

CORPORATE-OWNED LIFE INSURANCE

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I. Applicability

A. Scope

1. This outline supplements the individual and group life insurance product outlines on the Department's web site and is intended for life insurance products used as corporate-owned life insurance.
2. Corporate-owned life insurance is subject to all of the provisions of the New York Insurance Law, regulations and Department circular letters that are applicable to the type of life insurance product submitted, unless otherwise noted herein.
3. This outline identifies requirements and exceptions that are unique to corporate-owned life insurance.

B. Review Factors

In general, the review standards applicable to a corporate-owned life insurance submission will depend upon the following factors:

1. Purpose or Use. A corporation can use corporate-owned life insurance to fund an employee benefit plan or to provide key person insurance in New York.
2. Format Chosen. A corporation can use either a group life insurance policy covering a number of employees where insurable interest comes under §3205(d) or individual life insurance policies covering one or more of its employees to fund its corporate-owned life insurance program where insurable interest comes under §3205(a)(1)(B) or §3205(d). §3205(a)(1)(B) is not available in the group setting since the 4216(b)(1) would prohibit the employer from being the beneficiary.
3. Applicable Standards. All individual policies are subject to same standards applicable to non-COLI products. In the group setting where where insured has either at issue or potentially at a later date some incidence of ownership in the coverage the product is also subject to the to same standards applicable to non-COLI products. However, in the group setting where the insured is never expected to have any incidence of ownership in the coverage then we will consider variance from the usual standards to extent permitted by statute and Regulation.

II. Special Filing Requirements

A. Submission Letter

1. The letter must specifically identify the submission as a COLI product preferably in the caption or "Re" of the letter.
2. The letter should state the basis under which insurable interest is determined. These would be issued pursuant to New York Insurance Law §3205(d) to fund benefits provided under an employee benefit plan (e.g., post-retirement health benefits) or §3205(a)(1)(B) for key persons.

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3. The letter should explain how the insurer will verify that the conditions required for insurable interest will be satisfied for employee benefit plan and key person corporate-owned life insurance.
4. The letter must indicate (a) whether a separate notice and consent forms that sets forth the employee's consent and termination rights as required by §3205(d)(1)(A), (B), and (C) are included in the submission or (b) whether the insurer has a previously filed or approved forms. In the case of (b) above, the submission letter must supply the form numbers, the Department file numbers, and the date(s) of approval, along with a copy of the relevant forms. The letter should state if the employer is responsible under the policy for providing the required notices to employees and whether such notices are prepared by the insurer.
5. For group life products, the submission letter must explain whether there would ever be any potential incidence of ownership, either at issue or later, transferred to the insured, with a complete explanation of the circumstances under which this could occur. Incidence of ownership is usually associated with split dollar insurance.
6. For employee benefit plan COLI, the letter should confirm that the insurer will ensure that the total amount of insurance coverage does not exceed the incurred and future costs of the plan benefit at the time coverage is issued.
7. For key person COLI, the letter should describe what, if any, steps the company takes to ensure that the amount of insurance on any key person is not excessive (i.e., exceeds the estimate of the potential loss that the corporation would incur from the untimely death of the key employee).
8. For employee benefit plan COLI, the letter should identify the provisions of §4216(b)(1) and (4) with which the forms do not comply, such as the issuance of certificates, classes covered, limited selections, participation requirements, and beneficiary restriction.
9. For employee benefit plan COLI, the letter should provide an explanation as to why the forms should be exempt from any group life insurance requirements, other than as specified in §§ 3220(d) and 4216(i).

III. Contract Provisions

A. Group Life Insurance Exceptions For Employee Benefit Plan COLI

1. General Requirements

- (a) See appropriate group life product outline for provisions that remain applicable to corporate-owned life insurance, including, but not limited to, §3220(a)(1), (2), (3), (11) and (12); §4221; § 4240; Regulation No. 77 and Circular Letter Nos. 63-4 and 83-4. Note the application should be signed by the employee (incontestability). Reinstatement provision generally not applicable.
- (b) Section 3220(d) of the Insurance Law expressly provides that the provisions of §3220(a)(4), (5), (6), (7), (8), (9) and (10) and §3220(c)(1) shall not apply to policies issued under the authority of §3205(d) of the Insurance Law. See L. 1996, c. 491, §4.

