

# *Enhance Yield, Improve the Balance Sheet and Fund Liabilities With Insurance Company-Owned Life Insurance*



*A Brief, Informative White Paper for Insurance Company Executives  
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## INTRODUCTION

Corporate-Owned Life Insurance has long played an important role in the informal funding of executive benefit programs and other human resource liabilities. Because of its structural flexibility, tax benefits and favorable accounting treatment it is one of the most cost-effective financing tools available to corporate CFOs.

An interesting segment of the COLI market is the insurance industry itself which, like all financial institutions, is searching for yield enhancement in this extraordinary low interest rate environment. Whether or not an insurance carrier sells COLI to other corporations, it may be a good candidate for the purchase of ICOLI (Insurance Company-Owned Life Insurance).

Insurance companies can learn from the history of banks when purchasing ICOLI. In the late 1980s, after the Tax Reform Act of 1986 disallowed banks from using federal funds to buy tax exempt bonds, banks began purchasing Bank-Owned Life Insurance (BOLI) as an alternative. Since that time, guidance has been provided by tax authorities and regulators regarding the purchase of BOLI, including the 2004 “Interagency Statement on the Purchase and Risk Management of Life insurance” by the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of Thrift Supervision. This extensive guidance for BOLI transactions provides a roadmap for the prudent purchase of ICOLI by life and P&C insurance companies.

The following is a brief overview of the potential benefits of an ICOLI purchase, the prevalence of its use, the steps involved in structuring a transaction, and the associated accounting, tax and regulatory issues.

And finally, we will conclude with some observations about current market conditions.

## POTENTIAL BENEFITS

The potential benefits of an ICOLI investment include:

- Enhancement of Yields:

The tax advantages of life insurance provide an opportunity for a step-up in the after-tax yield if the value of those tax advantages is greater than the insurance loads and expenses associated with the insurance contract. If that is the case, an ICOLI investment will generally be immediately accretive to earnings. An additional tax benefit is the ability to reallocate or rebalance the purchaser’s portfolio from time-to-time without triggering tax cost.

- Asset Diversification: ICOLI offers a wide range of variable investment options managed by qualified investment managers. A purchaser can reconstruct its existing asset allocation strategy within ICOLI or consider diversification to alternative investments or asset classes in which it might not invest directly.

- Favorable Accounting and Reporting Treatment:

ICOLI is not treated as an “Invested Asset” for balance sheet reporting under either Statutory or GAAP accounting. For Statutory accounting, it is an admitted asset recorded under “Aggregate Write-ins Other Than Invested Assets.” For GAAP, it is included in “Other Assets.”

Cash value earnings are reported in the income statement as, “Aggregate Write-in for Miscellaneous Income” under Statutory accounting, and as “Other Income” for GAAP.

In addition, cash value earnings are considered a permanent difference requiring no deferred tax impact (assuming it is the purchaser's intent is to hold the policies until the death of the insureds). And finally ICOLI is not reported in Schedule BA. In fact, "cleaning up" Schedule BA has been one of the primary motivations for significant ICOLI purchases.

- *Repositioning of Assets with a Favorable Capital Impact:*

The result the of the accounting treatment described above is a repositioning of assets on the balance sheet from "Invested Assets" to "Other Assets" and a reduction in Risk-Based Capital charges, which are generally lower for ICOLI than for other investments (0% for Life/Health companies, and 5% for P&C companies).

Also, for life insurance carriers, the Asset Valuation Reserve requirements are lower for ICOLI than for other investments

- *Cost-efficient Financing of Employee Benefit Liabilities:*

The tax and accounting benefits of ICOLI could potentially reduce the long-term economic cost, and financial impact of executive benefit programs permitting the updating or enhancement of those programs on a cost-neutral basis to the Company.

