NEW YORK STATE
DEPARTMENT *of*
FINANCIAL SERVICES

Andrew M. Cuomo
Governor

Benjamin M. Lawsky
Superintendent

GROUP ANNUITY TERMINAL FUNDING AND CLOSE OUT CONTRACTS (Last Updated 9/24/2012)

This outline is current as of 9/24/2012. Subsequent changes to statutes, regulations, circular letters, etc., may not be reflected in the outline. In case of any doubt, please contact the Life Bureau.

GROUP ANNUITY TERMINAL FUNDING AND CLOSE OUT CONTRACTS (Last Updated 9/24/2012)

I. Applicability

I.A **Scope**: This product outline covers all group annuity terminal funding contracts and group annuity close out contracts.

I.B **Definitions:** The terms "terminal funding contracts" and "close out contracts" are often used interchangeably. For purposes of this outline, the terms

B.1 ***Close out contract*** refers to allocated group annuity contracts that provide for a single consideration and are used to fund terminating defined benefit plans and terminating defined contribution plans or to assume liability of certain segments of ongoing defined benefit plans, such as for terminated vested participants, or existing accrued benefits for currently active participants.

B.2 ***Terminal funding contracts*** refer to allocated group annuity contracts that are used for both defined benefit plans and defined contribution plans and provide for the purchase of annuity benefits on an ongoing basis as plan participants terminate employment (i.e., for benefit payments made as a result of retirement, disability or death).

a) Purchase of annuities for terminated vested or retired participants;
b) Funds accumulated under an alternative plan funding arrangement for active participant lives, such as a trust or certain unallocated group annuity contracts.

B.3 ***Allocated Contract*** means a contract in which deposits are credited to an accumulation fund, if applicable, and allocated to specific plan participants' accounts under the contract or to the purchase of annuity benefits for specific plan participants or their beneficiaries. See §3223(d).

B.4 ***Unallocated amounts*** means any funds credited to the accumulation fund which the insurer is not currently irrevocably committed to apply under the terms of the contract to the payment of benefits by it to specific plan participants or beneficiaries or to the purchase of annuities for specific plan participants, adjusted for any accrued experience rating charges or credits, including expenses and administrative, sales and surrender charges provided for under the contract. See §40.2(z) of Regulation 139.

B.5 ***Allocated amounts*** refers to any funds credited to the accumulation fund which the insurer is irrevocably committed to apply under the terms of the contract to the payment of benefits by it to specific plan participants or beneficiaries or to the purchase of annuities for specific plan participants, adjusted for any accrued experience rating charges or credits, including expenses and administrative, sales and surrender charges provided for under the contract.

I.C Markets

C.1. IRC 401(a) Qualified Plans

C.2 Non-Qualified Plans
a) Non-Qualified Excess Benefit Plans.
b) Non-Qualified Deferred Compensation Arrangements.

I.D Key References

D.1 Insurance Law §§ 2123, 3201, 3204, 3209, 3212, 3214, 3223, 3227, 4224, 4226, 4228(h), 4231, 4238, 4239, 4240
D.2 Regulations: Regulation 139, Regulation 34-A
D.3 Circular Letters: CL 4 (1963), CL 6 (1963), CL 1 (1964), CL 12 (1976), CL 14 (1997), CL 2 (1998), CL 8 (1998), CL 6 (2004), CL 27 (2008)

II Filing Process

II.A General Information

A.1 Prior Approval Requirement: Section 3201(b)(1) provides that no policy form shall be delivered or issued for delivery in this state unless it has been filed with and approved by the superintendent *as conforming to the requirements of the Insurance Law* (standard and generally applicable provisions*)* and *not inconsistent with law* (federal and state statutory, regulatory and decisional law).

A.2 Discretionary Authority For Disapproval: Section 3201(c)(1) and (2) permits the Superintendent to disapprove any policy form that contains provisions that are misleading, deceptive, unfair, unjust, or inequitable or if its issuance would be prejudicial to the interests of policyholders or members. See also §§2123, 3209, 4224, 4226, 4228(h), 4231, 4239.

A.3 No Filing Fee.

II.B Types of Filings

B.1 Prior Approval - Policy forms submitted under §3201(b)(1) of the Insurance Law are subject to the submission rules noted herein, especially Circular Letter Nos. 63-6 and 97-14. Submissions are generally handled on a first-in, first-out basis.

B.2 Alternative Approval Procedure - Section 3201(b)(6) and Circular Letter No. 2 (1998) provide for an expedited approval procedure designed to prevent delays by deeming forms to be approved or denied if the Department or insurer fail to act in a timely manner. Circular Letter No. 2 (1998) provides that the certification of compliance for this type of submission should make reference to any law or regulation that specifically applies or is unique to the type of policy form submitted. An alternative would be to submit a certification of compliance with the

applicable laws and regulations cited in this product outline. A statement that the filing is in compliance with all applicable laws and regulations is not acceptable.

