# Additional information from CapitalOne Life Securities for TELOS Rating 01/2014 (Capital Life Advisors/Capital Life Securities S.A. - Design and advisory work associated with Fixed Coupon Life Insurance Backed Securitisation) - because of changes in the company structure

## Here in reference to series II, communicated by TELOS

**Subject of the rating:**

Subject of the rating is the investment management process undertaken by *Capital One Life Securities SA* ("the Bond Issuer") with respect to the Secured Life Insurance Backed Investment Bond ("the Bond. The rating applies to the Asset Origination, Investment Management and Transactional Process only, the rating of assets and risks are excluded. The investment process is rated "AA" (very high quality).

### *Company Profile*

***Capital One Life Securities SA*** (further COLS) is a public limited liability company incorporated under the laws of Luxembourg, having its registered office at 6, route de Trèves, L-2633 Senningerberg, Luxembourg, registered with the RCS under number B-180853. COLS is an unregulated securitization undertaking subject to the provisions of the Securitization Act 2004 and the issuer of ***Secured Life Insurance Backed Investment Bonds*** ("the Bond").

COLS is owned by a select group of ***high net worth individuals and seasoned executives*** with an impeccable track-record of performance and experience acquired at leading global banks, investment firms and insurance companies, some of them as founder, owner, capitalizing on its ***in house competences*** in engineering of structured products and tax-efficient investment vehicles, financial and risk analytics and its long lasting relationships with custodians, depository banks, investment managers, administrators, auditors, etc. COLS has utilized leading law firms to arrange for the regulatory compliance, rating and listing of the bond. COLS has access to a vast ***network of investors***, primarily institutional investors (pension funds, insurance companies, [private] banks, asset and fund managers, trusts and family offices) as well as a ***comprehensive distribution network*** undertaking the actual bond sales.

### *Social Responsibility*

COLS supports and enacts, within its sphere of influence, the ***Ten Principles of the United Nations*** Global Compact, including the Universal Declaration of Human Rights, the International Labour Organization's Declaration on Fundamental Principles and Rights at Work, the Rio Declaration on Environment and Development and the United Nations Convention Against Corruption. Capital One Life Securities engages to provide full transparency to the public on these undertakings in the United Nations annual Communication on Progress.

COLS is a not-for-profit only undertaking. The investment vehicle and the bond are ***strictly in support of social responsibility objectives***. As stated in the articles of association, shareholder of COLS are committed to distribute up to fifty (50) percent of its net profits to social and environmental responsibility programs. Bond holders contribute implicitly to the intended social objectives (without depletion of their returns). The bonds are therefore considered as ***social impact bonds***.

One of the programs in which COLS has committed to invest its profits is the development of a revolutionary genetic test and therapy that resolves a serious medical condition currently affecting a large part of the global female population. The new test, developed by a leading US biotechnology firm, replaces the inhumane invasive and expensive diagnostics and the new cheap therapy prevents the development of the disease (infertility and ovarian cancer). The profit of the bonds will enable woman to obtain the best possible treatment irrespective of their income, social class and have the opportunity to have healthy babies. The test and therapy cause massive reduction of the cost of women' health care. The profits deriving from this medical project will fund development of new diagnostic tests and therapies.

In order to generate the profits for these social impact programs, COLS invests solely in life insurances. The policies are obtained mainly from A+ rated United States carriers, guaranteed by regulated states. These insurances are purchased at deep discount (approx. 20% to 40% of the face value). As the insurances have a fixed face value and mostly fixed costs (premiums) ***the intrinsic returns are highly calculable***. The only key risk factor is the longevity risk, the risk a policyholder lives far longer than expected. These excess premiums however will be hedged by re-insurance solutions.

COLS only purchases policies from policyholders that ***voluntary surrender the policy for mainly economic reasons***, i.e. the policy became obsolete (i.e. due to retirement, home sales, need to settle debts, education of children, divorce, etc.). COLS does not acquire so called VIATICALS (policies of terminal ill patients) or STOLIS (policies generated by agents for sale on secondary market). COLS considers the investment in life insurance policies as a ***highly respectable and ethical undertaking*** as the death benefits are largely re-invested into life-saving as well as more affordable health care, accessible to any world citizen irrespective race, religion, political preference and especially income.

The legitimacy of free trade of policies on the secondary market has even been endorsed by the US government in 1996, when the Clinton administration unwittingly strengthened the case for life settlements when it signed into law the Health Insurance Portability and Accountability

Act (HIPAA). It even allowed the proceeds of a Viatical settlement to be free of federal income tax. A key driver for this change was the need for AIDS patients, with little or no access to health insurance, to be able to fund their healthcare through the liquidation of available assets (source: www.clearlifeltd.com ).

