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## Community Banking- Unique Opportunities

*Operating Insurance Subsidiary  
BOLI Holdings Assessment*

James L Harvin Managing Director  
In Partnership with



# Why create an Operating Insurance Subsidiary?

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## Non Interest Products and Services

### ■ Attract and Retain Customers

#### Compete!

### ■ Create Revenue

### ■ Compliance

# Why create an Operating Insurance Subsidiary?

## Commercial Banks - Median Results

(For the Twelve-Month Period Ending December 31, 2008)

		<b>Total Assets (000)</b>	<b>Total Revenue (000) 1</b>	<b>Net Interest Income %</b>	<b>Non Interest Income %</b>
U.S. Comm. Banks +\$100 Billion	19	\$155,363,157	\$8,852,789	62.7%	37.3%
Midwest \$10 Billion - \$25 Billion	65	\$ 15,000,967	\$ 785,959	68.6%	31.4%
Largest in Ohio Median	5	\$146,013,198	\$5,089,269	52.9%	47.1%
Ohio \$500 Million - \$1 Billion	13	\$ 675,149	\$ 26,890	83.9%	16.1%
Ohio \$100 Million - \$500 Million	69	\$ 194,659	\$ 7,902	85.2%	14.8%
Ohio \$75 Million - \$100 Million	15	\$ 89,698	\$ 3,498	88.0%	12.0%

(1) Net interest income plus non interest income

# Why create an Operating Insurance Subsidiary?

## Credit Unions - Median Results

(For the Twelve-Month Period Ending December 31, 2008)

		<b>Total Assets</b>	<b>Total Revenue</b>	<b>Net Interest</b>	<b>Non Interest</b>
		<b>(000)</b>	<b>(000) 1</b>	<b>Income %</b>	<b>Income %</b>
U.S. Credit Unions +\$10 Billion	3	\$16,706,624	\$ 666,220	69.7%	30.3%
Midwest Credit Unions +\$1 Billion	24	\$ 1,359,339	\$ 56,866	65.4%	34.6%
5 Largest in Ohio Median	5	\$ 731,538	\$ 26,193	62.3%	37.7%
Ohio \$500 Million - \$1 Billion	4	\$ 628,851	\$ 24,048	64.6%	35.4%
Ohio \$100 Million - \$500 Million	42	\$ 160,616	\$ 6,239	58.9%	41.1%
Ohio \$75 Million - \$100 Million	14	\$ 86,872	\$ 3,067	49.4%	50.6%

(1) Net interest income plus non interest income

# Why create an Operating Insurance Subsidiary?

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- In virtually all other states, most banks have already taken advantage of an operating insurance subsidiary:
  - In Michigan, 90% of Banks have an insurance sub
  - In Ohio, 15% (35) - 10 created by CBAO

# Why create an Operating Insurance Subsidiary?

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- Does not create a retail insurance agency
- Does not require the offering of *any* insurance product/products
- Does not require large amounts of capital
- Does not create additional expense

# Why create an Operating Insurance Subsidiary?

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- ❑ In Michigan, banks started utilizing insurance subs only recently for other than commissions on bank insurance premiums:
- ❑ Commissions available on bank insurance premiums

# Why create an Operating Insurance Subsidiary?

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## Agency formation

- Multi owner Limited Liability Company (LLC)

- Owned by Bank Holding Company if available

  - Possible State Franchise Tax benefit

## Tax Considerations

  - Corporate Entity Election Form (IRS Form 8832)

  - Taxed as a "C" Corporation

  - Affiliation Form filed with consolidated tax return

# Why create an Operating Insurance Subsidiary?

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## Administrative Functions by CBAO Staff

- EIN acquisition.

- LLC preparation

  - Operating Agreement

  - Articles of Organization

- License filings - Determine license holder for agency

- Agency appointments- Ohio Department of Insurance

- Regulatory notification (s)

- Sample board policy that can be customized for use by the bank.

# Why create an Operating Insurance Subsidiary?

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## Consulting Services - Austin Associates

Pre formation interview and analysis.