B.3 Prior Approval with Certification Procedure - Circular Letter No. 6 (2004) provides for an expedited approval procedure based on an appropriate certification of compliance signed by an officer of the company in the format provided by Circular Letter No. 6 (2004). Certifications that have altered or otherwise modified language will not be accepted.

The original signed certification must be provided. The form number of each form and the memorandum of variable material for each form must be listed in the body of the certification. For long lists, it would be acceptable to begin the list in the body of the certification and include the rest of the list in an attachment to the certification. However, it would be unacceptable to list all of the forms in a separate attachment.

The submission letters for paper submissions and the Filing Description for submission made via the State Electronic Rate and Forms Filing system (SERFF) will need to comply with applicable circular letter and product outline guidance.

Substitution filings/follow-up correspondence with post-approval form changes requested prior to initial issuance of forms will not be permitted for Circular Letter No. 6 (2004) filings.

B.4 Out-of-State Filings

Filing Requirement for Domestic Insurers: Pursuant to §3201(b)(2), domestic insurers must file all unallocated group annuity contracts and funding agreements intended for delivery outside of the state. Since we are unaware of any terminal funding agreements or close-out contracts that are unallocated, it would appear that the out-of-state form filing requirement of §3201(b)(2) would not be applicable to these products. However, such contracts would be subject to the reporting requirement of §3201(c)(6)(B).

II.C Pre-filed Group Insurance Coverage - Circular Letter 1964-1.

C.1 Purpose. Circular Letter 64-1 permits insurers to provide or assume risk for group life and annuity coverage prior to the filing of approved forms.

C.2 Conditions For Providing Coverage Prior to Approval.

a) Immediate coverage requested by policyholder to meet specific need of policyholder.

b) Insurer has reasonable expectation of approval or acceptance.

c) Confirmation letter sent to policyholder by insurer stating:

(i) The nature and extent of benefits or change in benefits.

(ii) The forms may be executed and issued for delivery only after filing with or approval by the Department;

(iii) An understanding that, if such forms are not filed or approved or are disapproved, the parties will be returned to status quo insofar as possible, or the coverage will be modified retroactively to meet all requirements necessary for approval; and

(iv) The effective date of coverage (Best Practice).

d) Department Notification.

(i) Statement explaining circumstances and reasons for delay in submitting forms within twelve months for group annuity.

(ii) Follow-up statement every six months for group annuity until form is submitted. If reason for delay is unacceptable, Department may pursue a violation under Section 4241 for willful violation of the prior approval requirement.

C.3 Recommended Practice.

a) It is recommended that insurers notify the Department of coverage within 30 days (i.e., copy of confirmation letter) of coverage and submit forms within six months, notwithstanding the twelve month period noted in Circular Letter 64-1. (Best Practice).

Insurers should review pre-filings periodically (monthly) to verify compliance with conditions for pre-filing.

b) Insurers should vigorously pursue approval of pre-filed cases after forms have been submitted to mitigate harm if forms are found not to comply with applicable requirements.

II.D Preparation of Forms. Circular Letters 1963-6 and 1963-4.

D.1 Duplicates - Filings, except for SERFF, need to be made in duplicate. §I.E.7 of Circular Letter 63-6.

D.2 Form Numbers - Form numbers need to appear in lower left-hand corner of the cover page of the form. §I.D. of Circular Letter 63-6. The lower left-hand corner of the subsequent pages of the form should either contain the same form number as appears on the cover page or should be left blank. The subsequent pages should not contain form numbers that differ from the form number on the cover page.

D.3 Hypothetical Data - All blank spaces for policy forms need to be filled in with hypothetical data. § I.E.1 of Circular Letter 63-6.

D.4 Application - If an application will be attached to policy, it must be submitted with the contract for approval. If previously approved, the submission letter should so indicate. §I.E.4 of Circular Letter 63-6.

D.5 Final Format - Policy forms submitted for formal approval should be submitted in the form intended for actual issue. §I.F.1 of Circular Letter 63-6.

D.6 Submissions Made on Behalf of Company - If a filing is made on behalf of the company by another party, a letter of authorization from the company must be submitted by the party authorized to submit the filing.

D.7 Incorporation by Reference - All incorporations by reference should be attached to or accompany the submission. See also Section 3204.

II.E Submission Letters/SERFF Requirements

E.1 Caption Requirement – For paper filings, the "re" of the submission letter must identify each form and the memorandum of variable material for each form that is being submitted for approval or filed for informational purposes and must be in compliance with Circular Letter No. 8 (1999). Section 3201(b)(6) ("Deemer") filings must be identified in the "re" or caption. Circular Letter No. 6 (2004) filings must be identified in bold print in the body of the submission letter or in the "re" or caption.