- *Clear Regulatory and Tax Guidance:*

As discussed more fully below, there is clear guidance from the IRS, from the NAIC, and from the rating agencies as to the prudent structuring and management of ICOLI transactions:

- From a tax standpoint, Congress / the IRS codified "best practices" for the purchase of COLI in Section 101(j) added by the Pension Protection Act in 2006,
- The NAIC has provided clear guidance with respect to Statutory accounting and reporting and,
- A.M. Best and S&P have clarified their view of the impact of ICOLI purchases / holdings on their capital adequacy models and have recommended limits of ICOLI exposures.

### ***Potential Step-up in Yield: Tax Savings vs. Insurance Costs***

If the tax savings of an ICOLI investment outweigh the life insurance loads and expenses, the net asset yield would be increased; and, that increase would be immediately accretive to earnings. The table on the following page illustrates a hypothetical example of the potential step in the after-tax yield.

	<b>Hypothetical Taxable Investment</b>	<b>Hypothetical ICOLI Investment - Year 20</b>	<b>Hypothetical ICOLI Investment - Life of Plan</b>
<i>Hypothetical Investment Return</i>	6.50%	6.50%	6.50%
<i>Investment Mgt. Fees</i>	-0.25%	-0.35%	-0.35%
<i>Net Investment Rate</i>	6.25%	6.15%	6.15%
<i>Taxes on Investment Income at 21%</i>	-1.31%	0.00%	0.00%
<i>Insurance Loads and Expenses*</i>	0.00%	-0.60%	-0.25%
<i>Net After-Tax Return</i>	4.94%	5.55%	5.90%
<i>Potential Step-up in After-Tax Return</i>		0.61%	0.96%
<i>Effective Tax Rate / Insurance Expense Rate</i>	21.00%	9.76%	4.07%

\* Up-front Insurance charges include state premium and federal DAC taxes and broker/consultant compensation. Monthly expenses for policy administration, cost of insurance (COI), and mortality and expense (M&E) expenses are charged against cash value, as are investment management fees. These loads and expenses are expressed as a % of assets for illustrative purposes and are net of any revenue sharing allowance.

## Potential RBC Relief

The following is a hypothetical illustration of the potential RBC relief and step-up in income from an \$20 million ICOLI purchase.

<b>TAXABLE PORTFOLIO</b>						
<b>Asset Class</b>	<b>Amount</b>	<b>RBC Charges</b>	<b>Capital Charges</b>	<b>Yield</b>	<b>Weighted Yield</b>	<b>Pre-Tax Earnings</b>
Common Stock	8,000,000	15.00%	1,200,000	7.00%	2.41%	560,000
Schedule BA Investments	8,000,000	25.00%	2,000,000	9.00%	3.10%	720,000
Fixed Income	4,000,000	0.80%	32,000	3.00%	0.52%	120,000
Treasuries Reserved	3,232,000	0.00%	0	1.50%	0.21%	48,480
	<u>23,232,000</u>	16.16%	<u>3,232,000</u>		6.23%	<u>1,448,480</u>
					<b>Pre-tax Annual Income</b>	<b>1,448,480</b>
					<b>After Tax Annual Income (21%)</b>	<b>1,144,299</b>
					<b>After Tax Weighted Average Yield</b>	<b>4.93%</b>

## ASSETS HELD WITHIN ICOLI

<i>Asset Class</i>	<i>Amount</i>	<i>RBC Charges</i>	<i>Capital Charges</i>	<i>Yield</i>	<i>Weighted Yield</i>	<i>Pre-Tax Earnings</i>
Common Stock	8,000,000	5.00%	400,000	6.30%	2.40%	504,000
Schedule BA Investments	8,000,000	5.00%	400,000	8.30%	3.16%	664,000
Fixed Income	4,000,000	5.00%	200,000	2.30%	0.44%	92,000
Treasuries Reserved	1,000,000	0.00%	0	1.50%	0.07%	15,000
	21,000,000	16.16%	1,000,000		6.07%	1,275,000

