

MEMO# 9202

August 29, 1997

SEC ISSUES CONCEPT RELEASE REGARDING EQUITY INDEX INSURANCE PRODUCTS

* See Securities Act Release No. 7438 (August 20, 1997), 62 Fed. Reg. 45359 (August 27, 1997), (copy attached). [9202] August 29, 1997 TO: SEC RULES COMMITTEE No. 83-97 RE: SEC ISSUES CONCEPT RELEASE REGARDING EQUITY INDEX INSURANCE PRODUCTS

The Commission is considering the status of equity index annuities and other equity index insurance products under the federal securities laws.* As part of this consideration, the Commission is seeking comment on a variety of issues, including the structure of these products, the manner in which they are marketed, and the federal securities laws issues raised by equity index insurance products. The significant aspects of the Commission's release are summarized below.

I. Description of Equity Index Insurance Products An equity index annuity is a contract issued by a life insurance company that generally provides for accumulation of the contract owner's payments, followed by payment of the accumulated value to the contract owner in a lump sum or series of payments. During the accumulation period, the insurer credits the contract owner with a return that is based on changes in an equity index, such as the S & P 500 Index. The insurer also guarantees a minimum return to the contract owner if the contract is held to maturity. Equity index products combine features of traditional insurance products (guaranteed minimum return) and traditional securities (return linked to equity markets). Depending on the mix of features in any insurance product, including an equity index insurance product, the product may or may not be entitled to exemption from registration under the Securities Act of 1933 as an "insurance policy" or "annuity contract." To date, most equity index annuities have not been registered under the Securities Act, although commentators have acknowledged that substantial uncertainty exists whether all of these products are entitled to exemption from registration. Both purchasers and insurers may benefit from greater clarity in this area.

II. Applicability of the Federal Securities Laws to Equity Index Insurance Products Section 3(a)(8) of the Securities Act exempts from registration any "insurance policy" or "annuity contract" issued by a corporation subject to the supervision of the insurance commissioner, bank commissioner, or similar state regulatory agency. The Commission and the courts have addressed this exemption on a number of occasions and applied certain factors to determine whether a product is entitled to the exemption. Comment is requested on the application to equity index insurance products of the factors used by the Commission and the courts to determine whether the exemption is available for a particular product. These factors include the allocation of investment risk between insurer and contract owner, the manner in which the contract is marketed, and the applicability of state insurance

regulation. A. Allocation of Investment Risk Comment is requested on how investment risk is allocated between the insurer and contract owner in equity index insurance products. Comment also is requested on how this allocation of risk affects the application of the federal securities laws to these products. B. Marketing The Commission noted its concern that the nature of equity index insurance products may make it particularly difficult to market these products without primary emphasis on their investment aspects. Comment is requested on how these products are marketed. Commenters are asked to address both written sales materials and oral sales presentations, including the ability of an insurer to train and monitor its sales force to ensure that these products are not marketed with primary focus on their investment aspects. Commenters also are asked to identify the products that are viewed as competitive alternatives to equity index annuities and address how the nature of these competitive products affects the manner in which equity index insurance products are marketed. C. State Regulation Comment is specifically requested on whether equity index insurance products are regulated as annuities or insurance under state law. In addition, comment is requested on how the applicability of state insurance law affects the need for federal securities regulation of these products. Comments are due to the Commission by November 20, 1997. Please contact me with your comments on the Commissions release by October 9, 1997. You can reach me by phone at 202/326-5821, facsimile at 202/326-5827, or e-mail at donohue@ici.org. Dorothy M. Donohue Associate Counsel Attachment (in .pdf format)

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