For SERFF filings, please see the guidance available on the Department's website at http://www.dfs.ny.gov/insurance/serflife.htm

E.2 Submission Letters/SERFF Filing Description -- Circular Letter No. 6 (1963) §I.G

a) For paper submissions, the submission letter must be submitted in duplicate and signed by a representative of the company authorized to submit forms for the company.

b) For SERFF submissions, the Life Bureau no longer requires that a separate signed cover letter be included with submissions. Instead, any information that would ordinarily be included in the signed Cover Letter must be placed in the SERFF Filing Description. Inclusion of "Please see cover letter" or phrases of similar intent in the filing description section will not be considered as meeting filing requirements.

Note: References in this outline to submission letter content requirements are also requirements for the SERFF Filing Description.

c) Advise as to whether or not the form is replacing a previously submitted form. If there have not been a substantial number of changes, submit a highlighted copy showing the material differences or changes made to the form. If the changes are too extensive, then a highlighted copy is not required, but the changes must be identified in the submission letter. State whether the previously submitted form was approved, disapproved, withdrawn or otherwise disposed or is still pending approval (under review) with the Department and provide the form number and file number of the such form.

If a form submitted for approval had previously been submitted for preliminary review, a reference to the previous submission and a statement setting out either (a) that the formal filing agrees precisely with the previous submission or (b) the changes made in the form since the time of preliminary review. Submit a highlighted copy showing the differences or changes made to the form. A redlined copy is helpful.

If a form is intended to replace a very recently approved form because of an error found in the approved form and the approved form was not issued, the insurer may request to make a substitution of the approved form. The substitution request letter must confirm that the form has not been issued. The insurer may, under these circumstances, use the same form number on the corrected form being submitted. If the original form was approved in paper format the insurer must also return the stamped original of the approved form to the Department. If, however, the form has been issued, the insurer must place a new form number on the corrected form and need not return the previously approved form. This option is not available for policy forms approved under Circular Letter 6 (2004) filings.

d) If the form being submitted is other than a contract (i.e. rider, endorsement, or insert page), give the form number of the contract with which it will be used, or, if for more general use, describe the type or group of such forms as well as whether the pending form(s) will be used with new and/or previously issued/delivered contracts.

e) When the policy form is designed as an insert page form, the insurer must submit a statement of the mandatory pages which must always be included in the policy form, and a list of all optional pages, if any, including application forms, together with an explanation of how the form will be used (previously approved forms should be identified by form number and approval date). We object to a company's use of the matrix approach that identifies benefit provisions within a document with separate form numbers. See Circular Letter No. 6 (1963) § I.G.8. and Circular Letter No. 4 (1963) § I.A.2.

f) Statement as to how the form will be used as described in Circular Letter 1976-12.

g) Description of benefits/coverage provided. Circular Letter No. 6 (1963) § I.G.2 and 7.

h) Statement describing the type of pension plan or other program funded by the contract.

i) Submission letters should be as detailed as possible explaining the need for the product, any unique features and any special market or intended use of the form.

j) If the contract provides commutation benefits the letter must so indicate.

k) If the form does not comply with a specific product outline provision or if the Company has an alternate interpretation of a product outline provision, the submission letter must identify the provision and provide a complete explanation of the Company's position on the issue. Such submissions may not be submitted through the Circular Letter 6 (2004) certified process unless the Department has given permission.

l) Filings that are incomplete or do not comply with laws and regulations will be closed. See Circular Letter No. 14 (1997). Note a product that does not comply with a specific product outline requirement or which is considered a substantive noncomplying product will be a factor in determining whether a file will be closed, unless a noncompliance explanation is included in the submission letter.

m) If the form has been previously submitted to the Department and the file was closed or withdrawn, any resubmission of the annuity to the Department must be complete by itself, reference the file number of the previously closed file and address all outstanding issues in the new submission letter.

II.F Attachments To Submission

F.1 Memorandum of Variable Material

a) The submission must include a separate detailed Memorandum of Variable Material to explain any variable material in the policy forms. The Memorandum of Variable Material should be drafted in sufficient detail to determine the scope of variation for each variable item. Where text is variable, the memorandum should include alternative text and/or an explanation of when the bracketed text will be omitted from the form. Similarly, variable numerical items should include the range (i.e. minimum and maximum) of variation. It should be clear which item in the explanation corresponds to which variable item in the form. One option would be to number the items in the explanation of variable material and place the number of the item from the explanation next to the corresponding variable item in the form.

The Memorandum of Variable Material is subject to approval and must comply with all substantive and procedural filing guidance issued by the Department.

b) Open-face riders or endorsements may be filed for general use in amending illustrative or variable material within the scope of the approved memorandum of variable material for the form being amended. The memorandum of variability should include an explanation to that effect.

c) Contracts are typically submitted on a single-case basis for a particular contract holder. If a contract is submitted on a single-case basis, extensive variability would not be expected. All large cases (i.e. greater than $2.5 Billion) must be submitted on a single-case basis due to the risks associated with contracts of that size.

