Rate (CAGR)* of this particular 40-year constructed period was only 2.25% (including S&P 500 dividends). Without dividends, the *CAGR* of this period was 0.41%.

In such time period, the *Multiplier Charges* are less than the 40-year lookback period due to smaller policy *Accumulated Values*, however such charges during this time period are still quite substantial.

In *Policy Year 24*, the IUL with the *Multiplier Bonus* still has \$244,158 in *Total Charges* (compared to the IUL without the *Multiplier Bonus*, which only incurred \$36,185 in *Total Charges*).

| 2012 (Policy Year 24): | WITH MULTIPLIER | NO Multiplier |
|-------------------------------|--------------------|------------------|
| BOY Accumulated Value: | \$5,332,639 | \$6,239,132 |
| Multiplier Charges (%): | 3.90% | 0.00% |
| Multiplier Charges (\$): | -\$207,973 | \$0 |
| Standard Policy Charges (\$): | -\$36,185 | -\$36,185 |
| Total Policy Charges (\$): | -\$244,158 | -\$36,185 |

Due to the *Multiplier Charges* being so high, and *The Sandwich* period producing nine 0.00% policy index credits in the first twenty years of the sequence, the *Beginning-Of-Year (BOY) Accumulated Value* is less in the IUL with the *Multiplier Bonus* in *Policy Year 24*.

A *BOY Accumulated Value* of the IUL with the *Multiplier Bonus* is \$5,332,639 compared to \$6,239,132 in the IUL without the *Multiplier Bonus*.

In the next policy year however, the S&P 500 had a positive return, hence the *Multiplier Bonus* would be applied to the *Base Policy Index Credit*.

I will illustrate the positive affect of the *Multiplier Bonus* when the *Base Index Credit* is positive on the next page.

Calculating The Index Credit

The *Total Index Credit*, though applied at the end of the segment, is not necessarily applied to the *End-Of-Year (EOY) Accumulated Value*. With most carriers, the index credit is applied to the *Average Monthly Accumulated Value*.

Remember, the *Premium Load Charge* is deducted immediately upon premium payments, however the remaining charges are typically deducted monthly, hence the *Average Monthly Accumulated Value* will be higher than the *EOY Accumulated Value*.

Though the exact monthly charges are not calculated by dividing the annual charges by 12 months, the outcome is very similar. For an approximation of calculating the *Average Monthly Accumulated Value*, one could simply add in the new premium in that year, deduct all the *Premium Load Charges*, then deduct 6/12 of the remaining annual charges from the previous segment's *EOY Accumulated Value* after the previous segment's index credit has credited.

The *Total Index Credit* of the current segment would be applied to the current segment's *Average Monthly Accumulated Value* at the end of the current segment.

In *The Sandwich* lookback period, *Policy Year 24* is the calendar year 2012, during which time the S&P 500 produced a 13.29% positive return.

In this year, the *Base Policy Index Credit* would be 9.25% (hitting the IUL's cap), but with a *Multiplier Bonus* of 1.90, the *After-Multiplier Index Credit* would be 17.58%

| 17.58% | After-Multiplier Index Credit |
|--------|-------------------------------|
| x 1.90 | Multiplier Bonus |
| 9.25% | Base Policy Index Credit |

During this index segment, the IUL with the *Multiplier Bonus* would receive a \$915,756 *Total Index Credit* compared to only \$575,446 in the IUL without the *Multiplier Bonus*.

| 2012 (Policy Year 24): | WITH MULTIPLIER | NO Multiplier |
|------------------------------------|--------------------|------------------|
| S&P 500 Return (no dividends): | 13.29% | 13.29% |
| Base Policy Index Credit: | 9.25% | 9.25% |
| Multiplier Credit: | 1.90 | 1.00 |
| Total Index Credit (%): | 17.58% | 9.25% |
| Average Monthly Accumulated Value: | \$5,210,560 | \$6,221,039 |
| Total Index Credit (\$): | \$915,756 | \$575,446 |

Despite the larger *Total Index Credit* in this particular year, the IUL without the *Multiplier Bonus* has a higher *Accumulated Value* by the end of *Policy Year 24* (during *The Sandwich* backtested period).

This is due to the combination of high *Multiplier Charges* and 0.00% index credits in 9 out of the first 20 years of *The Sandwich* backtested period.

No *Multiplier Bonus* was realized in any of these nine years, because 1.90 times 0.00% is still 0.00%.

As we see in the next chart, the IUL with the *Multiplier Bonus* has an *End-Of-Year Accumulated Value* 11.42% less than the IUL without the *Multiplier Bonus/Charge* (\$6,004,237 vs. \$6,778,393).

| 2012 (Policy Year 24): | WITH MULTIPLIER | NO MULTIPLIER |
|----------------------------|--------------------|------------------|
| BOY Accumulated Value: | \$5,332,639 | \$6,239,132 |
| Total Policy Charges (\$): | -\$244,158 | -\$36,185 |
| Total Index Credits (\$): | \$915,756 | \$575,446 |
| EOY Accumulated Value: | \$6,004,237 | \$6,778,393 |

However if we revisit the 40-Year Lookback, at the end of the 24th Policy Year, the IUL with the Multiplier Bonus has an End-Of-Year Accumulated Value 46.40% greater than the IUL without the Multiplier Bonus (\$12,889,694 vs. \$8,804,154).

| 2002 (Policy Year 24): | WITH MULTIPLIER | NO MULTIPLIER |
|----------------------------|--------------------|------------------|
| BOY Accumulated Value: | \$13,450,446 | \$8,840,339 |
| Total Policy Charges (\$): | -\$560,752 | -\$36,185 |
| Total Index Credits (\$): | \$0 | \$0 |
| EOY Accumulated Value: | \$12,889,694 | \$8,804,154 |

When evaluating whether or not an IUL's *Multiplier Bonus* crediting method is mathematically advantageous to the client, it is important to backtest and stress-test the product with volatility and a poor sequence of returns, which most premium financing programs do not have the sophistication to model.