It is however common knowledge that insurance companies are objecting to the free trade of their life insurance policies, combatting such trades in court and even attempting to influence regulators. They qualify this trade as illegal, fraudulent and unethical and consider investment firms highly unqualified to manage the risks involved while remarkably trades by life insurance companies themselves is not (source: http://www.crownlifecanada.com/crown-life-canada-today-announced-purchase-107-5-million-life-settlement-portfolio/).
According COLS the real issue is that policyholders receive substantial more value from the free trade than from the surrender of the policy to their insurer, herewith cannibalizing the insurer's profit margins.

The recognition of a secondary market seems to become a fact. Blackstone Group, the largest alternative asset manager on the globe, has entered into the life settlements market with the recent purchase of a portfolio of USD 800 million in face value bodes well for the future of this asset class. A company with the size and calibre of the Private Equity firm which has USD 279 billion under management brings credibility to the secondary life insurance market. Other giants like TPG Capital and Oak Tree Capital Management have acquired multi-billion dollar portfolios in recent years. Also the policy owners are increasingly better educated. One case in particular that has gotten attention recently is a suit by an elderly California couple alleging that Lincoln National failed to tell them about the option of selling their policy when they no longer could afford the premiums.

***High Fixed Coupon***

The bonds of COLS distinguish itself from other investment bonds by ***the unique combination of high fixed coupon of 7% per annum and low risk***. The bond is structured as to:

- provide protection of the bondholders rights (their invested capital and interest) by "*securitization*"
- preserve the value and intrinsic profits of the assets by *longevity risk hedging*;
- calculate and plan adequate cash flows and cash reserves to timely meet payment obligations (premiums, interest) throughout the whole investment term by *liquidity risk hedging*;

***Securitization***
Under the Securitization Act 2004, the assets of COLS (the bond proceeds, the assets and proceeds deriving from assets) are in accordance with the Securitization Act 2004, held in trust under security deed by a security trustee in order to ***protect secure the investment and interest of the bond holders***. COLS is only entitled to invest in eligible assets as defined in the Offering Memorandum.

***Hedging Longevity Risk***
COLS invests the bond proceeds primarily in life insurance policies with a ***fixed, non-depleting face value*** (100%), which are ***purchased at deep discounts*** (20% to 40% of the face value). ***The life expectancy*** of the policyholder is determined on basis of ***two comprehensive medical tests*** undertaken by two independent medical examiners. For each year the policyholder is alive COLS pays for the premiums. The purchase decisions are made utilizing sophisticated mathematical models (NAV, IRR).
As life insurances have ***hardly correlated to market economies*** (i.e. inflation, economic growth, commodity prices) the ***risks are basically limited to just longevity risk*** (the policy holder lives longer than the expected life expectancy which erodes the calculated intrinsic profit). Instead of predicting the life expectancy of each individual policy holder or depending on averages provided by actuarial databases ***COLS hedges the longevity risk applying a stop-loss insurance, herewith preserving the intrinsic profits***.

***Hedging Liquidity Risk***
As life insurance policies purchases are largely deep-discounted, varying from approx. 20% to 40%. The ***collateral value of these policies therefore easily exceeds 200% of the bond principal and even 100% of the bond principal and full term interest obligations*** (securitization of the bond holder' rights). However, as life insurance policies are illiquid until the death benefits are being paid out, COLS reserves part of the bond proceeds to meet the annual servicing costs of the assets (premium, bond interest). In general ***COLS applies a liquidity sufficiency factor of 2 to 3 year***s. In addition COLS ***hedges the liquidity risk again with an insurance and/or standby credit facility***. COLS obtains only policies from insurance companies with ***investment grade*** or better ratings, domiciled in ***regulated states*** which provide ***guarantees*** on life insurance policies.

***Partners***

COLS utilizes the high quality professional solutions and services of a selected group of professional service companies and international partners to undertake the investment process, the transactions and associated administrative services in accordance with the regulatory compliance. The subject of this rating is not the bond itself, or the asset class but the underlying process. This process essentially involves the bond sales, the investment of the bond proceeds, the origination, procurement, tracing/tracking and collection of benefits of insurance policies, the planning of cash flow and servicing of the assets (premium and interest payments. These complex procedures are undertaken by specialist service companies, which have been collaborating for some time in comparable situations and thus operate as a well-rehearsed team. The partners include the depositary Hauck & Aufhäuser Privatbankiers, Luxembourg, which acts as depository and paying agent. Quintet House, Luxembourg is responsible for sourcing and procurement of life insurance policies, while Data Life Associates, United States provides the actuarial expertise during evaluation of the individual insurance policies. Torrey Pines United States undertakes the day-to-day administrative services associated with the policies (documentation, life expectancy certificates, tracing/tracking, claim submission and collection). Darion Capital Management, Netherlands, the Investment Manager, is responsible for the liquidity planning and allocation of funds. Wilmington Trust acts as security trustee for the Compartment. The Canadian expertise agency Guarantius Capital Inc. provides actuarial and risk management expertise. They assist the Board of Directors, monitoring the overall performance and supply strategic and tactical market information for their decision process. Deloitte Luxembourg undertakes the auditing. Fiscal and legal services are provided by Speechly Bircham, Global Fund House and Wolf Theiss.

