

**MEMO# 14617**

April 8, 2002

## **DRAFT ICI REGULATORY REFORM PROPOSALS RELATING TO VARIABLE INSURANCE PRODUCTS**

[14617] April 8, 2002 TO: VARIABLE INSURANCE PRODUCTS ADVISORY COMMITTEE No. 2-02 RE: DRAFT ICI REGULATORY REFORM PROPOSALS RELATING TO VARIABLE INSURANCE PRODUCTS In connection with plans to undertake a comprehensive review of the federal securities laws, SEC Chairman Harvey Pitt has invited the industry to make recommendations for possible regulatory changes. In response to this invitation, the Institute has prepared a draft package of regulatory reform proposals. Summarized below and attached are two recommendations that relate to variable insurance products. In particular, the Institute's recommendations would amend Rules 6e-2 and 6e-3(T) under the Investment Company Act to eliminate the need for mixed and shared funding relief and codify exemptive relief to permit substitutions of underlying funds. We have scheduled a conference call for Monday, April 15 at 3:00 pm Eastern to discuss the attached proposals. If you would like to participate on the conference call, the dial in number will be 888-455-0058 and the pass code will be "Variable Insurance." In addition, if you plan to participate on the conference call, please contact Monica Carter- Johnson by phone at 202-326-5823, by fax at 202-326-5827 or by e-mail at [mcarter@ici.org](mailto:mcarter@ici.org). Finally, if you have any comments on the proposals, please provide them to the undersigned by phone at 202-371-5408, by fax at 202-326-5839 or by e-mail at [aburstein@ici.org](mailto:aburstein@ici.org) no later than Friday, April 19.

I. Amend Rules to Allow Mixed and Shared Funding Currently, Rules 6e-2 and 6e-3(T) under the Investment Company Act provide exemptive relief from various provisions of the Act to separate accounts funding variable life insurance ("VLI") contracts to permit those contracts to be offered and administered under the Act. However, where the separate accounts funding these contracts are organized as unit investment trusts, certain relief provided by these rules is available only if shares of the underlying fund are offered "exclusively" to separate accounts funding VLI contracts of the insurance company and/or of any affiliated life insurance company. Because of this exclusivity requirement, to qualify for exemptive relief under the rules, the underlying fund cannot offer its shares to, among other things, separate accounts funding variable annuity ("VA") contracts of the same or an affiliated insurer ("mixed funding") and separate accounts funding VLI contracts of unaffiliated insurers or separate accounts funding VA contracts of unaffiliated insurers ("shared funding").

2 The draft submission recommends amendments to Rule 6e-2 and 6e-3(T) to eliminate the "exclusivity" requirements.

II. Adopt Rules to Allow Substitutions of Insurance Product Funds The draft submission recommends that the SEC adopt a new rule under the Investment Company Act to permit insurance companies and their registered separate accounts to substitute shares of one underlying fund for another without first obtaining SEC approval under Section 26(c) of the Act. The new rule would exempt

insurance company depositors from Section 26(c) based on a set of conditions that would capture the most important of the criteria that have been employed by the SEC in reviewing exemptive applications: (1) the compatibility of investment objectives and strategies; and (2) expenses. The recommended rule would leave for SEC approval on a case-by-case basis those applications that do not meet these conditions. In addition, the draft submission recommends that the SEC adopt a companion rule to the new rule on substitutions to permit the transfer in-kind of portfolio securities from an existing underlying fund to a new underlying fund in effecting a substitution. The new rule would codify the positions taken by the SEC in no-action letters and numerous exemptive orders. Among the conditions to which applicants have agreed is that the in-kind transaction will comply or will substantially comply with the conditions in Rule 17a-7 under the Act. Ari Burstein Associate Counsel Attachment Attachment (in .pdf format)

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