In the backtested modeling we just discussed, with the 2.25% S&P 500 Compounded Annual Growth Rate (CAGR) environment of The Sandwich (2000-2009 + 1999-2018 + 2000-2009), the IUL with the Multiplier Bonus produced an 11.42% worse Accumulated Value by the end of Policy Year 24 than the IUL without the Multiplier Bonus

However in the 11.56% S&P 500 Compounded Annual Growth Rate environment of the 40-Year Lookback (1979-2018), the IUL with the *Multiplier Bonus* produced a 46.40% better *Accumulated Value* than the IUL without the *Multiplier Bonus* by the end of *Policy Year 24*.

The fear that IUL products with aggressive *Multiplier Bonuses* (that incur high *Multiplier Charges*) will be devastated by too many underperforming index years is a legitimate fear. However we just finished modeling *The Sandwich* 40-year period

in which the market environment imposed major adversities in S&P 500 performance including a poor sequence of returns wherein:

- 1. The index credited 0.00% for the first 3 policy years.
- 2. The index credited 0.00% in 4 of the first 10 policy years.
- 3. The index credited 0.00% in 9 of the first 20 policy years.

The IUL with the *Multiplier Bonus* created a 46.40% better outcome in the *40-Year Lookback* period than the IUL without the *Multiplier Bonus*, and an 11.42% worse outcome in *The Sandwich* 40-year period.

I suppose one could argue that the downside potential of the IUL with the *Multiplier Bonus* is minimal (11.42% worse performance) compared to a much greater upside potential (46.40% better performance).

Under this philosophy, with these two very different S&P 500 performance scenarios, the *Multiplier Charge* appears to be worth the upside of the *Multiplier Bonus*.

However, for a more conservative client with a less optimistic view of future S&P 500 performance, an IUL without heavy *Multiplier Charges* may be a more appropriate fit.

Each client and advisor has their own risk tolerance and philosophy when it comes to the *Probability Of Risk* and the *Consequence Of Risk*, however from a stress-testing and backtesting standpoint (using the last 40 years, as well as *The Sandwich* 40-year constructed period), it is important to work with a premium financing firm that can actually model such comparisons.

Without the software and mathematical capabilities to model these variables in product design and financing design, the client does not truly understand the actual mathematical liabilities incurred by the strategy they are investing in.

Perhaps even worse, the advisor does not truly understand what they are selling.

This is a scary fact to ponder, but a very realistic problem within the premium financing industry as a whole.

Properly Designed Premium Financing Programs

When designed properly – without the use static index returns and abnormally low borrowing interest rate environments – premium financing is a cash flow-efficient strategy to purchase life insurance.

It allows the client to purchase the same amount of life insurance death benefit for substantially less cash outlay, compared to the cost of paying the premiums out-of-pocket without leveraging a lender's capital.

But in addition to the death benefit, premium financing can also be used as a strategy to accumulate a client's wealth, building an asset class that:

- 1. Receives tax-deferred treatment on gains
- 2. Offers protection against down markets
- 3. Is not subject to Required Minimum Distributions (RMDs)
- 4. Receives tax-free treatment upon liquidation.

In the next chapter, we will discuss how Premium Financing can be used for wealth accumulation.

DARREN SUGIYAMA & JEFF FAINE

Chapter 8 Wealth Accumulation

Buying life insurance solely for the *death benefit* is one of the least inspiring purchases a human being can make.

Yes, it is the responsible thing to do for your family, whether the intent of the *death benefit* payout is to be used to help with living expenses, or if it is to be used to pay the estate tax liability upon the insured's passing.

But it's an expense – an expense that the insured does not get to personally enjoy.

I'll use a brief analogy to illustrate the emotional component of this buying experience.

I live in an equestrian community. Many of my neighbors own horses, along with several different types of farm animals including cows, goats, sheep and chickens.

As a result, we have a lot of *critters* and *pests* that need to be dealt with, so we hire a pest control company to service our property twice a month.

I hate paying for this.

It is necessary, but it is a pure *expense* that I reap zero enjoyment from. Sure, you could argue that I get to enjoy a semipest free property despite our equestrian environment (which is a benefit to me), but I still despise making that monthly payment.

This is the way some people feel about their life insurance expense.

The difference is that a life insurance policy that accumulates cash value over time is *not* just an expense. In fact, it's an asset – a liquid asset with tax advantaged treatment – and in some cases, can be enjoyed by the insured during their lifetime.

But *how good* of an asset is a premium financed life insurance policy?