F.2 Flesch Score Certification -- Readability Requirement

a) Provide a Flesch score certification signed by an officer of the company in accordance with Section 3102. The Flesch score must be at least 45. Please refer to the Department's February 18, 1982 letter, available on the Department's website, for a sample certification.
http://www.dfs.ny.gov/insurance/life/guidance/3102Intro.doc

b) Section 3102(b)(1) excludes

(i) any certificates issued pursuant to a group life or accident and health insurance policy or group annuity contract issued to an employer covering persons employed in more than one state,

(ii) any group insurance policy covering a group of one hundred or more lives, other than dependents, at the date of issue, provided that this exclusion does not apply to certificates delivered or issued for delivery in this state.

(iii) any group annuity contract which serves as a funding vehicle for pension, profit sharing or deferred compensation plans; provided that this exclusion does not apply to any certificate issued pursuant to such group annuity contract.

F.3 Group Annuity Summary Sheet

A completed summary sheet must be included with the submission regardless of the submission method. The summary sheet is available on the Department's website at

http://www.dfs.ny.gov/insurance/life/product/ga_summary_08032012.pdf

III. Eligible Group Requirements

III.A Definitions

A.1 ***Group Annuity Contract*** means any policy or contract, except a joint, reversionary or survivorship annuity contract, whereby annuities are payable dependent upon the continuance of the lives of more than one person. Section 4238(a).

a) We view group contracts that provide for the purchase of annuities or the payment of annuity benefits for plan participants or their beneficiaries to be group annuity contracts

b) The terminology used in Sections 3223 and 4238 was drafted to apply to group deferred annuity contracts which are rarely sold today.

c) Plans funded by group annuity contracts include 401(a), 401(k), 457, 414(d), and 403(b), among others.

A.2 ***Contractholder*** means the party or parties to whom or to which the contract is issued. Section 4238(a).

A.3 ***Annuitant*** refers to any person upon whose continued life such annuity is dependent. Section 4238(a).

A.4 ***Participant*** means any employee or former employee of an employer, or any member or former member of an employee organization, who is or may become eligible to receive a benefit of any type from an employee benefit plan which covers employees of such employer or members of such organization, or whose beneficiaries may be eligible to receive any such benefit. See §3(7) of ERISA.

A.5 ***Annuities*** means all agreements to make periodical payment for a period certain or where the making or continuance of all or some of a series of such payments, or the amount of such payment depends upon the continuance of human life. Section 1113(a)(2).

A.6 ***Employee*** may include retired employees, employees of affiliates and subsidiaries of the employer, individual proprietors affiliated with the employer, and partners and employees of individuals affiliated with the employer and of firms controlled by the employer. §4238(c).

III.B **Types of Contractholders -** It is the insurer's responsibility to determine whether the definitional requirements in Section 4238(b) for an eligible group are satisfied at the time of issue and thereafter. The insurer should determine whether all employees or members eligible are covered.

1. **Employer/Employee** - Section 4238(a)(1)
2. **Employer Association** - Section 4238(a)(2)
3. **Labor Union** - Section 4238(b)(3)
4. **Employer/Labor Union Trust** - Section 4238(b)(4)
5. **Association (common interest, calling, profession)**- Section 4238(b)(5)
6. **IRA** - Section 4238(b)(6)
7. **Other Employer Trust** - Section 4238(b)(7)

8. **Foundation or Endowment Fund -** Section 4228(b)(8)
9. **Affinity Association** - Section 4238(b)(9)
10. **Financial Institution** - Section 4238(b)(10)
11. **Plaintiffs or Claimants** - Section 4238(b)(11)

III.C Non-Recognized Groups

Section 4238 was not modernized to permit Discretionary Groups like those permitted for group life insurance in Section 4216(b)(14) and for group accident and health insurance in Section 4235(c)(1)(M). As such, groups that fail to satisfy the definitional requirements in Section 4238(b) of the Insurance Law are not recognized groups under the Insurance Law. Such group annuity contracts cannot be delivered in this state. However, certificates covering New York residents under such group annuity contracts delivered out-of-state must be delivered in this State pursuant to Section 3219(b). Group annuity certificates delivered in this state that are funded solely by individual contributions must comply with the provisions of the Insurance Law applicable to individual annuities. Such certificates should be submitted for review and approval. The group annuity contract should be submitted as well. It will be reviewed to ensure that the contract and certificate are not inconsistent. The contract cannot include provisions that invalidate or impair the terms of the certificate.

III.D Unauthorized Insurers

D.1 Section 1101(b)(1) prohibits unlicensed insurers from doing an insurance business in this state by mail or otherwise.