### *Board of Directors*

The Board of Directors consists of 3 top executives. Mr. Cornelis Prins is acting CEO of COLS. He is highly experienced as an insurance and re-insurance professional. He obtained a bachelor degree in Economics and a master degree in Law. Mr. Prins held positions as VP at METLIFE, ING, FORTIS and SWISS-RE. Mr. Marcel Learbuch is a highly experienced banker and fund manager with over 20 years of work experience also in the environment of risk- and fund management. Since 2010 he is one of the managing directors of several financial undertakings within the Global Fund House Group. Mr. Learbuch oversees regulatory compliance, financial planning, risk management and statutory reporting. Mr. Uwe Geisler is a seasoned operations manager. He held positions at BNP Paribas Securities, Allfunds Bank and Atlantic Funds services in Luxembourg. At present Mr. Geisler is Director Fund Operations at Global Fund House. COLS retains also the experience of Mr. *Bram Boon* as board advisor. Mr. *Bram Boon* has master degrees in mathematics, actuarial science and business administration and former lead actuary at ING.

### *Issue of Series II*

COLS intends to issue around November 24, 2014 its Series II. The features are identical to Series I. The Offering Period an Offering Memorandum is planned on or around November 3rdl, 2014.

### *Investment Rationales*

COLS believes the secondary market of Traded Life Insurance Policies (LIP's_ (via capital secured bonds) is a potential target for qualified, professional and/or institutional investors due to:

- The life insurance market is a critical component for the US economy and social security of US households. After the economic crisis the US life insurance companies, after debt restructuring, recapitalization and upgrade of systemic risk policies, are in excellent shape;
- The volume and value of the US life insurance market is enormous and growing, providing a high potential for growth to the relative young secondary market (Traded LIP's) as well. In 2008, an influx of capital combined with growing awareness of Traded LIP's among brokers and policy owners increased annual volumes to a high point of $12 billion. In 2011 the total trade in life policies reached US$ 20 billion;
- The secondary market ( Traded LIPs) is highly regulated and the Traded LIP values are hardly correlated to global economic trends and market developments (i.e. commodity prices, stock exchange indices and therefore investments in Traded LIP have a "narrow scope of calculable risk";
- The US is an ageing society. The number of individuals over the age of 60 is growing three times as fast as the total population;. Between 2000 and 2050, the number of older people is projected to increase by 135%. Over this time period, the proportion of the population over 65 years old will increase from 12.7% to 20.3% in 2050; The proportion of the population that is age 85 and older will increase from 1.6% to 4.8% in 2050;
- Due to economic reasons (higher debt burden, lower pension and social security income) and psychographic reasons (life-style, better medical care) more individuals desire to surrender their policy;
- In general Traded LIPs offer the insured party higher economic benefits than the accelerated

benefits (or plain surrender) that insurance companies offer; and

- Life insurance policies have a fixed face value, are hardly correlated to financial markets, merely available from A-rated carriers and certain life insurance policies carry a guarantee on US state level by the US government up to the amount of US$ 500,000,- per policy.
- People buy life insurance to protect their dependents against financial hardship when the insured person, the policyholder, dies. Many life insurance products also allow policyholders to accumulate savings that can be used in a time of financial need. Most American families depend on life insurance to provide this economic protection: seventy percent owned some type of life insurance, according to LIMRA International.
- Americans purchased $2.9 trillion of new life insurance coverage in 2011, a 0.5 percent increase over 2010. By the end of 2011, total life insurance coverage in the US was $19.2 trillion, an increase of 4 percent from 2010.
- Individual life is the most widely used form of life insurance protection, accounting for 57 percent of all life insurance in force in the US at year-end 2011. Typically purchased through life insurance agents, this insurance is issued under individual policies with face amounts as low as $1,000, although larger minimum amounts are more typical in today's market.
- While individual life is principally used for family protection, it also is widely used for business purposes. A business may purchase life insurance to protect against the economic loss that would result from the death of the owner or a key employee.
- Individual life insurance protection in the United States totaled $11 trillion at the end of 2011 and has grown at an average annual rate of 1.6 percent since 2001, when $9.3 trillion was in force.
- The average size of new individual life policies purchased has decreased since 2008 to $162,000 in 2011. The number of individual policies purchased also grew 2 percent in 2011.

 

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