I was recently watching an interview with Tony Robbins, and he was talking about a conversation he had with Ray Dalio.

Ray Dalio founded investment firm *Bridgwater Associates*, one of the largest hedge funds in the world. To put the size of Dalio's firm into context, a *large* hedge fund manages \$15 billion.

Bridgewater Associates currently manages \$160 billion.²

Bridgewater's clientele includes approximately 350 of the largest and most sophisticated global institutional clients including public and corporate pension funds, university endowments, charitable foundations, sovereign wealth funds and central banks.

Ten years ago, you had to have a \$5 billion net worth and a minimum of \$100 million in liquid investable assets for him to even consider allowing you to join his fund.

Today, he has closed his fund to all new money, regardless of who you are or how much you can invest.

In 2012, Dalio was recognized by *Time Magazine* as one of the 100 most influential people in the world, and in January 2019, *Bloomberg* ranked Dalio as the 79th wealthiest person in the world.³

As you can see, Ray Dalio is one of the savviest investor minds in the world.

In his conversation, Tony Robbins asked Ray Dalio about his investment strategy, and after much prodding, Dalio shared some of his *secret sauce* with Robbins.

The first thing Dalio said was, "I use leverage."

The second thing Dalio shared was the importance of backtesting over a long period of time in order to quantify whether an investment strategy held water or not.

Hmm... sound familiar?

Robbins backtested Dalio's strategy over a period of 75 years. Here's what Robbins' backtest discovered.

85% of the time, the strategy produced a positive return.

During the 15% of the time the strategy produced a negative return, the maximum loss was only 3.90%.

The average loss was only 1.70%.

The average gain was 10.00%.

Take the basic framework of Dalio's strategy, and it begins to sound eerily similar to our proprietary *Leveraged Index* $Arbitrage^{TM}$ program.

Here's what I mean

If we look at the last 40 years of the S&P 500 (not including dividends), between the years 1979-2018, nine of those forty years produced a negative return.⁴

In an IUL with a 0.00% floor, 22.50% of the time the client would receive a 0.00% gain with no losses (outside of the total policy charges).

During the remaining 77.50% of this 40-year run, the average S&P 500 gain was 16.09%.

If a 10.00% cap were to be applied, the average gain in the *up years* would have been 8.39%. Raise that cap to 11.00% and the average gain in the *up years* would have been 9.10%.

If the upside were uncapped with a 5-point spread, the average gain in the *up years* would have been 11.59%.

During this 40-year backtest (beginning with the end-of-year prior to the 40-year run), the *Compounded Annual Growth Rate (CAGR)* including all of the ups and downs was 8.28%.⁵

Assuming a 10.00% cap on the upside, the CAGR was 6.25%. Raise the cap to 11.00%, and the CAGR was 6.77%.

Assuming an uncapped upside crediting method with a 5-point spread, the *CAGR* was 8.38%.

These numbers do not take into consideration the power of leverage nor the life insurance policy costs, however you must admit, the general principles echo Dalio's strategy.

Leveraged Index ArbitrageTM Case Study

As an example, let's look at a case study of a 55-year old male with a health rating of *Preferred Non-Tobacco*.

The net death benefit starts off at \$10,000,000.

In this case study on the next page, we used a first-year premium of \$500,000 paid out-of-pocket, then annual premiums of \$679,923 borrowed in years 2-7.

Borrowing Rates in Case Study

The projected borrowing interest rate is illustrated assuming the *1-Year U.S. Treasury Daily Yield Curve (USTDYC)* rate is:

Years 1-10: Increasing 8.00% per year

Years 11-20: Decreasing 8.00% per year

Years 21-30: Increasing 8.00% per year

Years 31-40: Decreasing 8.00% per year

The above borrowing rate volatility is intentionally more adverse than most premium financing illustrations.

Remember, between 1998-2018, the *1-Year USTDYC* has decreased at a *Compounded Annual Rate* of 5.31%, so an annual volatility rate of 8.00% is more adverse than historical data reveals.

The starting 1-Year USTDYC was 2.34% (as of May 20, 2019 when this illustration was run).

The lender spread is 2.50% for the first year of funds borrowed, then decreases to 2.25% once borrowed premiums have been seasoned in the policy for one year.

Client Outlay

The client pays the \$500,000 first-year premium out-of-pocket, then pays interest payments out-of-pocket in years 2-15.

We modeled a premium financing loan payoff in year 16 using a \$4,079,538 withdrawal under basis (not a policy loan).

Due to the LTV in the Leveraged Index ArbitrageTM program, the client is not required to post any outside collateral.