D.2 Section 1101(b)(2)(B) provides an exception (referred to as the "group exception") to the prohibition in Section 1101(b)(1) for certain types of group insurance issued outside of New York.

The group exception applies to group annuity contracts where the group conforms to the definitions of eligibility in §4238(b) of the Insurance Law, except paragraphs (6) and (7), and the master contracts were lawfully issued without this state in a jurisdiction where the insurer was authorized to do an insurance business.

D.3 Section 1101(b)(2)(B) excepts from the group exception to the mail order prohibition any transaction with respect to a group annuity contract used in the individual insurance market noted above, including

a) IRC §408 contracts (IRAs);
b) IRC§403(b) (Tax Sheltered Annuities), and
c) Plans under which payments are derived wholly from funds contributed by the persons covered thereunder. See L.1978, c.428.

D.4 As such, any New York certificate funded solely by employee or individual contributions is subject to prior approval.

IV Contract Provisions

IV.A Cover Page of the Contract and Certificate

A.1 Company's Name and Address

a) The New York licensed insurer's name should appear on the cover page (front or back).

b) Full street address of the company's Home Office (bracketed or underlined to reflect possible future changes) for disclosure purposes on the front or back cover page of the contract. For changes applicable to new business, an information filing is required. For changes applicable to existing business, an endorsement setting forth the new address must be submitted for approval and sent to all holders of in-force contracts. Please refer to the guidance available on the Department's website.

c) In addition to the home office address, the full street address of the administrative or service office (if different than the home office address) may be set forth on the front or back cover of each contract. The administrative or service office address, if any, should be bracketed or underlined to reflect possible future changes. (An informational filing is required for such changes.)

d) If the name of another entity is included on the cover page (insurance group designation, name of the licensed parent company or licensed affiliate, etc.) or if a logo, trademark or other device is included, such name or device shall not be displayed in a manner that would have a tendency to mislead or deceive as to the true identity of the insurer, or create the impression that someone other than the insurer would have any responsibility for the financial obligations under the contract. §3201(c)(1). This would apply to applications as well.

A.2 Form Identification Number -- A form identification number (consisting of numerical digits, letters, or both) must appear in the lower left-hand corner of the cover page in accordance with §I.(D) of Department Circular Letter No. 6 (1963). (Each form number should be sufficiently unique so as to distinguish the form from all others used by the insurer.)

A.3 Brief Description of Contract – Participation Status and Variability

a) A description of the contract, such as "Terminal Funding Contract" or "Close Out Contract".

b) There must be a statement indicating whether the contract is participating or nonparticipating.

A.4 Officer's Signatures

a) The signature of at least one officer of the company is needed to execute the separate account group annuity contract or funding agreement as a matter of contract law.

b) Signatures should be denoted as variable material.

c) When the signature is changed, the insurer should notify the Department for informational purposes. The contracts do not need to be re-filed.

IV.B Standard Provisions: §3223

Every group annuity contract delivered or issued for delivery in this state and every certificate used in connection therewith shall contain in substance the following provisions to the extent that such provisions are applicable or provisions which are more favorable to the annuitants, or not less favorable to annuitants and more favorable to the contractholders:

B.1 Grace Period-§3223(a)-There shall be a 31-day grace period following the due date of any required payment after the first payment within which the payment may be made. During such grace period, the contract shall continue in full force.

a) This provision has no application to single consideration close out contracts.
b) It does apply if a payment is required to pay any fee or expense charges.
c) If the contract continues in force without penalty, no grace period provision is necessary.
d) See liquidated damages provision below. IV.C.5.

B.2 Entire Contract-§3223(b)-A provision specifying the document or documents, which shall include the contract and, if a copy is attached thereto, the application of the contractholder, constituting the entire contract between the parties. See also §3204.

a) An attachment to the contract listing plan participants and/or their beneficiaries with the benefit amount, commencement date and type of annuity benefit should be submitted with the form. The sample attachment should include sufficient illustrative variable material for the Department to ascertain what information will be included in the list when the contract is issued.

b) For terminal funding agreements, if an insurer uses participant specific certificates in lieu of a benefit list in the contract then the entire contract provision in the contract must indicate that the certificates are part of the entire contract..