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- (c) Section 4216(i)(1) of the Insurance Law provides that §4216(d), (f) and (h) shall not apply to policies issued under the authority of §3205(d), provided that the policies are issued in compliance with §3205(d) and (e) of the Insurance Law. Such benefits are not required because the proceeds from such policies are used solely to employee benefit plans. See Memorandum in Support, New York State Senate, McKinneys Session Laws, p.A-558 (1996).
- (d) Section 4216(i)(2) of the Insurance Law provides that group insurance delivered in New York pursuant to Section 3205(d) to an employer or a trustee need not comply with the provisions of Section 4216(b)(1) or (4).
- * Note the Sections 2 through 9 below supplement the other group life outlines and provide exceptions to the general requirements.

2. Certificate Issuance Provision

- (a) The policy need not state that a certificate will be issued to the policyholder for delivery to the insured employee. A certificate containing a statement of the insurance protection to which the insured employee is entitled need not be provided to insured employees.
- (b) The insurer and employer may use certificates or some other means to account for such insurance coverage on employees. Instead of certificates, an exhibit or schedule of insured employees is made part of the policy.
 - (i) Since the employer pays all premium and insured employees have no rights under the policy, no certificate is necessary.
 - (ii) Providing certificates to the insureds in COLI cases is arguably inappropriate because it may give the insureds the mistaken impression that they might be entitled to an insurance benefit.
- (c) However, insured employees must consent to the issuance of such coverage and may terminate the coverage at any time. The initial notice and consent requirements under §3205(d) adequately protect the insured employee.
- (d) Note the requirement in §4216(b)(1) of the Insurance Law for the issuance of a certificate to the policyholder for delivery to the person insured or to such beneficiary, as evidence of such insurance, is not applicable by virtue of §4216(i)(2) of the Insurance Law.

3. Beneficiary and Facility of Payment

The provision required by Section 3220(a)(5) is not required since the employer or irrevocable trust is the beneficiary under corporate-owned life insurance policies. Section 3220(d).

- (a) The policy need not include a provision stating that the benefits payable under the policy shall be payable to the beneficiary or beneficiaries designated by the insured.
- (b) The policy need not provide that if no beneficiary is designated, then the proceeds shall be payable to the estate of the insured, or at insurer option, to one of the

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following surviving relatives: wife, husband, mother, father, child or children, brothers or sisters.

- (c) The policy may provide that the employer or trustee is the beneficiary of the policy. The policy need not provide for payment of all benefits thereunder to the person insured or to some beneficiary or beneficiaries other than the employer/policyholder. Section 4216(i)(2) excepts corporate owned life insurance from such requirement.
- (d) Since proceeds are payable to the policyholder (employer/trust), the policy need not describe any settlement options available to the insured's beneficiary.

4. Conversion Rights

- (a) Pursuant to §3220(d) of the Insurance Law, employees insured under corporate-owned life insurance policies issued under the authority of §3205(d) of the Insurance Law are not required to provide any conversion rights under §3220(a)(6), (7) and (8) of the Insurance Law.
- (b) However, employees insured under such policies can terminate such coverage at any time. Such employee must receive notice of termination rights upon termination of employment, unless such employee possesses a present or prospective right to receive any benefits under the employee benefit plan being financed, in whole or in part, by such life insurance coverage.
- (c) The notice of conversion requirement in §4216(f) is not applicable for corporate-owned life insurance. Note that the conversion requirements in §3220(a)(6), (7) and (8) are not applicable to corporate-owned life insurance by virtue of §3220(d) noted above.

5. Eligibility of New Insureds

- (a) Pursuant to Section 3220(d), the requirement in Section 3220(a)(9) that all new employees of an employer or members of the labor union or other association or eligible group or classes eligible for such insurance be added to such groups or classes for which they are eligible is not applicable.
- (b) Section 3220(a)(9) serves to ensure that new younger and healthy lives are added to the group. This requirement may not be appropriate for corporate-owned life insurance programs if the plan is adequately funded with the existing insured lives or the employer is using alternative financing methods to fund the post-retirement benefits.
- (c) The conditions imposed by Section 3205(d)(2) and (3) limiting the total amount of insurance coverage to the total costs of benefits incurred plus projected future costs and requiring the amount of coverage on each employee or retiree and selection of employees or retirees insured to be based on purely nondiscriminatory factors should protect against adverse selection.

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6. Premium Renewal Notice

Pursuant to Section 3220(d) the premium renewal notice provision is not required. For non-employee benefit plan corporate-owned life insurance group cases, Section 3220(a)(10) of the Insurance Law requires a notice in the policy to the effect that the premium for renewable term insurance depends on the attained ages of the member in the group (labor union or association) and increases with advancing age. Since employers do not use term insurance to fund corporate-owned life insurance plans, such notice is not necessary.