| # YEAR | AGE | PREMIUMS PAID | PREMIUMS BORROWED | CUMULATIVE PF LOAN BALANCE | FINANCING INTEREST RATE | INTEREST DUE | COLLATERAL REQUIRED |
|-----------|-----|------------------|----------------------|-------------------------------|----------------------------|-----------------|------------------------|
| 1 | 55 | \$500,000 | \$0 | \$0 | 0.00% | \$0 | \$0 |
| 2 | 56 | \$0 | \$679,923 | \$679,923 | 4.96% | \$33,753 | \$0 |
| 3 | 57 | \$0 | \$679,923 | \$1,359,846 | 4.97% | \$67,586 | \$0 |
| 4 | 58 | \$0 | \$679,923 | \$2,039,769 | 5.07% | \$103,340 | \$0 |
| 5 | 59 | \$0 | \$679,923 | \$2,719,692 | 5.19% | \$141,166 | \$0 |
| 6 | 60 | \$0 | \$679,923 | \$3,399,615 | 5.33% | \$181,228 | \$0 |
| 7 | 61 | \$0 | \$679,923 | \$4,079,538 | 5.48% | \$223,699 | \$0 |
| 8 | 62 | \$0 | \$0 | \$4,079,538 | 5.61% | \$228,914 | \$0 |
| 9 | 63 | \$0 | \$0 | \$4,079,538 | 5.79% | \$236,195 | \$0 |
| 10 | 64 | \$0 | \$0 | \$4,079,538 | 5.98% | \$243,863 | \$0 |
| 11 | 65 | \$0 | \$0 | \$4,079,538 | 5.78% | \$235,788 | \$0 |
| 12 | 66 | \$0 | \$0 | \$4,079,538 | 5.59% | \$228,142 | \$0 |
| 13 | 67 | \$0 | \$0 | \$4,079,538 | 5.41% | \$220,901 | \$0 |
| 14 | 68 | \$0 | \$0 | \$4,079,538 | 5.25% | \$214,046 | \$0 |
| 15 | 69 | \$0 | \$0 | \$4,079,538 | 5.09% | \$207,554 | \$0 |
| 16 | 70 | \$0 | \$0 | \$4,079,538 | 4.94% | \$201,407 | \$0 |
| 17 | 71 | \$0 | \$0 | \$4,079,538 | 4.79% | \$195,586 | \$0 |
| 18 | 72 | \$0 | \$0 | \$4,079,538 | 4.66% | \$190,074 | \$0 |
| 19 | 73 | \$0 | \$0 | \$4,079,538 | 4.53% | \$184,855 | \$0 |
| 20 | 74 | \$0 | \$0 | \$0 | 4.41% | \$0 | \$0 |
| 21 | 75 | \$0 | \$0 | \$0 | 4.52% | \$0 | \$0 |
| 22 | 76 | \$0 | \$0 | \$0 | 4.65% | \$0 | \$0 |
| 23 | 77 | \$0 | \$0 | \$0 | 4.77% | \$0 | \$0 |
| 24 | 78 | \$0 | \$0 | \$0 | 4.91% | \$0 | \$0 |
| 25 | 79 | \$0 | \$0 | \$0 | 5.05% | \$0 | \$0 |
| 26 | 80 | \$0 | \$0 | \$0 | 5.20% | \$0 | \$0 |
| 27 | 81 | \$0 | \$0 | \$0 | 5.35% | \$0 | \$0 |
| 28 | 82 | \$0 | \$0 | \$0 | 5.52% | \$0 | \$0 |
| 29 | 83 | \$0 | \$0 | \$0 | 5.69% | \$0 | \$0 |
| 30 | 84 | \$0 | \$0 | \$0 | 5.87% | \$0 | \$0 |
| 31 | 85 | \$0 | \$0 | \$0 | 5.68% | \$0 | \$0 |
| 32 | 86 | \$0 | \$0 | \$0 | 5.50% | \$0 | \$0 |
| 33 | 87 | \$0 | \$0 | \$0 | 5.33% | \$0 | \$0 |
| 34 | 88 | \$0 | \$0 | \$0 | 5.16% | \$0 | \$0 |
| 35 | 89 | \$0 | \$0 | \$0 | 5.01% | \$0 | \$0 |
| 36 | 90 | \$0 | \$0 | \$0 | 4.86% | \$0 | \$0 |
| 37 | 91 | \$0 | \$0 | \$0 | 4.72% | \$0 | \$0 |
| 38 | 92 | \$0 | \$0 | \$0 | 4.59% | \$0 | \$0 |
| 39 | 93 | \$0 | \$0 | \$0 | 4.47% | \$0 | \$0 |
| 40 | 94 | \$0 | \$0 | \$0 | 4.35% | \$0 | \$0 |

On the next page, we are modeling the 40-year backtested period between the years 1979-2018 (the last 40 years), showing historical S&P 500 returns (not including dividends) in these corresponding years.

The IUL crediting method we are modeling uses a 0.00% protective floor and a 10.00% cap.

There is no *Multiplier Charge* in this particular IUL product, however there is a small *Multiplier Bonus* of 1.15 that begins in policy year 11. This is a modest *Multiplier Bonus* compared to other IUL products with *Multiplier Bonuses*, however there is no *Multiplier Charge* in this particular product.

This IUL also has a *Persistency Bonus* of 0.50% that begins in policy year 1.

Starting in Policy Year 11, the cash value is eligible to receive both the *Multiplier Bonus* and the *Persistency Bonus*.

As an example, in Policy Year 11 of this lookback scenario on the next page, the S&P 500 produced a 27.25% return. The IUL would have hit the 10.00% cap, making the gross *Base Policy Index Credit* 10.00% in this year.

The 1.15 *Multiplier Bonus* would be applied, making the *After-Multiplier Index Credit* 11.50%.