On site strategic business and marketing planning session with Financial Institution Management

Product prioritization, opportunity assessment and selection

Recommendations for product and program offerings.

# Aggregation- A Community Banking Solution

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- Aggregation can provide needed products and services, competitive pricing and generate non interest revenue

# Aggregation- A Community Banking Solution

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- Provides scale
  - Product availability
  - Pricing

# Aggregation- A Community Banking Solution

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## □ CBAO - MACB

### ■ Community Banking Initiatives, LLC



50-50 CBAO – MACB:

Partner contracting with CBI, LLC

# Aggregation- A Community Banking Solution

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## □ Community Banking Initiatives, LLC

- Three states currently participating- CBAK
- 8 more Associations in discussions
- 76 banks enrolled to date
- 219,335 households
- New banks added daily

# Aggregation- A Community Banking Solution

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- Community Banking Website-
  - Association branded
  - Drop downs for specific products
  - Customer access- bank access with user ID and pass code
  - Marketing Materials, Training

# Aggregation- A Community Banking Solution

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- Current Products – in use or in development:
  - ID Theft – “Red Flag “ Solution
  - Commercial Check Recovery
  - Up-dated Accidental Death
  - Term Life Insurance
  - Home Warranty

# BOLI HOLDINGS ASSESSMENT

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*“The safe and sound use of BOLI depends on effective senior management and board oversight...”*

# BOLI HOLDINGS ASSESSMENT

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*“A comprehensive assessment of BOLI risks on an ongoing basis is an important element of the risk management process.....”*

*“The BOLI risks that should be assessed, managed, monitored, and controlled include liquidity, transaction/operational (including the tax and insurable interest implications), reputation, credit, interest rate, compliance/legal, and price risk.”*

# BOLI HOLDINGS ASSESSMENT

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*“Although the board may delegate decision-making authority related to purchases of BOLI to senior management, the board remains ultimately responsible for ensuring that the purchase and holding of BOLI is consistent with safe and sound banking practices.”*

# BOLI HOLDINGS ASSESSMENT

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*“Management should review the performance of the institution’s insurance assets with its board of directors at least annually”*

*“More frequent reviews are appropriate if there are significant anticipated changes to the BOLI program such as additional purchases, a decline in the financial condition of the insurance carrier(s), anticipated policy surrenders, or changes in tax laws or interpretations that could have an impact on the performance of BOLI*

# BOLI HOLDINGS ASSESSMENT

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- Financial Markets in a Period of Dramatic Change
  
- Credit Quality
  - Insurance Companies have Formed Bank Holding Companies to Received TARP Money