<i>Tax-Exempt Annual Income</i>	<b>1,260,000</b>
<i>After Tax Annual Income (21%)</i>	<b>11,850</b>
<i>Total After-Tax Net Annual Income</i>	<b>1,271,850</b>
<i>After Tax Average Yield</i>	<b>6.06%</b>

## COMPARATIVE SUMMARY

	<i>Taxable Portfolio</i>	<i>Assets Held Within ICOLI</i>	<i>ICOLI Advantage</i>
RBC Charges	3,232,000	1,000,000	-2,232,000
After-Tax Annual Income	1,144,299	1,271,850	127,551
After-Tax Annual Yield	4.93%	6.06%	1.13%

### PREVALENCE OF ICOLI

In the last 10 years, ICOLI holding have doubled to approximately \$30 billion as of December 31, 2018. Over 50% of life insurance companies held ICOLI assets as of that date accounting for approximately \$20 billion of that total, with P&C companies holding approximately \$10 billion. \*

More than a dozen well known insurance companies each reported over \$1 billion of ICOLI assets as of December 31, 2018: \*\*

- AIG
- Liberty Mutual
- Northwestern Mutual
- Chubb
- Met Life
- State Farm
- Equitable
- Nationwide
- TransAmerica
- John Hancock
- New York Life

For over 40% of companies reporting holdings, ICOLI assets amounted to 10% or more of Statutory Capital and, for a few, as much as 15 – 24%. While historically ICOLI holdings have been concentrated among the

largest insurance companies, a number of mid-sized carriers have made purchases in recent years. The chart below summarizes ICOLI assets by size for both Life and P&C insurance companies:

UTILIZATION OF ICOLI	
<i>Asset Size</i>	<i>Percent of Carriers</i>
\$50 Billion +	43%
\$ 10 - \$50	25%
\$5 - \$10	25%
\$1 - \$5	16%
Under \$1	4%

\*Source: Glasir Life Sciences

\*\* S&P Global database

**STRUCTURING AN ICOLI INVESTMENT**

The ICOLI purchaser faces several key decisions in structuring the investment to maximize the performance of the asset in a manner consistent with the company’s objectives and tax and regulatory requirements. A discussion of two key issues follows:

General Account versus Separate Account

COLI / BOLI / ICOLI transactions can be structured using a general account product or a separate account contract. The primary distinction between the two types of products lies in the investment of the policy cash value.

In a general account product, the investments are held in the insurance company's general account and managed in accordance with the carrier’s investment guidelines, which generally requires a significant allocation to fixed income securities. As a result, interest rate risk is inherent in the crediting of earnings to policy cash value.

The cash value of a variable life insurance policy (referred to as a “separate account” contract) varies based on the performance of the investment sub-accounts selected by the policyholder. There is generally a wide variety of investment funds offered in the contract, some of which may be managed internally by the insurance carrier, and others managed by professional asset managers selected by the carrier (for example, PIMCO, Goldman Sachs, BlackRock or Morgan Stanley).

Separate account variable universal life policies are considered securities by the SEC, are further categorized as “Registered” products (VUL), or as “Private Placement Variable Universal Life” (PPVUL) contracts. The graphic below provides a comparative summary of the key characteristics of general account versus separate account COLI / BOLI / ICOLI products.

# PRODUCT STRUCTURE

## Investment of Policy Cash Value

### GENERAL ACCOUNT

- Assets managed by insurance carrier in accordance with its investment guidelines, and state regulatory requirements. The policyholder has no control over the investment of general account assets.
- Interest is credited to cash value based on the carrier's portfolio yield primarily from investment-grade bonds and mortgages, with lesser allocations to equities, real estate and alternative investments.
  - Usually, with a minimum guaranteed rate.
- Provide diversification to asset classes in which an ICOLI purchaser might not invest directly.
- Commonly used for BOLI purchases.
- Some equity index options are available, which credit earnings to cash value based on the change in the index (e.g., S&P 500), subject to a minimum and maximum rate. While popular in the retail market, there are few choices for institutional buyers.
- NAIC Risk-Based Capital charges are 0% for life and 5% for P&C companies.
- Rating agency ratings are based on the rating of the issuing insurance company.
- Subject to credit risk of carrier.
  - A multi-policy, multi-carrier approach often used to mitigate the credit risk.

