

MEMO# 22949

October 2, 2008

ICI Comment Letter on FINRA Proposal Regarding Communications About Variable Insurance Products

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TO: VARIABLE INSURANCE PRODUCTS ADVISORY COMMITTEE No. 27-08 RE: ICI
COMMENT LETTER ON FINRA PROPOSAL REGARDING COMMUNICATIONS ABOUT VARIABLE
INSURANCE PRODUCTS

As we previously informed you, FINRA has requested comment on a proposed rule change to modify, simplify, and codify the guidance governing communications with the public about variable insurance products. [\[1\]](#) Specifically, the proposal would change guidelines on illustrations of tax-deferred versus taxable compounding in advertising and sales literature; shorten and simplify existing provisions regarding product identification, liquidity, and guarantee claims; address changes in variable insurance products and the manner in which they are advertised, particularly with regard to riders and hypothetical illustrations; and, require that all marketing materials clearly identify the type of variable product that is being discussed. The Institute's comment letter is attached and summarized below.

The Institute's Comment Letter

The comment letter supports FINRA's proposal governing communications about variable insurance products, noting that its implementation would advance consistent disclosure to variable contract owners, provide an accurate basis for comparing different products, and assist in portraying a balanced picture of variable insurance products overall.

Pre-Dated Performance

The letter supports the provision in the proposal that would permit presentation of Pre-Dated Performance subject to certain conditions. It explains that investors are interested in assessing the performance of an underlying fund from its inception and not simply from the date of its inclusion as an investment option through a variable insurance contract. The letter seeks clarification, however, on several of the proposed conditions.

Requirement to Accompany Pre-Dated Performance with Certain Standard Performance

The comment letter requests guidance from FINRA on the application of the proposal to variable annuities and to variable life policies. With respect to variable annuities, it seeks clarification that it was not FINRA's intention to require Pre-Dated Performance to be accompanied by non-charge-adjusted investment option performance from the availability date. If that was the intended interpretation, however, the letter expresses the Institute's opposition to the requirement because it would mandate a new type of performance that has not been included in Pre-Dated Performance presentations. With respect to variable life policies, the comment letter seeks confirmation that Pre-Dated Performance presented in such communications would not be required to be accompanied by any form of investment option performance for the period commencing on the separate account "availability" date.

Deduction of Maximum Guaranteed Charges

The letter supports the proposed exclusion of optional rider charges from the definition of maximum guaranteed charges. The letter states that it is inappropriate, however, to require the maximum charges possible under a contract to be deducted in calculating Pre-Dated Performance in situations where the current charges are lower.

Availability of Investment Option

The letter explains that the proposal would prohibit a communication including Pre-Dated Performance from including the performance of a fund that is not available as an investment option through the separate account. The letter notes that the guidance provided in Notice 08-39 regarding the intent of the proposed prohibition – that it would not permit the presentation of the performance of a similar "clone" fund – provides useful clarity, and requests that similar guidance be provided in the proposal as to what types of funds or other accounts could be permitted.

Significant Changes in Investment Options

The comment letter seeks clarification with respect to the phrase "significant change," and specifically requests that the phrase be interpreted in conformity with SEC guidance in this area. It also seeks clarification of "significant change" with respect to a variable insurance

contract that includes an asset allocation program as an investment option. Specifically, it asks whether a “significant change” in a portfolio included in an asset allocation program would preclude the use of pre-dated performance information for the asset allocation program.

Variable Annuity Performance and Variable Life Insurance Policy Performance

The letter supports the proposal relating to communications of variable annuity historical performance and the disclosure regarding which policy level fees are deducted from variable life historical performance. It seeks clarification that the proposal would eliminate the current requirement that variable life insurance policy performance be used only if preceded or accompanied by a statutory prospectus.

Illustrations Based on Assumed Rates of Return

The Institute’s letter generally supports the provisions in the proposal regarding assumed-rate illustrations but it makes several recommendations. For example, the letter supports use of a standardized assumed rate of return of up to ten percent but recommends that FINRA continue to monitor prevailing market conditions on a regular basis to determine if additional changes to the maximum permitted assumed rate of return may be appropriate. The letter also requests confirmation that illustrations may demonstrate the deduction of current charges in addition to maximum guaranteed charges. With respect to presentations of multiple assumed rates of return, the comment letter notes that the term “broad-based securities market” is not defined and seeks clarification on any limitations with respect to the term. It recommends that FINRA provide a significant transition period to permit compliance with the new rule, and requests that FINRA confirm that it would be permissible to use multiple-rate illustrations where the rates are based on blended index performance.

Illustrations Based on Historical Performance

The letter supports the proposed use of historical performance illustrations using assumed dollar investment amounts. It notes, however, that there is no definition of “illustration” in the proposal and expresses concern that, without some limitations, the provisions of the proposal relating to “illustrations” could be read broadly to encompass product explanations that were not intended to be captured. Accordingly, the letter seeks clarification regarding the type of illustrations meant to be included in the proposal.

Guarantee Claims and Riders

The comment letter commends FINRA for its efforts to make discussions of riders more uniform and accurate, and supports the requirement that communications be “fair and balanced” with respect to whether a guarantee or rider will not benefit a customer. Nonetheless, the letter seeks clarification regarding the scope of the proposed disclosure so as to prevent second-guessing of what is “fair and balanced.” It also recommends that a

reference in sales materials to the specific location of such disclosure in the product prospectus would be sufficient to satisfy the proposed requirement. In addition, the letter requests that further guidance be provided as to what is meant by a “discussion” of a guarantee, so that investors are not overwhelmed with an exhaustive list of limitations every time a guarantee is mentioned.

Product Identification and Liquidity

The Institute’s comment letter supports the proposed prohibition that communications may not represent or imply that variable insurance products are mutual funds. It seeks clarification, however, that communications may continue to state that the product invests in mutual funds, to inform customers that a mutual fund underlies the product.

Tax-Deferred Illustrations

The letter generally supports the provisions in the proposal concerning comparative illustrations of the mathematical principle of tax-deferred versus taxable compounding contained in communications. It requests clarification that it is permissible to use an assumed state tax rate in general communications, provided it is clear from the surrounding disclosure that the state tax rate used is an assumed one.

Application of IM-2210-2 to Institutional Sales Material

The comment letter supports excluding institutional sales material from IM-2210-2. It notes that FINRA’s Rule 2211 currently provides that “[a]ll institutional sales material and correspondence are subject to . . . the applicable Interpretive Materials under [Rule 2210](#)” The letter therefore recommends that paragraph (d)(1) of FINRA’s Rule 2211 be revised so that it is consistent with the proposed institutional sales material exclusion of IM-2210-2.

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[Attachment](#)

endnotes

[\[1\]](#) See Memorandum to Variable Insurance Products Advisory Committee No. 22-08, dated August 11, 2008 [22788]. See also Variable Insurance Products, “FINRA Requests Comments on Proposed New Rules Governing Communications About Variable Insurance Products,” FINRA Regulatory Notice 08-39, July 2008.

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