

ACT ICA

SECTION 3(c)(11)

RULE _____

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RESPONSE OF THE OFFICE OF
INSURANCE PRODUCTS
DIVISION OF INVESTMENT MANAGEMENT

Our Reference No. IP-1-98
Massachusetts Mutual Life
Insurance Company

By letter dated July 17, 1998, Massachusetts Mutual Life Insurance Company ("MassMutual") requests our assurance that we would not recommend enforcement action to the Commission if, as more fully described in your letter, MassMutual offers and sells MassMutual group annuity contracts and interests in MassMutual separate investment accounts ("Separate Accounts") funding the group annuity contracts to State and local government deferred compensation plans qualifying under Section 457 of the Internal Revenue Code of 1986, as amended (the "Code"). MassMutual does not intend to register the group annuity contracts or the Separate Accounts under the federal securities laws in reliance on Section 3(a)(2) of the Securities Act of 1933 ("Securities Act"), Section 3(a)(12) of the Securities Exchange Act of 1934 ("Exchange Act"), and Section 3(c)(11) of the Investment Company Act of 1940 ("Investment Company Act").

Facts

MassMutual is a mutual life insurance company established under the laws of the Commonwealth of Massachusetts and operating in all fifty states, the District of Columbia, and the Commonwealth of Puerto Rico. Currently, MassMutual offers and sells group annuity contracts to pension or profit-sharing plans that qualify for favorable tax treatment under Code Section 401(a) or for the deduction for the employer's contributions under Code Section 404(a)(2) ("Qualified Plans"), and to governmental plans under Code Section 414(d) described in Section 3(a)(2) of the Securities Act ("Section 414(d) Plans").¹ MassMutual proposes to issue group annuity contracts to deferred compensation plans established by State and local governments pursuant to Code Section 457 that satisfy the requirement of Code Section 457(g) that plan assets and income be held for the exclusive benefit of plan participants and beneficiaries ("New Section 457 Plans"). Each group annuity contract to be issued to a New Section 457 Plan will require that the assets and income of the New Section 457 Plan held under the group annuity contract be used for the exclusive benefit of the plan's participants and beneficiaries.

MassMutual group annuity contracts provide for plan contributions to be allocated to MassMutual's general investment account, to one or more Separate Accounts, or to both MassMutual's general investment account and to one or more Separate Accounts.

¹ Plans for self-employed individuals within the meaning of Code Section 401(c)(1) may be considered Qualified Plans. Group annuity contracts are only offered without registration to these plans, and the assets of these plans will only be held in the Separate Accounts, if the conditions for exemption from registration pursuant to Rule 180 under the Securities Act are satisfied.

Contributions to MassMutual's general investment account are credited with a stated, guaranteed rate of return. Obligations under group annuity contracts funded through the general investment account are backed by MassMutual's reserves and statutory surplus.

Investment returns of a Separate Account vary based upon the investment experience of the Separate Account.² The income, gains, and losses of a Separate Account are credited to or charged against the net assets held in the Separate Account without regard to the income, gains, and losses arising out of any other Separate Account or business that MassMutual may conduct.

Assets of New Section 457 Plans that are held under group annuity contracts and invested in MassMutual Separate Accounts will be commingled with assets of Qualified Plans and Section 414(d) Plans that are held under group annuity contracts and invested in MassMutual Separate Accounts. The Separate Accounts will be used for no purpose other than to fund Qualified Plans, Section 414(d) Plans, and New Section 457 Plans investing in the Separate Accounts through MassMutual group annuity contracts. No assets of individual retirement accounts or annuities established pursuant to Code Section 408 or tax-sheltered annuities or custodial accounts established pursuant to Code Section 403(b) are or may be invested in the Separate Accounts.