Then the 0.50% *Persistency Bonus* would be applied, making the *Total Index Credit* 12.00% in that year.

| 12.00% | Total Policy Index Credit: |
|---------|--------------------------------|
| x 0.50% | Persistency Bonus: |
| 11.50% | After-Multiplier Index Credit: |
| x 1.15 | Multiplier Bonus: |
| 10.00% | Base Policy Index Credit: |

Using these historical returns and this index crediting method, after this particular 40-year run, the *Surrender Value Net Of Loans* is \$28,096,197.

The after-policy charges *Surrender Value Net Of Loans* IRR is 6.63% during this modeled time period.

It also has a \$10,000,000 initial death benefit.

This construction is a very conservative set up.

| # YEAR | AGE | CALENDAR YEAR | S&P RETURN NO DIV | GROSS INDEX CREDIT | TOTAL INDEX CREDIT | GROSS POLICY CSV | CUMULATIVE PF LOAN BALANCE | POLICY CSV NET OF LOANS |
|-----------|-----|------------------|-------------------------|--------------------------|--------------------------|------------------------|----------------------------------|-------------------------------|
| 1 | 55 | 1979 | 12.31% | 10.00% | 10.50% | \$320,601 | \$0 | \$320,601 |
| 2 | 56 | 1980 | 25.77% | 10.00% | 10.50% | \$1,045,293 | \$679,923 | \$365,370 |
| 3 | 57 | 1981 | -9.73% | 0.00% | 0.50% | \$1,659,828 | \$1,359,846 | \$299,982 |
| 4 | 58 | 1982 | 14.77% | 10.00% | 10.50% | \$2,518,447 | \$2,039,769 | \$478,678 |
| 5 | 59 | 1983 | 17.26% | 10.00% | 10.50% | \$3,464,708 | \$2,719,692 | \$745,016 |
| 6 | 60 | 1984 | 1.38% | 1.38% | 1.88% | \$4,167,555 | \$3,399,615 | \$767,940 |
| 7 | 61 | 1985 | 26.36% | 10.00% | 10.50% | \$5,303,554 | \$4,079,538 | \$1,224,016 |
| 8 | 62 | 1986 | 14.62% | 10.00% | 10.50% | \$5,847,292 | \$4,079,538 | \$1,767,754 |
| 9 | 63 | 1987 | 2.04% | 2.04% | 2.54% | \$5,975,680 | \$4,079,538 | \$1,896,142 |
| 10 | 64 | 1988 | 12.39% | 10.00% | 10.50% | \$6,581,419 | \$4,079,538 | \$2,501,881 |
| 11 | 65 | 1989 | 27.25% | 10.00% | 12.00% | \$7,340,088 | \$4,079,538 | \$3,260,550 |
| 12 | 66 | 1990 | -6.56% | 0.00% | 0.50% | \$7,344,967 | \$4,079,538 | \$3,265,429 |
| 13 | 67 | 1991 | 26.30% | 10.00% | 12.00% | \$8,190,353 | \$4,079,538 | \$4,110,815 |
| 14 | 68 | 1992 | 4.48% | 4.48% | 5.65% | \$8,616,337 | \$4,079,538 | \$4,536,799 |
| 15 | 69 | 1993 | 7.07% | 7.07% | 8.63% | \$9,320,839 | \$4,079,538 | \$5,241,301 |
| 16 | 70 | 1994 | -1.56% | 0.00% | 0.50% | \$5,228,766 | \$4,079,538 | \$5,228,766 |
| 17 | 71 | 1995 | 34.13% | 10.00% | 12.00% | \$5,814,495 | \$4,079,538 | \$5,814,495 |
| 18 | 72 | 1996 | 20.26% | 10.00% | 12.00% | \$6,470,712 | \$4,079,538 | \$6,470,712 |
| 19 | 73 | 1997 | 31.01% | 10.00% | 12.00% | \$7,207,353 | \$4,079,538 | \$7,207,353 |
| 20 | 74 | 1998 | 26.67% | 10.00% | 12.00% | \$8,036,250 | \$0 | \$8,036,250 |
| 21 | 75 | 1999 | 19.53% | 10.00% | 12.00% | \$8,971,596 | \$0 | \$8,971,596 |
| 22 | 76 | 2000 | -10.14% | 0.00% | 0.50% | \$8,999,694 | \$0 | \$8,999,694 |
| 23 | 77 | 2001 | -13.04% | 0.00% | 0.50% | \$9,031,852 | \$0 | \$9,031,852 |
| 24 | 78 | 2002 | -23.37% | 0.00% | 0.50% | \$9,060,972 | \$0 | \$9,060,972 |
| 25 | 79 | 2003 | 26.38% | 10.00% | 12.00% | \$10,127,099 | \$0 | \$10,127,099 |
| 26 | 80 | 2004 | 8.99% | 8.99% | 10.84% | \$11,198,375 | \$0 | \$11,198,375 |
| 27 | 81 | 2005 | 3.00% | 3.00% | 3.95% | \$11,609,131 | \$0 | \$11,609,131 |
| 28 | 82 | 2006 | 13.60% | 10.00% | 12.00% | \$12,961,501 | \$0 | \$12,961,501 |
| 29 | 83 | 2007 | 3.52% | 3.52% | 4.55% | \$13,502,194 | \$0 | \$13,502,194 |
| 30 | 84 | 2008 | -38.49% | 0.00% | 0.50% | \$13,510,261 | \$0 | \$13,510,261 |
| 31 | 85 | 2009 | 23.65% | 10.00% | 12.00% | \$15,052,479 | \$0 | \$15,052,479 |
| 32 | 86 | 2010 | 12.63% | 10.00% | 12.00% | \$16,760,676 | \$0 | \$16,760,676 |
| 33 | 87 | 2011 | 0.10% | 0.10% | 0.62% | \$16,748,511 | \$0 | \$16,748,511 |
| 34 | 88 | 2012 | 13.29% | 10.00% | 12.00% | \$18,606,821 | \$0 | \$18,606,821 |
| 35 | 89 | 2013 | 29.43% | 10.00% | 12.00% | \$20,651,039 | \$0 | \$20,651,039 |
| 36 | 90 | 2014 | 11.54% | 10.00% | 12.00% | \$22,895,614 | \$0 | \$22,895,614 |
| 37 | 91 | 2015 | -0.73% | 0.00% | 0.50% | \$22,792,240 | \$0 | \$22,792,240 |
| 38 | 92 | 2016 | 9.54% | 9.54% | 11.47% | \$25,196,027 | \$0 | \$25,196,027 |
| 39 | 93 | 2017 | 19.42% | 10.00% | 12.00% | \$28,049,376 | \$0 | \$28,049,376 |
| 40 | 94 | 2018 | -6.24% | 0.00% | 0.50% | \$28,096,197 | \$0 | \$28,096,197 |

