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COLI MECHANICS: WHY AGGREGATE FUNDING?

Corporate-owned life insurance ("COLI") is a financing alternative widely utilized by public and private companies, financial institutions, banks and insurance companies as a means of financing executive benefit obligations. When companies purchase policies on the lives of their executives – namely, the eligible participants in a non-qualified plan – they pay the premium, own the cash value of the policy, and are the beneficiary of the insurance.

The majority of COLI acquisitions are structured in a manner referred to as "aggregate funding," which equalizes the COLI premiums or death benefits across the entire population of Plan participants.

Why is aggregate funding the recommended approach?

- **Creates a more efficient structure to finance plan liabilities –** An aggregate funding strategy provides for the flexibility to allocate COLI premiums as a whole, which produces more reliable premium streams. If COLI policies were purchased for and linked to each individual plan participant, it could result in erratic and inconsistent premiums, which can increase costs and make the policies inherently inefficient.
- **Consistency** – Aggregate funding allows a company to structure the COLI in a manner that applies equal premiums or death benefits across all insureds, which eliminates issues/questions as to why a policy on one employee is different than another of comparable age/status.
- **Streamlines insurability –** Aggregate funding enables carriers to issue COLI policies on a Guaranteed Issue basis without the employees having to provide any medical information. A funding strategy whereby individual policies are purchased on each and every Plan participant to fund individual liabilities may require medical underwriting, a time-consuming and intrusive requirement that introduces risk of participants being declined for coverage.
- **Mitigates future changes to eligible pool –** Aggregate COLI funding typically reduces the number of policies (currently and in the future) that are purchased to cover plan liabilities. This, in turn, can help a company better manage plan changes and avoid the cost of liquidating policies on terminated employees.
- **Designed to maximize COLI performance –** Aggregate funding enables plan sponsors to have some level of control over whom they choose to insure by allowing them to eliminate higher-risk participants. Rather than having to link coverage to every individual in the NQDCP, aggregate funding enables COLI to be thoughtfully limited to only those NQDCP participants who can help maximize COLI performance.
- **Simplifies administration –** Aggregate COLI funding helps with limiting the number of reallocation transactions as rebalancing and reallocations are completed in the aggregate, not individually.

In addition to the points outlined above, aggregate funding serves to help ensure that COLI is *informally (not formally)* funding the benefit liability.

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