### SEPARATE ACCOUNT

- Cash value growth is linked directly to the performance of the underlying investments in the sub-accounts selected by the policyholder.
  - There is no minimum rate guarantee
  - Subject to market risk, and sometimes acquired with a Stable Value Wrapper.
- Greater transparency with respect to earnings and loads and expenses.
- Greater flexibility with respect to the structuring of premiums and withdrawals.
- Separate account assets are not subject to the carrier's general creditors or liabilities of other separate accounts.
- A separate account contract is both an insurance product regulated by the states, and a security regulated by the SEC.
- NAIC Risk-Based Capital charges are the same as for general account products; 0% for life and 5% for P&C companies.
- Rating agencies may "look through" separate account to underlying investments; but the capital charges are generally less than those for direct investment.
- Commonly used for ICOLI purchases.

### REGISTERED VUL

- Cash value assets can be allocated by the policyholder among a menu of funds, established by the carrier, representing all major asset classes.
  - The funds may be managed by the carrier or by well-known outside asset managers.
  - Assets can be reallocated without triggering tax on gains.
  - Some carriers have, or are considering, including collared index equity options among the investment line-up as they offer the benefit of exposure to equity markets, but with downside protection. However, few equity index contracts offer true institutional pricing.

### PRIVATE PLACEMENT VUL

- Investment oriented, institutionally priced contract
- Limited security offering with reduced SEC regulation available only to institutional or "accredited investors."
- Portfolio can be custom tailored to meet specific investment objectives (e.g., to mirror an existing portfolio).
- Up-front loads and expenses (including premium and DAC taxes, sales loads and capital charges) are significantly reduced in comparison to those of retail products:
  - And, can be deferred and amortized to maximize early cash values.

### Stable Value Wrap

A Stable Value Wrap can be used with a separate account product to smooth volatility. In addition, it may allow book value accounting treatment rather than mark-to-market accounting treatment for separate

account assets. While commonly used by banks and publicly traded companies with respect to separate account purchases, it is not as frequently used for ICOLI transactions.

In general, the stable value wrap provider will set limits and restrictions on the composition of the portfolio to be wrapped (e.g., requiring that at least xx% of the portfolio be allocated to fixed income securities), and the frequency of reallocation. The cost of the stable value wrap is highly dependent on the volatility of the portfolio assets being wrapped and can range upward from 30 bps.

**MEC vs. Non-MEC Contracts**

In addition to the type of policy or investment accounts, there are two policy structures to consider that impact performance, liquidity and taxation. The following table provides a comparative summary of the key characteristics of each policy structure - Modified Endowment Contract (MEC) and Non-Modified Endowment Contract (Non-MEC).