7. Assignment

An assignment provision is not required. Section 3220(c)(1) provides that a person whose life is insured under a group life insurance policy is permitted to make an assignment of all or any part of his incidents of ownership in such insurance, including, without limitation, any right to designate a beneficiary and any right to convert to an individual policy. Section 3220(c)(1) permits the insurer and group policyholder to prohibit or restrict the right of assignment by appropriate policy provision. Since the insured employee does not have any incidents of ownership under the policy (and does not receive a certificate) there is nothing for the insured employee to assign.

8. Dependent Coverage

- (a) Corporate-owned life insurance is not subject to the dependent coverage provisions of §4216(f) of the Insurance Law.
- (b) Since corporate-owned life insurance coverage only applies to employees of an employer, it does not appear that dependent spouses or dependent children can be covered.

9. Dividends -- Recovery of Group Policyholder/Employer Costs

The policy need not provide that dividends or rate reductions must be applied to reduce the insured's premium or distributed to the insured by the policyholder. Section 4216(i)(1) makes Section 4216(h) inapplicable.

10. Nonforfeiture Requirements For Group Life Insurance

- (a) The group policy should include provisions that address the risks of disintermediation (for products with a fixed account) and anti-selection (where employer can surrender policies of healthy employees but continue paying premiums on unhealthy employees).
- (b) Section 3220(a)(11) gives the Superintendent discretion in determining nonforfeiture requirements for group life insurance.
 - (i) Because these products are more like group insurance and even group annuities the Department recommends that these products be filed as group products so that additional protections can be implemented (e.g., downward market value adjustments, limitations on the number of surrenders in a given period of time,

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requiring complete surrender over time if more than a certain portion of the contract is surrendered).

- (ii) Group universal life insurance and variable universal life insurance are generally subject to the provisions of the Insurance Law applicable to individual products because such coverage is solely funded by employee (or member) contributions. See §4221 and Regulation 77. However, since the employer pays the full costs and the employee has no incidence of ownership, there is no reason to apply or extend the provisions of the Insurance Law applicable to individual life insurance in the COLI context.

B. Additional Provisions Pertaining To Non-Ownership Plans

In situations where the insured has no incidence of ownership, the Department may relax the review standards for such forms. Where there is a possibility that insured employees will have incidents of ownership in the corporate-owned life insurance context, individual review standards will generally be applicable, with some exceptions.

1. Free Look Provision

A free look provision at the individual employee level is not necessary if the employee would never have any incidence of ownership of the policy.

2. Restrictions on Surrenders

It is permissible to place restrictions on surrenders that are subject to IRC Section 1035 that do not apply to other surrenders.

3. Right to Exchange

The right to exchange requirement in Regulation No. 77 does not apply if the insured employee has no incidence of ownership in the policy. If the insured has incidents of ownership when the investment policy of the separate account is materially changed, then the exchange right is triggered.

4. Loans and Withdrawals

- (a) If loans or partial withdrawals are allowed under the policy, it should be clear whether they are made at the group policy level or at the individual insured level. If made at the group level, then the policy should describe how the loan or partial withdrawal and other policy benefits would be allocated to individual insureds or among insureds under a group policy.
- (b) The policy cannot permit the employer or trust (during the first five years subsequent to issuance of the policy or policies providing life insurance issued pursuant to 3205(d)) to undertake a pattern of borrowing that is likely to require all or a substantial part of the cash values of the policies to be pledged as security against repayment of such loans, unless such borrowing was incurred because of an unforeseen increase in financial obligations.

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5. Discontinuance and Termination Provisions

- (a) The individual and group policy should describe insured employees rights to discontinue or terminate coverage on their lives, the means by which such termination must be executed, and the consequences of the employee's or retiree's failure to comply with the requirements of Section 3205(e) (i.e., neither the employee, retiree nor his or her successor in interest, may contest the validity of the coverage).
- (b) The policy must state that the individual policy terminates upon the written request of the insured as of the date the notice of such request is received by the insurer. See Section 3205(e).
- (c) The policy must describe all terms and conditions relating to the amounts payable to the employer or trust policy owner as the result of such termination of coverage.
- (d) The insurer should reserve the right to terminate the group policy or individual policies if the employer selects against the insurer by surrendering healthy lives.
- (e) The policy must state that the employer must notify the insurer of the employee's request to reject, discontinue or terminate coverage.

6. Proof of Loss

The policy must contain a proof of loss provision which requires evidence that the beneficiary has an insurable interest in the insured employee at the time of the insured employee's death, such as the written consent signed by the insured and an affirmation that the insured employee did not in writing request the termination of coverage prior to his or her death.

