

MEMO# 31506

November 29, 2018

SEC Proposes Summary Prospectus for Variable Insurance Products

[31506]

November 29, 2018 TO: ICI Members

Investment Company Directors SUBJECTS: Compensation/Remuneration

Compliance

Disclosure

Distribution

Fees and Expenses

Fund Accounting & Financial Reporting

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Variable Insurance Products RE: SEC Proposes Summary Prospectus for Variable Insurance Products

On October 30, 2018, the Securities and Exchange Commission proposed rule and form amendments to modernize disclosure regarding variable annuity and variable life insurance contracts (“Proposal”).[\[1\]](#) The centerpiece of the Proposal is new Rule 498A (“VIP Summary Prospectus Rule”), which would allow issuers of variable annuity contracts and variable life insurance policies to use a summary prospectus to satisfy prospectus delivery obligations under Section 5 of the Securities Act of 1933.

The SEC requests comment on a variety of significant issues, both in connection with the VIP Summary Prospectus Rule and VIP regulation more generally. The public comment period expires on February 15, 2019.

We have summarized, below, the key aspects of the Proposal, focusing on those most relevant to registered open-end investment companies that serve as investment options for variable insurance products (VIPs).

I. Overview of Proposed VIP Summary Prospectus Rule

The Proposal includes the following components:

- *Option to Use Summary Prospectus*—Proposed Rule 498A would permit the use of two types of summary prospectuses describing the VIP: (1) an “initial summary prospectus” delivered in hard copy, or electronically if an investor elects, to *new*

investors that would include certain key information about the VIP; and (2) an “updating summary prospectus” delivered in hard copy, or electronically if an investor elects, to *existing* investors that would include a summary of any VIP changes, as applicable, since the last update, as well as certain information from the initial summary prospectus.

- *Internet Availability of Statutory Prospectus and Other Information*—Proposed Rule 498A would require that, to rely on the rule, the related VIP statutory prospectus and statement of additional information (SAI) must be publicly accessible, free of charge, at a website address specified on, or in the case of an electronic copy, hyperlinked in, the cover page or beginning of the VIP summary prospectus, with a hard copy made available by request at no cost.
- *Optional Delivery Method for Portfolio Company Prospectuses*—The Proposal provides an optional method to satisfy the prospectus delivery obligations of the underlying portfolio company issuers. Under this method, the VIP issuer would include certain key information about these portfolio companies in an appendix to the VIP summary prospectus. The VIP issuer would be required to make the portfolio companies’ summary and statutory prospectuses available online at the website address specified on, or in the case of an electronic copy, hyperlinked in, the cover page or beginning of the VIP summary prospectus, with a hard copy made available by request at no cost.
- *VIPs No Longer Actively Sold to New Investors*—For VIPs no longer actively sold to new investors (referred to by the SEC as “Discontinued Contracts”), the SEC noted that many issuers rely on SEC staff no-action letters permitting issuers to cease filing updates to the VIP registration statements and delivering updated prospectuses and other information to existing investors under certain circumstances. With respect to such Discontinued Contracts, the SEC proposes to effectively “grandfather” contracts relying on the existing no-action relief as of the effective date of a final VIP Summary Prospectus Rule, subject to continued compliance with the no-action letters. For all other Discontinued Contracts, issuers would be required to file post-effective amendments to update their registration statements and provide updated prospectuses in reliance on the new VIP Summary Prospectus Rule framework. The SEC also discussed, and requested comment on, alternative approaches to address Discontinued Contracts.
- *Form Amendments; XBRL; Other Amendments*—The SEC also proposes to update and enhance certain disclosure requirements for VIPs under Forms N-3, N-4, and N-6 and would require VIP registrants to use the Inline XBRL format for filing certain information. In addition, the Proposal includes certain technical and conforming amendments to implement the proposed VIP summary prospectus regime, and to update or rescind other rules and forms applicable to VIPs.

The approach reflected in the VIP Summary Prospectus Rule is similar to that taken in Rule 498, the mutual fund summary prospectus rule, but includes several key differences that reflect the unique nature of variable insurance products, as discussed below.

II. VIP Summary Prospectuses

The VIP Summary Prospectus Rule would permit, but not require, use of two distinct types of summary prospectuses for VIPs to satisfy prospectus delivery obligations under Section 5(b)(2) of the 1933 Act: (1) an “initial summary prospectus” to be provided in connection with sales of VIPs to new investors; and (2) an “updating summary prospectus” to be provided to investors who are existing contract owners. Use of summary prospectuses

would be conditioned on, among other things, making the statutory prospectus and other materials available online, and sending such materials to investors in paper or electronically upon request. Importantly, like the mutual fund summary prospectus rule, the VIP Summary Prospectus Rule, subject to certain conditions, would permit issuers of VIPs to incorporate by reference into both the initial summary prospectus, as well as the updating summary prospectus, information contained in the statutory prospectus, SAI and, in the case of variable annuity separate accounts registered as management investment companies, shareholder reports.[\[2\]](#) The SEC requests comment regarding the various disclosure requirements and presentation of information for the initial and summary prospectus.