<b>MECS VS. NON-MECS – KEY CHARACTERISTICS</b>			
<b>Characteristic</b>	<b>MEC</b>	<b>Non-MEC</b>	<b>Comments</b>
<ul style="list-style-type: none"> <li>Premium Structure</li> </ul>	<ul style="list-style-type: none"> <li>Single pay</li> </ul>	<ul style="list-style-type: none"> <li>Annual pay (generally 5 – 7 years)</li> </ul>	<p>A single premium MEC structure generally provides the best performance, and is typically used to maximize returns for an investment-oriented balance sheet transaction.</p>
<ul style="list-style-type: none"> <li>Death Benefit</li> </ul>	<ul style="list-style-type: none"> <li>Minimum death benefit is generally lower resulting in lower Cost of Insurance (COI) charges</li> </ul>	<ul style="list-style-type: none"> <li>Minimum death benefit is generally higher resulting in additional COI charges</li> </ul>	
<ul style="list-style-type: none"> <li>Typical Application</li> </ul>	<ul style="list-style-type: none"> <li>Financial transaction – seeking enhancement of portfolio yield</li> </ul>	<ul style="list-style-type: none"> <li>Informal funding of executive benefit liabilities</li> </ul>	<p>A 5 or 7-pay premium non-MEC structure is typically used for the informal funding of executive benefit liabilities where it is anticipated that cash value may be withdrawn to pay benefits.</p>
<ul style="list-style-type: none"> <li>Liquidity / Taxation</li> </ul>	<ul style="list-style-type: none"> <li>Withdrawal of cash value and loans come out as taxable gains first, basis second.</li> <li>Gains are taxed at the corporate rate, plus a 10% penalty tax</li> <li>Death benefits are tax-free</li> </ul>	<ul style="list-style-type: none"> <li>Withdrawal of cash value comes out as basis first, then taxable gains, but no 10% tax penalty</li> <li>After basis has been fully withdrawn, taxable gains can be avoided with a switch to loans</li> <li>If the policy lapses or is surrendered, any gains (including loans) are taxed at the corporate rate.</li> <li>Death benefits are tax-free</li> </ul>	



## PROCESS

The purchase of ICOLI involves a number of steps; but the process is simplified by the availability of substantial regulatory and tax guidance, and the assistance of an experienced consultant.

- Identification of goals and objectives: For example:
  - Yield enhancement,
  - Repositioning of assets for RBC relief,
  - Cost-efficient financing of executive benefit liabilities and/or,
  - Improved Schedule BA disclosures.
- Preliminary design of ICOLI transaction based on goals and objectives:
  - Identification of the desired asset allocation strategy
  - Identification of the employees to be insured, subject to the requirements of Section 101(j) (the codification of COLI best practices incorporated in the 2006 Pension Protection Act)
- Comprehensive financial modeling:
  - Cost / benefit analysis comparing the frictional costs associated with the ICOLI purchase to the projected tax benefits
  - Capital impact analysis
  - Downside analysis
- Carrier / Product Analysis and Selection:
  - Consistent with established goals and objectives for ICOLI program:
    - General versus separate account product
    - MEC versus non-MEC structure
    - Use of multiple carriers in consideration of concentration limitations
- Approval Process
- Implementation:
  - Documentation of the purchase / due diligence process
  - Participant / insured employee communication (notice and consent)
  - Wiring of premium
- On-Going Administration
  - Preparation of administration manual
  - Identification of any special accounting & reporting requirements
  - Tax compliance (annual reporting of ICOLI holdings)