In this example we just analyzed, it is undeniable that the premium financed IUL using the *Leveraged Index Arbitrage*TM program is not a mere expense, but a great accumulation strategy.

The question is whether or not this indisputable mathematical outcome is a *good return on investment* from a liquid asset standpoint.

A net 6.63% IRR (after all policy charges) is a great return on investment, in addition to the value of the death benefit.

But the adjective *great* is a subjective term.

The real question is "great compared to what?"

Whenever we design on a client's life insurance portfolio, we illustrate all viable options, including non-financed options as well as financed options.

Our software also has the ability to model the financed life insurance policy's *Cash Value Accumulation* compared to a hypothetical *Managed Investment Account*.

We back-test the same 40-year runs that we use in stress-testing our premium financing programs to show the difference in *Cash Value Accumulation* compared to the *After-Tax Investment Account Growth*.

We model the same outlay in our premium financed Leveraged Index $Arbitrage^{TM}$ program (the first year premium, then interest payments) being invested in this hypothetical Managed Investment Account.

We will have the client chose an equity/bond ratio (ie: 60/40), input their adjusted gross income, marital status, state of residence, and their age.

We will input the current State and Federal tax brackets, calculating the short-term capital and long-term capital gains tax rates.

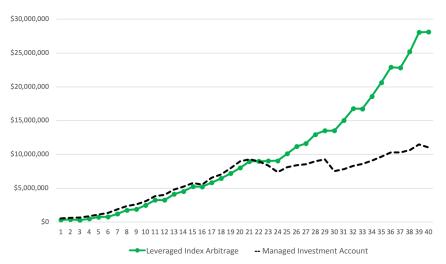
We will also ask what percentage of their equities they would like to see taxed at short-term versus long-term capital gains tax rates.

Lastly, we will input what they are currently being charged in advisor fees in their managed investment account, and calculate an estimation of what they're paying in investment fees, all-in (including the fund manager fees and broker dealer fees). In this model, for equities returns, we model historical S&P 500 returns including dividends, and for bond returns, we model historical 10-year T-Bond returns.

We subtract investment fees from both the equities returns and the bonds returns, then taxes, which calculates the actual net after-fees/after-taxes portfolio return.

The first 40-year backtested period we use is a simple 40-year lookback from the previous year (in this case, 1979-2018), during which time, the S&P 500's *Compounded Annual Growth Rate (CAGR)* was 11.56%.

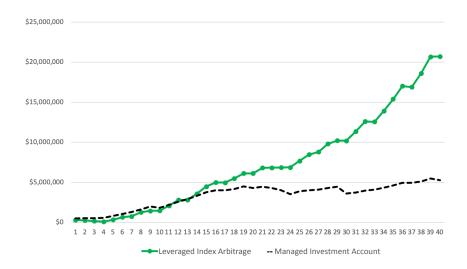
Using the parameters of this hypothetical *Managed Investment Account*, net IRR is calculated to be 3.71%, resulting in a speculated End-Of-Year net account balance of \$11,021,331 versus \$28,096,197 in the *Leveraged Index ArbitrageTM* program.



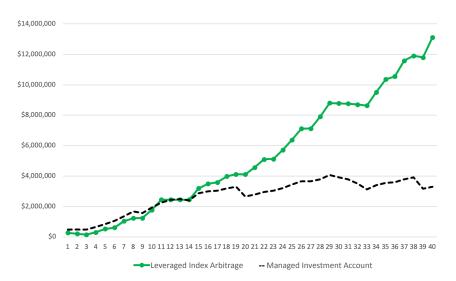
This enormous disparity in accumulation values was not limited to this particular 40-year run.

We also modeled the 20-year period of 1999-2018 and ran this period back-to-back, creating a hypothetical 40-year period where the CAGR would have been 5.59% including dividends. Again, an enormous disparity.