B.3 Misstatement of Age or Sex-§3223(c)-A provision for the equitable adjustment of the benefits payable or of the payments to be made to the insurer if the age or sex of any person, or of any other fact affecting the amount or date of payment by or to the insurer has been misstated.

a) The *Arizona vs. Norris* decision held that Title VII of the Civil Rights Act of 1964 prohibits an employer from offering its employees a retirement benefit option where a women is paid a lower monthly retirement benefit than a man who has made the same contributions.

b) We have permitted misstatement provisions that omit the reference to sex.

c) §3219(a)(5) requires that the interest rate to be charged or credited to underpayments and overpayments be specified in the contract and cannot exceed six percent. . (Best Practice)--*The §3223(c) provision should also state whether and how much interest will be charged against or credited to such underpayments and overpayments. The rate must be the same for overpayments and underpayments. We may question any rate above six percent.*

B.4 Retired Life Certificate-§3223(e)-A provision stating that the insurer shall issue for delivery to each person to whom annuity benefits are being paid thereunder a certificate setting forth a statement in substance of the benefits to which such person is entitled under the contract.

a) The retired life certificate should include the following provisions:

(i) Entire contract provision.
(ii) Misstatements provision.
(iii) A provision identifying the insurer, including the mailing address.
(iv) A provision describing the annuity benefit and any limitations, if any, on the insurer's guarantees with respect to such benefit, including the amount and frequency of annuity payments, the minimum number of payments, any refund features and survivorship rights, etc.
(v) A facility of payment provision. Note that such provision should not conflict with Article 81 of the New York Mental Hygiene Law and the Americans with Disability Act. In New York, until a person is found to be legally incompetent to handle annuity payments and no guardian has been appointed, the insured is entitled to such payments.
(iv) A beneficiary provision.

b) The retired life certificate should be submitted for review, unless a previously approved certificate will be used. In such case, the submission letter should specify the form number, file number and approval date. Please note that retired life certificates are considered policy forms as defined in §3201(a).

B.5 No Active Life Certificate Required. Note that no active life certificate is required for terminal funding and close out contracts because the contract does not provide for the maintenance by the insurer of one or more accounts for each plan participant/annuitant. See §3223(d).

IV.C Regulation No. 139 And Other Provisions

C.1 General Note

a) Pursuant to §40.1(a)(3) of Regulation No. 139, only the disclosure rules in Section 40.3 apply to group annuity contracts under which funds received by the insurer are immediately applied to the purchase of immediate and deferred annuities.

b) Furthermore, since Section 40.5(a) only applies to unallocated amounts, the contract termination rules in §40.5 do not apply to close out and terminal funding contracts because such contracts do not include any unallocated amounts.

c) However, to the extent that an insurer uses a single contract to fund immediate and deferred annuity payments as well as an active life fund rather than a separate terminal funding contract or close out contract, the contract provisions should not conflict with the provisions in Regulation No. 139. The provisions noted below are listed primarily for reference purposes.

C.2 Plan Benefit Rule -- §40.4(a) of Regulation 139 – Any contract issued in connection with a defined contribution plan which provides the contractholder with the right to withdraw from the contract the amounts required to pay lump sum benefits of the participant's individual account balance as they arise in accordance with the provisions of the plan upon bona fide termination of employment must provide for such withdrawals to be made on a basis pursuant to which neither the amount withdrawn from the contract nor the amount of the remaining principal balance of the accumulation fund following such withdrawal is adjusted to reflect changes in interest rates or asset values since the receipt of funds.

Terminal funding contracts and close out contracts do not give annuitants the right to withdraw funds once annuity payments have commenced.

C.3 Betterment of Rates -- §40.4(b) -- For any group annuity contract funding a defined contribution plan, the contract must provide that any annuity benefit purchased with respect to an amount equal to the plan participant's account value as determined at the time of its commencement shall not be less than that which would be determined by the application of such amount to purchase a single consideration immediate annuity offered by the company to the same class of contracts.

a) The betterment of rates provision ensures that annuities will be purchased on a new money basis.

b) For single consideration close out contracts, a betterment of rates provision is not necessary because the contractholder will seek the lowest responsible price.

c) For terminal funding contracts that allow for subsequent purchases of annuity benefits as plan participants terminate their employment and retire, a betterment of rates provision is not necessary if the contractholder can shop around for the lowest price (defined benefit plans) or the highest benefit (defined contribution plan).

C.4 Bona Fide Termination of Employment -- §40.4(f) – The contract can include procedures or conditions in order to establish that a requested contractual withdrawal is being made in accordance with a bona fide termination of employment and in accordance with the plan provisions.

a) Termination of employment means the cessation of an employment relationship with an employer, multiple employer or membership in an employee organization sponsoring the plan, including cessations due to retirement, death, and disability.

b) Termination of employment does not include:

(i) Any temporary absence,

(ii) A change in position or other occurrence qualifying as a temporary break in service under the plan,

(iii) Transfer or other change of position resulting in employment by an entity controlling, controlled by, or under common control with the employer,

(iv) Cessation of an employment relationship resulting from a reorganization, merger, or sale or discontinuance of all or any part of the plan sponsor's business. The risk for these transactions is typically not considered by the insurer in making the guarantees provided in the contract. Such transaction may result in unexpected withdrawal activity that was not priced for when the contract was issued.]

(v) Plan termination or partial plan termination.