# BOLI HOLDINGS ASSESSMENT

Company Name	Standard & Poors				Moody's				Fitch			
	Rating	Financial Strength Direction	Financial Strength Rating Watch	Financial Strength Rating Date	Rating	Financial Strength Direction	Financial Strength Rating Watch	Financial Strength Rating Date	Rating	Financial Strength Direction	Financial Strength Rating Watch	Financial Strength Rating Date
Northwestern Mutual Life	AAA	Affirm	Stable	9/17/2008	Aaa	Affirm	Stable	4/8/2009	AAA	Affirm	Stable	6/12/2008
Mass Mutual Life	AAA	Affirm	Negative	5/27/2009	Aa1	Affirm	Negative	5/26/2009	AAA	Affirm	Negative	3/25/2009
New York Life	AAA	Affirm	Stable	8/28/2008	Aaa	Affirm	Negative	3/17/2009	AAA	Affirm	Negative	4/16/2009
Guardian Life	AA+	Upgrade	Stable	7/16/2008	Aa2	Affirm	Stable	5/19/2006	AA+	Affirm	Stable	7/31/2008
John Hancock Life	AA+	Downgrade	Stable	2/24/2009	Aa3	Downgrade	Negative	3/18/2009	AA	Downgrade	Negative	2/27/2009
Great-West Life	AA	Affirm	Stable	2/1/2007	Aa3	Affirm	Stable	11/27/2007	AA+	Affirm	Stable	4/20/2009
MONY Life	AA	Affirm	Negative	2/19/2009	Aa3	Affirm	Stable	7/25/2007	AA-	Downgrade	Negative	3/20/2009
Ohio National Life	AA	Affirm	Stable	1/4/2005	A1	Affirm	Stable	1/10/2005	-	Remove	-	2/5/2003
Sun Life	AA	Downgrade	Negative	3/6/2009	Aa3	Downgrade	Negative	2/12/2009	AA-	Downgrade	Negative	3/23/2009
Transamerica Life	AA-	Downgrade	Negative	3/31/2009	A1	Downgrade	Negative	2/17/2009	AA	Downgrade	Negative	3/6/2009
General American Life	AA-	Downgrade	Negative	2/26/2009	Aa2	Affirm	Negative	2/9/2009	AA	Affirm	Negative	2/11/2009
MetLife	AA-	Downgrade	Negative	2/26/2009	Aa2	Affirm	Negative	2/9/2009	AA	Affirm	Negative	2/11/2009
ING Life	AA-	Affirm	Negative	4/16/2009	A1	Downgrade	Stable	1/28/2009	AA-	Downgrade	Negative	1/28/2009
Security Life of Denver	AA-	Affirm	Negative	4/16/2009	A1	Downgrade	Stable	1/28/2009	AA-	Downgrade	Negative	1/28/2009
Lincoln National Life	AA-	Affirm	Negative	5/6/2009	A2	Downgrade	Negative	4/15/2009	A+	Downgrade	Negative	4/16/2009
Prudential	AA-	Downgrade	Stable	2/26/2009	A2	Downgrade	Negative	3/18/2009	A+	Downgrade	Negative	2/19/2009
Protective Life	AA-	Downgrade	Stable	2/26/2009	A2	Downgrade	Negative	2/12/2009	A+	Downgrade	Negative	11/5/2008
West Coast Life	AA-	Downgrade	Stable	2/26/2009	A2	Downgrade	Negative	2/12/2009	A+	Downgrade	Negative	11/5/2008
Principal Life	A+	Affirm	Positive	5/13/2009	Aa3	Affirm	Stable	5/20/2009	AA-	Affirm	Negative	5/13/2009
AIG Life Insurance	A+	Affirm	Negative	3/2/2009	A1	Downgrade	Developing	3/2/2009	A-	Downgrade	Developing	5/15/2009
Midland National Life	A+	Downgrade	Stable	2/26/2009	-	-	-	7/25/2007	A	Downgrade	Negative	5/7/2009
Connecticut Gen Life	A	Affirm	Negative	11/4/2008	A2	Affirm	Negative	11/3/2008	A	Downgrade	Stable	4/13/2009
Hartford Life	A	Downgrade	Negative	3/3/2009	A3	Affirm	Developing	5/18/2009	A-	Downgrade	Negative	5/12/2009

# BOLI HOLDINGS ASSESSMENT

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- Decline in Crediting Rates Have Exposed Policy Design Flaws
  - Universal Life
  - Internal Policy “Guarantees”

# BOLI HOLDINGS ASSESSMENT

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## Independent BOLI Assessment

- Fiduciary Responsibility
- Regulatory Requirement
- Provided by Current Vender?

# BOLI HOLDINGS ASSESSMENT

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- Austin Associates - as a Consultant to CBAO:

*Provides an Independent Preliminary Assessment of Bank BOLI Holdings:*

- Credit Quality
- Yield
- Policy Structure
- Compliance
- Options for Remediation

# BOLI HOLDINGS ASSESSMENT

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## □ Austin Associates

- Not Licensed to Sell Insurance- Process will Not Sell the Bank Anything
- Does Not Represent any BOLI Administrator
- Over 25 Years Experience with BOLI
- Conducted "Due Diligence" on Top 25 Administrative BOLI Providers
- Compensated by CBAO as a Part of Ongoing Consulting Relationship

# *Questions?*

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# Thank you!

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James L Harvin