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In addition, we modeled *The Sandwich* 40-year period beginning and ending with 2000-2009, and sandwiched in between are the 20-year period of 1999-2018, creating another 40-year period where the CAGR was 2.25% including dividends.



Of course, we did not include S&P 500 dividends in the *Leveraged Index Arbitrage*TM program because the IUL crediting method does not include index dividends in its calculation of the index credit.

4.25%

As you can see, the difference is astonishing. Below is the summary ledger that illustrates the disparity in results in the three different backtested periods.

| 40-YEAR PERIOD: (1979-2018) | MANAGED INVESTMENT ACCT | LEVERAGED INDEX ARBITRAGE |
|--|----------------------------|------------------------------|
| 40-Year Account Balance: | \$11,021,331 | \$28,096,197 |
| Net 40-Year IRR: | 3.71% | 6.63% |
| 40-YEAR PERIOD: (1999-2018) x2 | MANAGED INVESTMENT ACCT | LEVERAGED INDEX ARBITRAGE |
| 40-Year Account Balance: | \$5,286,186 | \$20,688,712 |
| Net 40-Year IRR: | 1.43% | 5.67% |
| | | |
| 40-YEAR PERIOD: (2000-2009, 1999-2018, 2000-2009) | MANAGED INVESTMENT ACCT | LEVERAGED INDEX ARBITRAGE |

The main reasons for the disparity between the two accumulation models is the *Leveraged Index Arbitrage*TM program has several unique advantages:

-0.02%

Net 40-Year IRR:

1. Leverage.

The client's outlay is the first-year premium and the interest payments, however the lender has front-loaded the premium in years 2-7, so it has the advantage of compound growth (whereas the *Managed Investment Account* does not).

2. 0.00% Protective Floor.

This unique crediting method protects the principal against negative return years.

3. Tax-Advantaged Treatment.

The tax-deferred growth and tax-free liquidation (due to *Title 26 – Internal Revenue Code § 264*) creates major accumulation efficiencies.

In addition to the *apples-to-apples* comparison we just discussed showing the accumulation outcome comparing the *Leveraged Index ArbitrageTM* program to the hypothetical *Managed Investment Account*, we also run comparisons against virtually every other potential life insurance solution so the client can make a mathematically sound decision.

The next chart illustrates a comparison between:

- 1. GUL (death benefit only)
- 2. Non-financed IUL
- 3. Leveraged Index ArbitrageTM

The *Guaranteed UL (GUL)* policy has a \$4,927,040 outlay (premium cost) compared to the \$3,091,940 outlay in the *Non-Financed IUL*.

The Leveraged Index ArbitrageTM program requires a cumulative outlay of \$3,066,175 which is a slightly lower outlay than the GUL, and a slightly lower outlay than the Non-Financed IUL as well.

But look at the disparity in *Net Cash Surrender Value* and *Net Death Benefit* between the *Non-Financed IUL* and the *Leveraged Index Arbitrage*TM program.

| | NON-FINANCED | NON-FINANCED | LEVERAGED INDEX |
|----------------------------|--------------|--------------|-----------------|
| | GUL | IUL | ARBITRAGE |
| TOTAL OUTLAY: | \$4,927,040 | \$3,091,940 | \$3,066,175 |
| INITIAL NET DEATH BENEFIT: | \$10,000,000 | \$10,000,000 | \$10,000,000 |
| YEAR 40 NET DEATH BENEFIT: | \$10,000,000 | \$21,220,282 | \$31,059,932 |

These *Year 40 Death Benefit* amounts in both IULs were calculated using the same carrier, the same IUL product, and the same static gross *Policy Index Credit*.

Obviously, the IULs shown above would also accumulate significant cash value in addition to the death benefit, unlike the GUL.

We also compare our *Leveraged Index Arbitrage*TM program to a traditional *First-Dollar Premium Financing* model from an accumulation standpoint.

Yes, the traditional *First-Dollar Premium Financing* model requires the client to post collateral and sign a personal guaranty, but we always offer this arrangement as an alternative to our proprietary *Leveraged Index Arbitrage*TM program.

This comparison uses the three backtested 40-year periods we used in the *Managed Investment Account* comparison, comparing both financing arrangements.

The Total Outlay is very similar in both programs - \$3,272,223 in the *First-Dollar Financing program*, and \$3,314,432 in the *Leveraged Index Arbitrage*TM program.

| 40-YEAR PERIOD: | FIRST-DOLLAR | LEVERAGED |
|--|--------------------------------|------------------------------|
| (1979-2018) | PREMIUM FINANCING | INDEX ARBITRAGE |
| 40-Year CSV (Net of Loans): | \$25,671,329 | \$28,096,197 |
| Net 40-Year IRR: | 6.58% | 6.63% |
| 40-YEAR PERIOD: | FIRST-DOLLAR | LEVERAGED |
| (1999-2018) x2 | PREMIUM FINANCING | INDEX ARBITRAGE |
| 40-Year CSV (Net of Loans): | \$18,249,322 | \$20,688,712 |
| Net 40-Year IRR: | 5.41% | 5.67% |
| 40-YEAR PERIOD: (2000-2009, 1999-2018, 2000-2009) | FIRST-DOLLAR PREMIUM FINANCING | LEVERAGED INDEX ARBITRAGE |
| 40-Year CSV (Net of Loans): | \$10,638,705 | \$13,119,952 |
| Net 40-Year IRR: | 3.71% | 4.25% |

As we see in the ledger on the next page, the *Cumulative Outlay* is very similar in both models, \$3,272,223 in the traditional *First-Dollar Premium Financing* program and \$3,314,432 in the *Leveraged Index Arbitrage*TM program.