C.5 Liquidated Damages Provision -- §40.2(m) of Regulation 139 defines liquidated damages as the charges or adjustments which may become applicable in the event contributions are not made in the amounts or on the dates specified in the contract and which reasonably reflect the actual losses anticipated by the insurer in making commitments in advance of the receipt of the specified contributions. A liquidated damages provision is an alternative to contract termination in the event that the contractholder fails to make a scheduled contribution.

a) For most close out and terminal funding contracts this provision is not applicable, since additional contributions are not required.

b) We have objected to provisions that provide for a fixed charge or fixed interest rate reduction for any such failure to contribute.

c) The method for calculating the charge should be set forth in the contract. The contractholder should be able to calculate the adjustment from the terms of the contract. Many insurers use an explicit formula similar to the market-value adjustment formula.

C.6 Purchase Rate Guarantee -- Unilateral Change. For terminal funding contracts, the mortality and interest basis for guaranteed purchase rates should be stated in the contract. Companies can make unilateral changes in guaranteed annuity purchase rates for new contributions.

C.7 Involuntary Cashout. ERISA §203(e)(1) and IRC §411(a)(11) provide for a $5000 threshold amount for annuity payments. The contractholder/plan sponsor may decide to pay the participant a lump sum, in lieu of a small annuity.

IV.D Participating and Nonparticipating Contracts – Dividend Provisions

D.1 General Note – Participating annuity contracts differ considerably from the nonparticipating annuity contracts typically used to close out terminated plans.

a) Under a typical nonparticipating annuity, plan assets are paid to the insurer which assumes the obligations to make benefit payments under the terminated plan. All actuarial experience under the arrangement whether favorable or not, is borne by the insurer and no additional funds are paid to or from the plan's trust or the employer with respect to those plan benefits.

b) Under a participating annuity contract an ongoing relationship is created between the contractholder (the plan's trust or the employer) and the insurance company. The cost of the participating annuity contract is more than the cost of the nonparticipating annuity. In return for the payment of the additional amount, the contractholder is entitled to receive funds (dividends) resulting from favorable actuarial experience under the contract (e.g., investment gains or higher than expected mortality). In some participating contracts, the insurer establishes a separate account for assets under the contract.

D.2 Non Participating Immediate Annuities – §4231(e)(1). Pursuant to §4231(e)(1), any policies or contracts described in §4231(g)(2) and deferred annuity providing a period of deferment of annuity payments not in excess of one year can be issued on a nonparticipating basis.

a) As such, immediate annuity contracts and deferred annuity contracts providing a period of deferment of annuity payments not in excess of one year can be issued on a nonparticipating basis pursuant to §4231(e)(1).

b) A mutual insurer does not need acquire a revocable permit to issue such nonparticipating contracts.

c) Since payments to annuitants usually commence immediately in close out contracts and terminal funding contracts, the contracts can be and usually are written on a nonparticipating basis.

d) Close out contracts and terminal funding contracts are almost always written on a nonparticipating basis. We would raise questions if a close out or terminal funding contract used in connection with a defined contribution plan was written on a participating basis. For defined contribution plans, it is clear that any participating feature should benefit the plan participant/annuitant rather than the group annuity contractholder.

D.3 Plan Termination – Guaranteed Cost Nonparticipating Deferred Annuities §4231(g)(2). Section 4231(g)(2) provides, in part, that dividends need not be distributed on:

a) Any deferred annuity contract for the period following the period of deferment of annuity payments, nor

b) On any group annuity contract providing deferred annuities

(i) for a class or classes of participants in a qualified pension or profit sharing plan who have terminated their participation under such plan, or

(ii) with respect to which class or classes further contributions have been discontinued under the plan and notice of such discontinuance has been given

to the commissioner of internal revenue (or regulatory authority of such other jurisdiction). See Chapter 752 of the Laws of 1961 and Chapter 90 of the Laws of 1966.

c) By virtue of §4231(g)(2), an insurer can issue guaranteed cost nonparticipating immediate and deferred annuities in connection with the termination of pension plans or termination of a class or classes of participants in a pension plan.

d) The Department has approved the use of guaranteed cost nonparticipating deferred annuities in connection with corporate acquisitions and mergers where benefit accruals are frozen and future pension accruals are funded under the surviving corporation's pension plan. A single premium guaranteed cost nonparticipating deferred annuity is used to fund the "frozen" accrued benefits under a defined benefit plan (for retired participants, vested terminated participants and active participants) and to irrevocably fix the cost of plan benefits accrued to a specified date.

(i) The insurer assumes the liability of the accrued benefits as determined as of a specified date in accordance with plan requirements;

(ii) The insurer determines a present value of such accrued benefits using then current mortality and interest assumptions to arrive at a guaranteed purchase price. The consideration for the contract is payable in single sum subject to adjustment upon receipt of final employee benefit data.