7. Aggregate Amount of Insurance Coverage

At time coverage is issued, the total amount of insurance coverage issued to date to the employer (or trust) shall not exceed costs of employee and/or retiree benefits already incurred in connection with such employee benefit plan since the earliest date coverage on an employee or retiree was issued under §3205(d), plus the projected future cost of such benefits as established by the employer. §3205(d)(2)

- (a) The total amount of insurance coverage at issue cannot exceed the incurred and projected costs of employee benefits under an employee benefit plan.
- (b) The present value of death benefit payments must not exceed the present value of the aggregate of existing and future costs of such employee benefits.
- (c) The total amount of insurance coverage refers to the aggregate face amount of life insurance purchased at the time of issue (not the net amount at risk).
- (d) Note that the amount of insurance is also limited for key person insurance. The value of the employee is an estimate of the potential loss of net income that the corporation may incur from the untimely death of the key person.

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8. Coverage Amount and Employee Selection Factors

- (a) The amount of coverage on each insured employee or retiree and the selection of such employees or retirees to be insured must be based purely on nondiscriminatory factors, and not on conditions or terms of employment other than participation in an employee benefit plan. See §3205(d)(3).
- (b) For group corporate-owned life insurance, conditions pertaining to employment include geographic situs of employment, earnings, method of compensation, hours, and occupational duties. See §52.18(f) of Regulation No. 62 and Circular Letter 63-4 §I.B.2 of the *Guidelines For The Examination of Group Life Forms*.

IV. Insurer Responsibilities

A. Eligible Group Requirements

- 1. Section 3205(d) permit corporate-owned life insurance to be issued an employer or irrevocable trust established by an employer or by one or more employers or one or more employers and one or more labor unions.
- 2. Section 4216(i)(2) of the Insurance Law provides that any authorized life insurer may deliver group insurance policies (issued under the authority of §3205(d)) to an employer or to the trustee of a fund established by one or more employers, or one or more employers and one or more labor unions *without complying with the provisions of §4216(b)(1)*.
 - (a) This provision eliminates the certificate requirement, employer beneficiary prohibition, selections by employees and minimum number and participation requirements.
 - (b) It can be argued that only authorized insurers can avail themselves of §4216(i)(2) of the Insurance Law and only with respect to group policies delivered in this state. However, if an insurer can assure the Department of compliance with the conditions in §3205(d) and (e), the Department may consider permitting out-of-state corporate-owned life insurance coverage that provides insurance coverage on resident employees of this state under groups described in §4216(b)(1) and (4).
 - (c) The Department will not require the delivery of COLI certificates to New York resident employees in out-of-state multiple employer trust cases or prior approval of such certificates (under the deemed to be delivered language in Section 3201(b)(1)) as long as the requirements of §3205(d) and (e) are satisfied and the insured employee has no incidence of ownership.
 - (d) An unlicensed insurer cannot provide corporate-owned life insurance coverage in New York. In the corporate-owned life insurance context, direct contact between the insurer and insured employee is required to terminate coverage pursuant to §3205(e). Such contact would appear to constitute doing an insurance business in the state.
- 3. It is the insurer's responsibility to determine whether the definitional requirements in Section 4216(b) for eligible groups are satisfied. Only employer groups (or trusts

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established by such employers) described in Section 4216(b)(1) and (4) qualify for exceptional treatment.

B. New York Insurable Interest Requirement

1. It is the insurer's responsibility to determine whether the policyholder (corporation) has an insurable interest in the person or persons insured under the policy at the time of issue and, where applicable, thereafter.
2. For key person corporate-owned life insurance, the insurer must have procedures in place to ensure that the corporation/policyholder has a "lawful and substantial economic interest in the continued life, health or bodily safety of the person insured, as distinguished from an interest which would arise only by, or would be enhanced in value by, the death, disablement or injury of the insured" pursuant to Section 3205(a)(1)(B) of the Insurance Law and that the insured consents in writing to the making of such contract.
3. For employee benefit plan corporate-owned life insurance, the insurer must monitor compliance with the conditions in §3205(d) and (e) of the Insurance Law closely at and after issue of the policy to ensure that insurable interest requirements are (and continue to be) satisfied. The insurer should have procedures in place to ensure that:
 - (a) the employer receives the required consent from insured employees and notifies the insurer when an employee or retiree rejects the issuance of such insurance ;
 - (b) the employer provides the required notices upon termination of employment or termination or reduction in plan benefits or replacement of such insurance coverage;
 - (c) insured employees can exercise their statutory right to discontinue and terminate coverage after issue.