Due to the outlay being virtually the same in both models, yet the performance being substantially better in the *Leveraged Index Arbitrage*TM program, there are only two reasons a client might opt for the *First-Dollar Premium Financing* program, despite being required to post collateral and sign a personal guaranty:

- The client was going to fund the first-year premium with an investment account that had unrealized gains and does not want to incur the immediate capital gains tax by liquidating and moving funds into the policy.
- 2. The client is going to make an emotional decision because they just don't want to write a large check to pay for the first-year premium.
 - Though mathematically less efficient, they may still make an emotional decision instead of a rational

decision and prefer to borrow all the premiums, post collateral and sign a personal guaranty.

The important thing to understand is that at the end of the day, the client is always afforded the luxury of making their own decision once the mathematical facts have been presented.

At Lionsmark Capital, we can facilitate both the traditional *First-Dollar Premium Financing* program and the *Leveraged Index Arbitrage*TM program.

Whether the client wants a more efficient way to purchase a large life insurance policy, or a way to use leverage to exponentially grow a liquid asset, premium financing (done properly) is a mathematically indisputable superior way to achieve both outcomes

I will end by revisiting the concept of the *Probability Of Risk* versus the *Consequence Of Risk*.

I would passionately argue that the *Probability Of Risk* in some of these alternative premium financing arrangements is very high.

Interest Accrual programs – where the client doesn't make the actual interest payments – results in compounding debt. Multiply that arrangement with rising borrowing interest rates, and you have a runaway train that is going to crash. Sprinkle in some poor policy performance in the beginning stages of the policy, and you've got dynamite on that train... with a lit fuse.

But even if you want to argue that the probability of borrowing rate increases while the policy is receiving 0.00% index credits is low, it still doesn't take into consideration the *Consequence Of Risk*.

For example, I have a 9-year old son.

I love my son more than life itself.

I have never been in a car accident with my son in the car, hence the *Probability Of Risk* is very low, statistically.

Despite the *Probability Of Risk* being low, I still make my son wear a seat belt because the *Consequence Of Risk* is very high.

If we were to get into a high-speed car wreck and he wasn't wearing a seat belt, he could die.

That is a risk that I'm not willing to take.

In many of these *Interest Accrual* premium financing programs, if the S&P 500 doesn't perform as illustrated and borrowing rates go through a hyper-inflated increase, the policy cash value will not be able to pay off the larger accrued loan balance

The client will be trapped.

But it can get even worse.

If there is barely enough cash value to pay off the loan, the *Net Amount At Risk* will be too high for the cash value growth to keep pace with the higher *Cost Of Insurance (COI)* charges, and the policy will lapse early.

If this happens, the client will be subject to phantom tax liability because they had to pull out an amount greater than basis in order to pay off the higher compounded/accrued loan debt. If the policy lapses prior to the client's death, they will pay ordinary income taxes on all the cash value gains above basis.

This could result in a 6-figure (or even 7-figure) tax bill.

The *Consequence Of Risk* is too high.

As a trusted advisor to our clients, we believe it is a huge responsibility (and honor) to protect our clients' best interests, which involves transparently disclosing every potential risk that could possibly exist in the future.

It's just the *right* thing to do as an advisor.

It is also the *only* thing to do.

In an industry that has been plagued by greed, a lack of transparency and aggressive sales tactics, at Lionsmark Capital, our mission is to be an industry disruptor.

We have completely dismantled the old model of premium financing and have built a truth-exposing business model analogous to *Wonder Woman's* lasso.

As we have repeatedly articulated, our job is to transparently show our clients the indisputable math – void of opinion and subjectivity – to deliver the clarity they need to make a great decision. Our commitment is to always stand in the truth.

This is the legacy I want to leave behind for my son, Estevan. This is the legacy Jeff wants to leave behind for his sons, Kai and Breck.

NOTES:

- ¹ Macro Trends, "LIBOR Rates 30 Year Historical Chart," www.macrotrends.net, May 26, 2019, https://www.macrotrends.net/1433/historical-libor-rates-chart
- ² Bridgewater Associates, "What We Do," *Bridgewater.com*, April 30, 2019, *https://www.Bridgewater.com*
- ³ Wikipedia, "Ray Dalio," *Wikipedia.com*, April 30, 2019, https://en.wikipedia.org/wiki/Ray Dalio
- ⁴ MoneyChimp, "CAGR of the Stock Market," *MoneyChimp.com*, April 30, 2019, www.moneychimp.com/features/market_cagr.htm
- ⁵ Ryan Furhmann, "CAGR vs. IRR: What's the Difference?" *Investopedia.com*, April 17, 2019, *https://www.investopedia.com/ask/answers/070914/what-are-main-differences-between-compound-annual-growth-rate-cagr-and-internal-rate-return-irr.asp*

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