(iii) Since the pricing assumptions are not conservative in nature as is the case with traditional participating insurance products, it is not expected that any significant dividends will accrue.

e) The Department has approved the use of guaranteed cost nonparticipating deferred annuities in connection with the settlement of defined benefit plan liabilities by plan sponsors pursuant to the Financial Accounting Standards Board's Statement of Financial Accounting Standards Codification Topic 715.

(i) While there may not be a technical termination of the entire plan as envisioned by the current language in §4231(g)(2), the settlement of accrued benefits as of a specified date could be viewed as a "freeze" of the plan sponsor's liability for pension benefits.

(ii) From a defined benefit plan participant's viewpoint, the issuance of a guaranteed cost nonparticipating annuity contract will not adversely affect retirement benefits.

D.4 Participating Contracts. For terminating defined benefit plans that use immediate participation guarantee contracts to fund annuity payments for retired lives, please consult the Immediate Participation Guarantee and Deposit Administration Contracts product outline available on the Department's website.

a) IRS Memorandum dated February 27, 1987 provides that the employer and insurer must certify that the participating annuity contract provides

(i) For payment of all plan benefits on a termination basis, except for benefits satisfied in a single sum,

(ii) That the insurer's obligation to individuals under the contract is irrevocable and not conditioned upon the experience under the contract,

payment of subsequent premiums, or the sufficiency of assets in any separate account, and

(iii) That the plan participants under the contract have equivalent and legally enforceable rights to the general assets of the insurance company as have participants in a traditional annuity in the event separate account funds are exhausted or the insurance company becomes insolvent.

b) If residual assets are to be distributed to plan participants, a participating annuity contract may be purchased to satisfy the requirement that annuities be provided by the purchase of irrevocable commitments. However, the portion of the price of the contract that is attributable to the participation feature may not be (i) taken into account in determining the residual assets; or (ii) paid from residual assets allocable to participants. See PBGC Reg. §4041.28(c)(4).

V. Advertising and Disclosure

V.A Regulation 139 - Section 40.3

A.1 Written statement and/or specimen contract with a statement citing location in contract of disclosures required by paragraphs (1),(3),(4),(5),(6),(9) and (10) of §40.3(b) of Regulation 139. See §40.3(a)

a) Statement indicating any restrictions as to amount and timing of contributions, and penalties for non-payment. §40.3(b)(1)

b) Description of the right to discontinue contributions to contract, and penalties resulting from such action. §40.3(b)(2)

c) Statement of all current fees and charges that are or may be assessed against the contractholder or deducted from the contract, including a description of the extent and frequency to which such fees and charges may be modified and the extent to which they take precedence over other payments. §40.3(b)(3)

d) Statement of the interest rates and/or method of determination of rates and a description as to how any withdrawals, transfers or payments will affect the amount of interest credited. §40.3(b)(4)

e) Description of expense, interest and benefit guarantees under the contract and any rights to modify or eliminate such guarantees, including the right to apply surrender charges or market-value adjustments to plan benefit payments if there are plan amendments or changes in the manner of plan administration. .§40.3(b)(5)

f) Description of the contractholder's and participant's right to withdraw funds (or apply to purchase annuities), along with a description of any charges, fees or market-value adjustments applicable to such withdrawals or a statement that no such withdrawals or payment are permissible prior to maturity or the happening of a certain event. §40.3(b)(6)

g) Statement indicating any pro rata, percentage or other limitations which may apply to benefit payments to be purchased or provided under the contract when the plan is not funded entirely under the contract. §40.3(b)(7)

h) Statement that contractholder or participant withdrawals under the contract are to be made in a FIFO or LIFO basis or other applicable basis. §40.3(b)(8)

i) Statement that the contract may be amended, including any right of the insurer to unilaterally amend the contract. §40.3(b)(9)

j) Statement, if applicable, that any dividends and experience rate credits are subject to the insurer's discretion. §40.3(b)(10)

k) Statement, if applicable, concerning supporting asset's affect on withdrawal timing. §40.3(b)(11)

l) Statement that the contractholder or plan sponsor is solely responsible for determining whether the contract is a suitable funding vehicle. §40.3(b)(12)

m) Statement, if applicable, that the insurer does not have responsibility to reconcile participants' individual account balances with the accumulation fund balance where the insurer does not maintain individual account balances. §40.3(b)(13)

A.2 In general, terminal funding contracts and close out contracts should disclose the information in subsections (a), (b), (e), (i), (j) and (l) above.

V.B **Rules Governing Advertisements of Life Insurance and Annuity Contracts**

See Regulation 34-A.

V.C **Pension Benefit Guaranty Corporation (PBGC)**

The PBGC may require additional disclosure for participants and beneficiaries. The Department recommends that insurers review any available PBGC regulations and guidance, particularly where the insurer is providing administrative services to the plan.