

THE NORTHWESTERN MUTUAL LIFE INSURANCE COMPANY

# Bank Owned Life Insurance (BOLI)

## Frequently Asked Questions

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***This piece addresses commonly asked questions about The Northwestern Mutual Life Insurance Company's (Northwestern Mutual) Bank Owned Life Insurance (BOLI) product. It is a Single Premium Life (SPL) general account, participating whole life insurance contract that is a MEC at issue. The contract includes an "Amendment to Dividends and Cash Surrender Provisions". This amendment waives the contract's surrender charges as well as pays a prorated dividend upon surrender if all the provisions of the amendment are met at the time of the contract surrender.***

### **Why should a bank consider buying BOLI from Northwestern Mutual?**

Northwestern Mutual's product is unique in the BOLI market. It is a participating dividend-paying contract with a schedule of guaranteed cash value that increases each year to age 100. Dividends are not guaranteed. The interest component of the dividend is designed to allow the bank to share in the performance of Northwestern Mutual's general account portfolio. Northwestern Mutual's BOLI product is backed by our financial strength. We have consistently maintained the best possible insurance financial strength ratings from all four major rating agencies (Moody's, Standard & Poor's, Fitch and A.M. Best). Only one other insurance group (TIAA) can make that claim.

### **How much BOLI has Northwestern Mutual sold?**

Many banks have found our offering of strong policy values from a AAA-rated carrier attractive. While Northwestern Mutual has been issuing policies to banks for decades, the product most often purchased by our bank clients is our Single Premium Life with the Amendment to Dividends and Cash Surrender Provision (SPL BOLI). Through 2007, over 600 banks have purchased about 1,200 tranches of SPL BOLI. The large number of repeat purchases indicates product satisfaction. The 12,300 inforce SPL BOLI contracts have \$3.5 billion of cash value. We have had less than 25 of these SPL BOLI policies lapse and zero policies exchanged to another insurance carrier.

In April, 2002 we extended availability of SPL BOLI to the community bank market. Of the total \$3.5 billion in SPL BOLI cash value, \$2.3

billion is from purchases made April 1, 2002 or later. In addition to the SPL BOLI, we have been issuing policies to banks for almost 50 years. Over 200 banks have 15,700 policies with a total of \$2 billion in cash value.

Therefore, in total, Northwestern Mutual has over 800 bank clients with 28,000 policies that have a total of \$5.5 billion of cash value.

### **How are the assets backing Northwestern Mutual's BOLI policies invested?**

The same assets backing our general account cash value life insurance policies back the cash values of our BOLI contracts. In other words, there is no segregated investment portfolio for BOLI. In our general account investment portfolio, we pursue a long-term strategy with a target balance of about 80 percent fixed-income investments and about 20 percent equities, including common stock, real estate, oil and gas investments, and direct investments in select companies. It is our experience that owning three to four times as much in equities as a typical competitor delivers superior long-term performance on a risk-adjusted basis. Our ability to actively manage a diversified portfolio and pursue a long-term investment strategy has been a key reason for our success at delivering exceptional returns in a variety of economic environments.

## **Do Northwestern Mutual BOLI illustrations comply with all applicable regulations?**

Yes, all our general account (i.e., non-variable) product illustrations including BOLI, are subject to and comply with all insurance regulations. One requirement is that illustrated dividend scales reflect investment earnings, mortality and expenses that are not more favorable than actual current experience. In other words, our illustrated values must reflect the dividends we are actually paying right now, not assumed or hoped-for improvements, and that our illustration actuary personally certifies that fact to the state regulators.

## **Are illustrations projections of future values?**

No, illustrations show how the policy will work under a given set of assumptions. The non-guaranteed values shown are not “projections” or “estimates” of future results and this is stated directly on the illustrations themselves. Indeed, state insurance regulations, with which all insurance companies and vendors are obligated to comply, prohibit suggesting otherwise. Dividend scales go up and down in reaction to investment earnings, expense, and mortality factors. Actual policy performance is rarely exactly as was originally illustrated. The factor most likely to affect BOLI product performance is the dividend scale interest rate. Our illustration software allows illustrations at lower than the current rate. Banks interested in seeing illustrations under an alternate dividend scale interest rate assumptions should contact their Northwestern Mutual financial representative.

## **Are Northwestern Mutual’s current dividends supportable?**

Yes, the dividends we are paying today are supported by current experience. As a mutual company, we operate for the benefit of our policyowners. If we do a good job of managing the company, operating gain is generated. In a stock company, these gains are paid out to shareholders. In contrast, Northwestern Mutual

can either return the gain to policyowners through dividends or add to surplus and the asset valuation reserve (AVR). Surplus and AVR are monies set aside to allow the company to weather adverse experience. In 2007, dividends to participating policyowners approved for payment during 2008 are expected to surpass \$5 billion for the first time in company history. In addition, the combination of surplus and AVR reached an all-time high of \$15.8 billion, an increase of \$1 billion from year-end 2006.

## **Northwestern Mutual's illustrated dividend scale interest rate is sometimes higher than its National Association of Insurance Commissioners (NAIC) Net Yield. Does this imply that Northwestern Mutual is crediting more than it earns?**

No, the interest portion of a dividend shown in our illustrations is based upon the current interest rate actually being paid to our policyowners. This rate reflects actual portfolio results. The NAIC Net Yield is defined by state insurance regulators for their own narrow purposes and does not accurately reflect the BOLI product's crediting rate for two reasons:

- It includes income from lower yielding policy loans. Non-borrowed “direct recognition” policies such as BOLI would not be impacted by these policy loans.
- It excludes capital gains and losses. These items would contribute to or detract from a product's crediting rate. Capital gains have in fact long contributed to the actual yield of Northwestern Mutual’s actively managed investment portfolio.

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A final word about our investment strategy for the managed assets (which do not include policy loans) in our general account and the historical investment performance of these assets.

The investment performance of the managed assets is reflected in the company's dividend scale interest rate for unborrowed funds (which also reflects charges for taxes and a contribution to surplus). This rate is set annually by the company as part of the dividend scale and is used in determining dividends for cash value policies in the company's general account. All other things being equal, a higher (lower) dividend scale interest rate for unborrowed funds means a higher (lower) policy dividend.

The dividend scale interest rate for a particular policy is the interest rate used for crediting interest on policy values after deducting mortality and expense charges. It reflects investment performance of both managed assets and policy loans. Depending on the type of policy, either individual policy loan activity or average loan activity of all policies in the dividend class is reflected.

Because the mortality and expense charges vary each year, a policy's cash value growth will vary each year. As a result, one should not use the dividend scale interest rate as a measure of what the policy's internal rate of return on cash value is or may be.

Policy dividend and underlying interest rates are not guaranteed for the future. The dividend scale is reviewed annually and is subject to change by the company.

For more information about Northwestern Mutual dividends, general account, and investments, the following are available.

- The Power of the Portfolio (29-4692)
- The Portfolio Approach (29-4306)
- Value Through Performance (29-4714)
- Bank Owned Life Insurance (BOLI) - Northwestern Mutual's General Account Product versus Separate Account Products (34-2004)

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