## ACCOUNTING AND REPORTING

ICOLI ACCOUNTING TREATMENT			
ACCOUNT	STATUTORY	GAAP	COMMENTS
<b>Balance Sheet Asset</b> <ul style="list-style-type: none"> <li>Cash Surrender Value</li> </ul>	<ul style="list-style-type: none"> <li>Admitted asset recorded at realizable value as, "Aggregate Write -ins Other than Invested Assets"</li> </ul>	<ul style="list-style-type: none"> <li>Classified as "Other Assets"</li> </ul>	<ul style="list-style-type: none"> <li>Repositioning of assets from "Invested Assets" to "Other Assets" creates a favorable capital impact with RBC relief, especially in the case of highly rated RBC assets.</li> </ul>
<b>Income Statement</b> <ul style="list-style-type: none"> <li>Cash value earnings</li> </ul>	<ul style="list-style-type: none"> <li>Recorded as, "Aggregate Write-ins for Misc. Income"</li> <li>Book value accounting for general account products, and for a separate account with a stable value wrap</li> </ul>	<ul style="list-style-type: none"> <li>Recorded as, "Other Income"</li> <li>Book value accounting used for general account, or for a separate account with a stable value wrap</li> <li>Mark to market required for a separate account with no SVW</li> </ul>	<ul style="list-style-type: none"> <li>Realized gains are recognized in income in each case.</li> <li>With ICOLI, unrealized gains are recognized in the P&amp;L as part of cash value earnings rather than in Surplus.</li> </ul>
<b>Income Statement</b> <ul style="list-style-type: none"> <li>Insurance loads and expenses</li> </ul>	<ul style="list-style-type: none"> <li>Charged against cash value, the change in which is reflected in the income or expense to be recognized under the contract.</li> <li>If net expense, recorded as "Misc. Expense."</li> </ul>	<ul style="list-style-type: none"> <li>Charged against cash value, the change in which is reflected in the income or expense to be recognized under the contract.</li> <li>If net expense, recorded "Other Expenses."</li> </ul>	
<b>Income Statement</b> <ul style="list-style-type: none"> <li>Death benefits in excess of CSV</li> </ul>	<ul style="list-style-type: none"> <li>Recorded in, "Aggregate Write-ins for Misc. Income"</li> </ul>	<ul style="list-style-type: none"> <li>Recorded in "Other Income"</li> </ul>	
<b>Deferred Tax Treatment</b> <ul style="list-style-type: none"> <li>Cash value earnings</li> </ul>	<ul style="list-style-type: none"> <li>NA – ICOLI earnings are treated as a permanent difference under SSAP 101.</li> </ul>	<ul style="list-style-type: none"> <li>NA – Permanent difference</li> </ul>	<ul style="list-style-type: none"> <li>Subject to the purchaser's intent to hold the policies until death of the insured. If not, then deferred tax accounting would be required.</li> </ul>
<b>Schedule BA</b> <ul style="list-style-type: none"> <li>Other Invested Assets</li> </ul>	<ul style="list-style-type: none"> <li>NA</li> </ul>	<ul style="list-style-type: none"> <li>NA</li> </ul>	<ul style="list-style-type: none"> <li>"Cleaning up" BA may be a key motivating factor for an ICOLI purchase.</li> <li>Alternatives (PE / hedge funds) in a separate a/c are not "Other Invested Assets."</li> </ul>
<b>Basket Clause</b>	<ul style="list-style-type: none"> <li>ICOLI alternative assets are not "Other Invested Assets" and, therefore, not included.</li> </ul>	<ul style="list-style-type: none"> <li>NA</li> </ul>	<ul style="list-style-type: none"> <li>ICOLI is not included among Basket Clause assets as it is not an Invested or Capital asset.</li> </ul>

## ***Reporting Requirements for ICOLI***

Employers who own life insurance policies issued after August 17, 2006, are required to report the following information to the IRS annually on Form 9925:

- Total number of employees at the end of the year.
- Number of employees insured under employer-owned life insurance contracts at end of year.
- Total amount of insurance in force under such contracts at the end of year.
- Statement verifying the employer has valid consent forms for each insured employee.

## **REGULATORY NOTES**

- NAIC:
  - For ICOLI, classified as “Other Than Invested Assets,” the RBC charge is 5% for P&C companies, and 0% for Life companies, in comparison to 15-20% for P&C companies and up to 30% for life companies for equities and alternative investments.
  - For 2018, NAIC expanded required disclosures to include the underlying investment categories of the ICOLI contract’s CSV (for example, the percentage allocated to bonds, equities, mortgage bonds, real estate, short-term derivatives and other invested assets).
- AM Best:
  - AM Best classifies ICOLI in the same manner as the NAIC - as a Class 1 bond with the same rating as the insurance company that issued the ICOLI.
  - BCAR charge of .8% for Life, and 5% for P&C companies in comparison to 15-20% for P&C companies and up to 30% for life companies for equities and alternative investments.
- S&P:
  - S&P rates general account ICOLI in the same manner as the NAIC but will generally “look through” a separate account to the underlying asset.
  - Capital Adequacy Model charges applied to ICOLI are based on the ratings of both the purchaser and the issuing carrier and range from 5% - 8% for P&C companies, and 1% to 7% for life companies.
  - Guideline purchase limits are 25% of Total Adjusted Capital and 10% of Total Adjusted Surplus for exposure to a single entity.