A. Initial Summary Prospectus

Under the VIP Summary Prospectus Rule, an initial summary prospectus may describe only a single contract[\[3\]](#) that the registrant currently offers for sale, and would be required to include certain information, and only that information, in the same order, and under the relevant corresponding headings, as the proposed rule specifies, including the following:

- A cover page including certain identifying information (such as the name of the insurance company, the separate account registrant, and the contract), legends with identifying information about the VIP and certain general information that applies to all VIPs, and a hyperlink where additional information about the contract may be found;
- An optional table of contents;
- An overview of the contract, providing introductory information about the contract, how it works, and its primary features (including death benefits, withdrawal options, loan provisions, and any available optional benefits);
- A table with a standardized format, order, and headings, outlining key information about the contract (“Key Information Table”), including fees and expenses; risks; restrictions or limitations, primarily relating to investment options or benefits; taxes; and conflicts of interest;[\[4\]](#)
- A discussion of the standard death benefit available under the contract and how it operates;
- A table summarizing other benefits available under the contract, including each benefit’s name, purpose, whether the benefit is standard or optional, associated fees, and limitations or restrictions;
- A description of the procedures for purchasing the contract, including the minimum initial and subsequent payments required, and limitations or restrictions on payments;
- For variable life insurance policies, a description of when and under what circumstances the contract will lapse, any lapse options, the effect of the lapse, and under what circumstances a contract may be reinstated;
- A discussion of how investors may access their money through surrender or withdrawal, including any limits on the ability to surrender, how proceeds are calculated, and when they are payable;
- The full fee table (including the expense example in the case of variable annuity contracts) that also would appear in the statutory prospectus detailing all of the expenses incurred when an investor buys, sells, and owns the contract; and
- An appendix (discussed in more detail below) describing the portfolio companies currently available as investment options under the contract.[\[5\]](#)

B. Updating Summary Prospectus

Under current industry practice, insurance companies typically send the updated VIP statutory prospectus to existing contract owners each year to satisfy prospectus delivery obligations in connection with additional purchase payments or premium payments that may be received, or the reallocation of contract value that may be made, in the coming year. Under the VIP Summary Prospectus Rule, this obligation could be satisfied with respect to existing investors by providing an “updating summary prospectus” rather than a full statutory prospectus. An updating summary prospectus would discuss any material changes that have occurred with respect to the contract during the past year, as well as certain information required in the initial summary prospectus, including the following:

- A cover page including certain identifying information and legends similar to the initial summary prospectus and a hyperlink where additional information may be found;
- An optional table of contents;
- A brief description of any changes to the contract since the most recent updating summary prospectus or statutory prospectus was sent to investors with respect to the fee table, the standard death benefit, other benefits available under the contract, portfolio companies available under the contract, as well as other changes that the registrant wishes to disclose;
- A Key Information Table with the disclosure required in the initial summary prospectus; and
- An appendix (discussed in more detail below) with portfolio company disclosure, identical to the appendix required in the initial summary prospectus.[\[6\]](#)

The SEC stated that, in describing any changes to the contract, issuers should “provide enough detail to allow investors to understand the change and how it will affect them.”[\[7\]](#) Appendix B to the Proposing Release, which provides a hypothetical updating summary prospectus and briefly lists contract changes in bullet format, suggests that this disclosure need not be extensive.[\[8\]](#)

The updating summary prospectus would be required to contain the information required by the VIP Summary Prospectus Rule in the specific order outlined in the rule. In addition, the VIP Summary Prospectus Rule would permit the updating summary prospectus to describe one or more contracts covered in the statutory prospectus to which the updating summary prospectus relates. This contrasts with the initial summary prospectus, which would be limited to describing only one contract. However, a registrant would only be permitted to use an updating summary prospectus if it uses an initial summary prospectus for each currently offered contract described under the current statutory prospectus to which the updating summary prospectus relates.

C. Appendix of Portfolio Companies

The VIP Summary Prospectus Rule would require an appendix of portfolio companies that would include a legend: (1) stating that the portfolio companies listed are currently available under the VIP and are subject to change; (2) providing a hyperlink to a landing page, a telephone number and an email address that investors may use to obtain a copy of a portfolio company’s summary and statutory prospectus; and (3) stating that the portfolio company expense information provided does not reflect contract charges, performance would be lower if these charges were included, and past performance does not indicate future performance. The appendix would then identify each portfolio company available as an investment option in a table indicating each portfolio company’s type or investment

objective, name, investment adviser or subadviser, gross expense ratio and average annual total returns for the past 1-year, 5-year and 10-year periods. Additionally, if the portfolio companies that are available vary based on benefit options selected, the appendix also would include a separate table identifying the portfolio companies available under each benefit.

The SEC requests comment regarding the disclosure and presentation requirements of the appendix of portfolio securities and whether alternative disclosure or a different presentation would be more useful to investors. It requests comment on specific issues including whether: (1) particular disclosure items that it has proposed for inclusion in the appendix are useful and appropriate for consideration by investors, or should it revise, supplement or replace those items; (2) to require advertising disclosures contemplated by Rule 482, such as legends providing certain statements about performance data and certain information about sales loads or performance fees; and (3) in the case of an updating summary prospectus, the appendix should identify portfolio companies that have been added, removed, or closed to additional investment during the period covered by the update.

