

# Seventh Circuit: Profit-Related Considerations OK in Setting COI Rates

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In December, insurers battling challenges to their exercises of discretion in setting non-guaranteed elements in universal life policies received a boost when the Seventh Circuit, via companion opinions, affirmed the dismissals of breach of contract actions by plaintiffs targeting the insurers' cost of insurance (COI) rates. In both *Norem v. Lincoln Benefit Life Co.*, and *Thao v. Midland National Life Ins. Co.*, the court interpreted COI provisions that provided rates must be "based on" certain identified factors, and subject to maximum guarantees. The plaintiffs – both represented by the same law firms – had alleged that the insurers could only consider factors expressly identified in the policies, such as issue age, sex, policy year, and payment class. Plaintiffs argued that other pricing considerations such as profit margins were, by their absence from the contracts, forbidden. But after consulting dictionary definitions of the term "based on" to discern its plain and ordinary meaning, the Seventh Circuit concluded in *Thao* that "when the policy says that the monthly COI rate will be 'based on' specified factors, it does not mean that the rate will be based exclusively on those factors. ... Rather, it signifies that the named factors will have a significant, foundational role in determining the rate." The Seventh Circuit also weighed in on competing COI rulings presented by the parties, ultimately recognizing that cases cited by the insurers, which "hold generally that absent a promise to use a specific formula when calculating a COI rate, an insurer is not bound to consider *only* those factors listed in a COI provision," were "more convincing." Indeed, in rejecting them, the *Norem* court said that the cases proffered by the plaintiffs "imply that a for-profit life insurance company should not be allowed to make a profit on its COI rates. This approach, however, seems disconnected from the reality of insurance. ... [I]t is not unreasonable in a universal life insurance policy to consider profit as a secondary factor in calculating the COI rate."

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