## TAX TREATMENT

In addition to meeting the general requirements under the Internal Revenue Code for favorable tax treatment as a life insurance contract under Sections 7702 / 7702A, the following are tax provisions and issues of specific relevance to ICOLI transactions and holdings:

- Section 101(j): Added by the Pension Protection Act in 2006, it provides statutory support for the use of COLI / BOLI / ICOLI as a corporate financing vehicle and provides clear guidance with respect to the employees that can be insured under the arrangement (generally, the top 35% highest paid employees), as well as the notice and consent requirements.
- Separate Accounts: There are special tax rules applicable to insurance-dedicated funds in a separate account which require a minimum level of diversification. In addition, they limit the amount of control the policy holder has over asset management. In general, the “Investor Control” doctrine requires that the fund be managed on an independent discretionary basis.
- Revenue Procedure 2007-61: Confirms favorable tax treatment subject to compliance with the Section 101(j) and, in addition, clarifies that ICOLI earnings are not subject to the proration rules of Section 264(f) generally applicable to tax-exempt income.
- TCJA Changes: The Tax Cuts and Jobs Act of 2017 made a number of changes to the taxation of insurance companies, in such areas as; calculating tax reserves, the treatment of deferred acquisition costs and the dividends received deduction. Those provisions relevant to ICOLI transactions and holdings are as follows:
  - The reduction in the corporate tax rate to 21%: As a result of this change, deferred tax assets and liabilities will reverse at the lower rate impacting their recorded value and the “Change to Deferred Taxes” in Capital and Surplus.
  - Elimination of the Corporate Alternative Minimum Tax: Some insurance carriers were historically “AMT taxpayers.” The elimination of the corporate AMT may impact the company’s effective tax rate, which is a key component of the analysis of the potential benefits of an ICOLI transaction.
  - NOL Changes: Under old law, 100% of net operating losses could be carried back 2 years and then forward 20 years. TCJA changes the NOL rules for life insurance companies. It repeals the 2-year carryback and limits the NOL deduction to 80% of taxable income. However, any remaining NOLs can be carried forward indefinitely. This change could impact the valuation of related deferred tax assets. For P&C Companies, the old rules still apply.
  - Proration (P&C companies only): Under old law, the calculation of the amount of tax-deductible loss reserves was reduced by 15% of tax-exempt interest and the dividends received deduction. TCJA increased the proration percentage to 25%. However, this should have no direct impact on an ICOLI transaction as Revenue Procedure 2007-61 clarifies that the proration adjustment is not applicable to ICOLI earnings.

## IN SUMMARY

ICOLI holdings have more than doubled in the last 10 years primarily because of the on-going search among insurance companies for investment yield in this continuing low interest rate environment. The favorable tax treatment and the opportunities for greater asset diversification among non-traditional asset classes make it an attractive investment which is generally immediately accretive to earnings.

In addition to the potential for yield enhancement, ICOLI also provides an opportunity to improve a carrier's RBC ratio and, in some cases, mitigate certain disclosure requirements.

And finally, the availability of clear tax and regulatory guidance make the ICOLI purchase process relatively straightforward.



## ABOUT EBS

EBS is an independent executive benefits consulting firm which provides total plan management services with respect to programs specifically designed for key employees and professionals. Those services include:

- Consulting with respect to plan design,
- The structuring of related financing and benefit security arrangements,
- The design and management of the participant communication, education and enrollment processes,
- Management of any informal funding assets and,
- On-going plan administration and technical support.

More information about the firm can be found at: [www.executivebenefitsolutions.com](http://www.executivebenefitsolutions.com).

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