

**MEMO# 28992**

May 18, 2015

# **SEC Charges Life Insurance Company with Pricing Violations under the Investment Company Act**

[28992]

May 18, 2015

TO: VARIABLE INSURANCE PRODUCTS ADVISORY COMMITTEE No. 7-15

SEC RULES MEMBERS No. 32-15

COMPLIANCE MEMBERS No. 17-15

INTERNAL AUDIT ADVISORY COMMITTEE No. 7-15

SMALL FUNDS MEMBERS No. 21-15 RE: SEC CHARGES LIFE INSURANCE COMPANY WITH PRICING VIOLATIONS UNDER THE INVESTMENT COMPANY ACT

On May 14, 2015, the Securities and Exchange Commission (“SEC” or “Commission”) brought a settled enforcement proceeding against a life insurance company (“Company”) based on alleged violations of the pricing rule under the Investment Company Act of 1940 (“1940 Act”) in connection with purchase and redemption orders for variable insurance contracts and underlying mutual funds. As described briefly below and in the attached order, [1] the SEC charged that the Company willfully violated Rule 22c-1 under the 1940 Act [2] by treating purchase and redemption orders received at its U.S. post office boxes prior to 4:00 p.m. as being received after 4:00 p.m., and processing those orders using the next day’s price.

## **Description**

The Order states that the Company was subject to the pricing requirements of Rule 22c-1 at two levels. It was designated in the variable contract prospectuses as authorized to consummate transactions in the variable contracts, and it was designated in the prospectuses of the underlying mutual funds as authorized to consummate transactions in underlying mutual fund shares. According to the Order, the variable contract prospectuses generally stated that orders received at the Company’s home office before 4:00 p.m. would receive the current day’s accumulation unit value (“AUV”) [3], and that orders received after 4:00 p.m. would receive the next day’s AUV. The prospectuses of the underlying mutual funds disclosed the same 4:00 p.m. cut-off for determining whether a purchase or redemption order received the current day’s NAV or the next day’s NAV.

According to the Order, the Company received purchase and redemption orders relating to

its variable contracts through a variety of methods, including mail sent to its multiple U.S. post office boxes at the post office or its home office either by First Class or Priority Mail, electronic orders, telephone requests, and facsimile. The Order states that the Company requested that the post office divide mail received for the variable products business, including mail containing purchase and redemption orders for variable contracts, from mail for the Company's other business units. The SEC alleged that the Company sent a courier to travel to the post office at 3:00 a.m., 5:00 a.m., and 7:00 a.m., each business day to retrieve the other mail, but specifically instructed the courier not to retrieve mail related to the variable contracts business at those times. The SEC further alleged that a courier was sent separately at 10:00 a.m. each business day to retrieve only Priority Mail from the post office, including purchase and redemption orders for variable contracts sent via Priority Mail. According to the Order, the courier was separately sent after 3:00 p.m. to retrieve the First Class mail related to the variable contracts business, and was told not to deliver that mail to the Company's building before 4:01 p.m. The SEC alleged that purchase and redemption orders received in such mail were then marked by the Company with a post-4:00 p.m. time stamp, and the Company then processed the orders for pricing at the next day's AUV and transmitted the orders to the underlying mutual funds for pricing at the next day's NAV. The SEC claimed that, by contrast, variable contract purchase and redemption orders that were received by the Company through Priority Mail at the post office were retrieved promptly by the courier and processed by the Company before 4:00 p.m. for pricing at the current day's price.

The SEC stated that the Company's intentional delay of the retrieval and delivery of purchase and redemption orders contained in its variable contract mail to its home office, as described in the Order, did not alter its obligation to process the orders using the current day's AUV, and to transmit orders to the underlying mutual funds for processing using the current day's NAV. The SEC alleged that, by processing the orders, which were received before 4:00 p.m., using the next day's price, the Company violated Rule 22c-1.

## **Sanctions**

The SEC noted that it considered remedial acts promptly undertaken by the Company and its cooperation in accepting its settlement offer. The Commission imposed a cease and desist order and a civil money penalty of \$8,000,000.

Sarah A. Bessin  
Associate General Counsel

## **endnotes**

[1] In re Nationwide Life Insurance Company, Investment Company Act of 1940 Release No. 31601 (May 14, 2015), available at <http://www.sec.gov/litigation/admin/2015/ic-31601.pdf> ("Order").

[2] Rule 22c-1 under the 1940 Act provides, in relevant part, that "[n]o registered investment company issuing a redeemable security, no person designated in such issuer's prospectus as authorized to consummate transactions in any such security, and no principal underwriter of, or dealer in, any such security shall sell, redeem, or repurchase any such security except at a price based on the current net asset value of such security which is next computed after receipt of a tender of such security for redemption or of an order to purchase or sell such security . . ."

[3] AUV is the measure of the contract owner's investment in a contract and is based on the net asset values ("NAVs") of the underlying mutual funds, adjusted for contract charges.

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