III. Prospectus Delivery Requirements

A. Availability of VIP Disclosure Documents

Under the VIP Summary Prospectus Rule, an issuer could satisfy its prospectus delivery obligations by providing investors with a contract summary prospectus and making the contract statutory prospectus available online and in paper or electronically by request. The VIP Summary Prospectus Rule's requirements relating to online accessibility would be similar to those for mutual funds and would require that:

- A current version of each document remains on the website, publicly accessible to investors for at least 90 days following the time of the "carrying or delivery" of the contract security;
- Any documents posted online must be "human readable" (*i.e.*, text appears legible and is not cut off);
- The documents are linked so that a user can move between an electronic version of the table of contents and a particular section of the document and also between sections of the contract summary prospectus and related sections of the contract statutory prospectus and SAI;
- Investors are able to view the definition of any special terms used in the summary prospectus by hovering over or selecting the term, or by moving between the special term and its respective glossary definition; and
- Investors accessing the online documents are able to permanently retain such documents free of charge in an electronic format.

In addition, a contract summary prospectus may not be bound together with any other materials except for summary and statutory prospectuses of portfolio companies, provided that those portfolio companies are available investment options for the investor to whom the materials are sent or given and the materials include a table of contents identifying each portfolio company prospectus included and the page on which it may be found. The SEC requests comment on the conditions in the VIP Summary Prospectus Rule regarding the online availability of the required online VIP documents.

B. New Delivery Option for Portfolio Company Prospectuses

The Proposal includes a new delivery option that would satisfy portfolio companies' prospectus delivery obligations through a "notice and access" approach. The Proposal provides that VIP issuers that provide investors with a contract summary prospectus would not be required to include prospectuses of the underlying portfolio companies if certain conditions are met.^[9] Under the optional delivery method, there would be no affirmative obligation to deliver prospectuses of underlying portfolio companies, absent an investor request for delivery in paper or electronically.^[10]

Under this delivery option, the VIP issuer would be required to include certain key information about the portfolio companies available under the contract in an appendix to the contract's summary prospectus (as discussed above), and must make the summary and statutory prospectuses for the portfolio companies available online at the website address specified on or hyperlinked in the VIP summary prospectus. This approach would satisfy the portfolio companies' prospectus delivery obligations if: (1) an initial summary prospectus is used for each currently offered VIP described under the related registration statement; (2) a summary prospectus is used for the portfolio company; and (3) the portfolio company's current summary prospectus, statutory prospectus, SAI, and most recent shareholder reports are posted online under similar posting requirements for the VIP's summary prospectuses and other documents. These documents would be subject to similar online formatting and accessibility requirements as mutual fund summary prospectuses under Rule 498, but the Proposal would require the documents to be posted at the same website address as the VIP materials that appear online. If a portfolio company amends or supplements its prospectus between annual updates, the updated prospectus must be posted online.

The SEC requests comment on several aspects of the new delivery option for portfolio company prospectuses, including, among others, whether: (1) to permit the use of the new option if a portfolio company does not use a summary prospectus; (2) portfolio company documents should be required to be posted at the same website address as the VIP materials; (3) the separate requirements of Rule 498 regarding mutual fund summary prospectus documents create any confusion that should be addressed by the VIP Summary Prospectus Rule; and (4) interim portfolio company prospectus supplements should be required to be delivered to investors.

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endnotes

^[1] SEC Release Nos. 33-10569, 34-84508 and IC-33286 (Oct. 30, 2018), *available at* <https://www.sec.gov/rules/proposed/2018/33-10569.pdf> ("Proposing Release").

^[2] Notably, the VIP Summary Prospectus Rule would not permit incorporation by reference

of any other information. See Proposed Rule 498A(d).

[3] An initial summary prospectus may, however, describe more than one class of a contract. *Id.* at 33. This is similar to a mutual fund summary prospectus, which “may describe only one [f]und, but may describe more than one [c]lass of a [f]und.” Rule 498(b)(4).

[4] Among other things, the Key Information Table would require VIP registrants to disclose minimum and maximum annual fees for portfolio company fees and expense, using the gross expense ratio disclosed in fee table of the portfolio company’s current prospectus.

[5] Proposed Rule 498A(b). The Proposing Release includes an appendix with a hypothetical initial summary prospectus. See Proposing Release at Appendix A.

[6] Proposed Rule 498A(c).

[7] Proposing Release at 104. The Proposing Release indicates, for example, that stating merely that a fee has changed is not sufficient. Rather, the updating summary prospectus should disclose that the fee has changed from 1.5% to 1.7%. *Id.*

[8] See Proposing Release at Appendix B.

[9] This new option would be available to Form N-4 and Form N-6 registrants, but would not be available to Form N-3 registrants because they do not have underlying portfolio companies.

[10] See Proposed Rule 498A(j)(1)(iii).