Leveraged RBC Insurance Security Fund SRIA Surrender Value Shortfall

WESTWARD ADVISORS

WESTWARD'S VIEWPOINT

The cash surrender value **(CSV)** of the Smoothed Return Investment Account **(SRIA)** in RBC Insurance **(RBCI)** Security Fund universal life insurance policies is currently impaired due to the Market Value Adjustment **(MVA)**.

The SRIA MVA has caused the SRIA CSV to fall below the SRIA account balance and in many cases the SRIA CSV is less than the loan balance that it secures **(SRIA CSV Shortfall)**.

The SRIA CSV Shortfall is a **temporary issue** affecting the collateral value of the SRIA to lenders in the event of loan default.

Lenders are accepting some of the SRIA CSV Shortfall risk on a loan-by-loan basis after considering the policy's Tax Refund feature and the financial strength of the borrower and loan guarantor.

When the SRIA CSV Shortfall exceeds the lender's risk tolerance, the lender will require the borrower/guarantor to provide **Additional Security** by way of one or more of the following actions *until the SRIA CSV recovers:*

1. Defer planned loan draws
2. Provide evidence of liquid assets
3. Provide additional guarantees
4. Provide additional collateral
5. Reduce the loan balance

The MVA and resulting SRIA CSV Shortfall do not significantly impact the long-term results of the leveraged life insurance plan but may defer planned loan draws and may require Additional Security temporarily.

For more information, clients can contact their Account Manager or Wayne Stone at waynes@ westwardadvisors.com.

THE SRIA CSV SHORTFALL FORMULA

The formula for the SRIA CSV is:

$$\text{SRIA CSV} = [\text{SRIA Account Value}] - [\text{MVA}] + [\text{Tax Refund}]$$

The **MVA** is (1) SRIA interest credited to the policy, less (2) the policy's share of the actual return in the underlying Smoothed Return Reference Portfolio **(SRRP),** measured only when there is no RBCI loan secured by the SRIA.

The SRIA CSV is partially protected by the Tax Refund if applicable, which is 15% of the CSV in excess of the policy's adjusted cost basis **(ACB).** Since the MVA reduces the CSV, it also reduces the Tax Refund.

Example of SRIA CSV to Lender	
Loan Balance	**10,000,000**
Policy ACB	8,000,000
SRIA Balance	**10,000,000**
MVA	(1,500,000)
Tax Refund @ 15% x (CSV-ACB)	88,235
CSV	**8,588,235**
CSV Shortfall	**(1,411,765)**

THE MVA

The MVA does **not** affect the SRIA interest income guaranteed at 4.1% for calendar 2022, nor the accumulating SRIA account value and tax-free death benefit.

The MVA will apply if the SRIA account value is withdrawn from the policy, transferred to another investment account in the policy, or used to pay insurance charges.

The MVA as a % of the SRIA will vary from policy to policy because the measurement period is different for every policy. The MVA will increase and decrease for all policies in unison, but by a varying % of the SRIA.

The MVA can also increase the CSV, as it did until early 2022, when the SRIA interest credited to the policies is less than their share of the actual SRRP return during the measurement period.

THE PATH FORWARD

The collateral lending value of the RBCI Security Fund policies are not immune to the current market downturn affecting the lending value of many assets. We are working closely with the lenders on every loan to help them assess their risk and minimize Additional Security.

When a lender requires Additional Security from a Westward client, we expect the lender will notify us first and then the private banker will contact the borrower to discuss options.

We will work closely with both to navigate the current economic storm until the markets recover, the CSV Shortfall recovers with it, and Additional Collateral requirements are released.

In the meantime, the SRIA policy values to our clients (as opposed to the lenders) remain unaffected by the MVA, and the leveraged life insurance plans are still on track to achieve their projected results, less the impact of any Additional Security.