MassMutual states that prior to the enactment of the Small Business Job Protection Act of 1996 ("Job Protection Act"),³ in order for a deferred compensation plan of a State or local government or instrumentality to be eligible under Code Section 457, the assets of the plan were required to remain the property and rights of the sponsoring employer and to be subject to the employer's general creditors. In the Job Protection Act, however, Congress added Code Section 457(g) to require that the assets and income of an eligible deferred compensation plan maintained by a State, political subdivision of a State, and any agency or instrumentality of a State or political subdivision of a State be held in trust for the exclusive benefit of plan participants and their beneficiaries. Section 457(g)(3) treats a custodial account or contract described in Code Section 401(f), such as an insurance company group annuity contract, as a trust for this purpose.⁴ This "exclusive benefit" requirement applies immediately to all State

² No New Section 457 Plan assets will be allocated to the purchase of securities issued by a New Section 457 Plan employer or any company directly or indirectly controlling, controlled by, or under common control with any New Section 457 Plan employer.

³ Pub. L. No. 104-188.

⁴ Code Section 401(f) treats an annuity contract as a qualified trust under Code Section 401(a) if, among other things, the requirements of Code Sections 401(a)(1) and 401(a)(2) are met. Code Sections 401(a)(1) and 401(a)(2) generally provide that a trust constitutes a qualified trust if (1) contributions are made to the trust for the purpose of distributing to employees or their beneficiaries the corpus and income of the trust; and (2) under the trust instrument, it is impossible, at any time prior to the satisfaction of all liabilities with respect to the employees and their beneficiaries, for any part of the

and local government plans created after August 20, 1996, and applies beginning January 1, 1999, to plans in existence on August 20, 1996.

Analysis

Section 3(a)(2) of the Securities Act and Section 3(a)(12) of the Exchange Act exempt from registration any security arising out of a contract issued by an insurance company, which security is issued in connection with a governmental plan as defined in Section 414(d) of the Code that has been "established by an employer for the exclusive benefit of its employees . . . if under such plan it is impossible . . . for any part of the corpus or income to be used for, or diverted to, purposes other than the exclusive benefit of such employees" ⁵ Section 3(c)(11) of the Investment Company Act excludes from the definition of "investment company" any separate account the assets of which are derived solely from such plans.

MassMutual notes that the staff has previously granted relief from registration under Section 3(a)(2) of the Securities Act to insurers and banks offering contracts and interests in collective trusts, respectively, to State and local government plans under Code Section 457 and has consistently treated these plans as "governmental plans" for purposes of the exemptions under the Securities Act, Exchange Act, and Investment Company Act. ⁶ MassMutual also notes that in the staff's most recent letter, State Street Bank and Trust Co. (pub. avail. Aug. 1, 1996), the staff indicated that its earlier letters no longer represented its position on the availability of the specified exemptions to State and local government plans that complied with Code Section 457 as it existed prior to amendment by the Job Protection Act ("Old Section 457 Plans").

corpus or income to be used for, or diverted to, purposes other than the exclusive benefit of the employees or their beneficiaries.

⁵ Section 414(d) of the Code provides that a "'governmental plan' means a plan established and maintained for its employees by the Government of the United States, by the government of any State or political subdivision thereof, or by any agency or instrumentality of any of the foregoing."

⁶ See, e.g., State Street Bank and Trust Co. (pub. avail. Aug. 1, 1996); The Lincoln National Life Insurance Co. (pub. avail. Oct. 26, 1992); Hartford Life Insurance Co. (pub. avail. June 24, 1992); Pan American Life Insurance Co. (pub. avail. Nov. 19, 1991); Standard Insurance Co. (pub. avail. Sept. 11, 1991); Aetna Life Insurance and Annuity Co. (pub. avail. Sept. 11, 1991); Principal Mutual Life Insurance Co. (pub. avail. June 27, 1991); Metropolitan Life Insurance Co. (pub. avail. June 6, 1991); Monarch Life Insurance Co. (pub. avail. Apr. 3, 1991); The Travelers Insurance Co. (pub. avail. Aug. 6, 1990); Great-West Life & Annuity Insurance Co. (pub. avail. Feb. 1, 1990); Fidelity Management Trust Co. (pub. avail. Nov. 2, 1989); Aetna Life Insurance Co. (pub. avail. Oct. 18, 1989); Nationwide Life Insurance Co. (pub. avail. May 12, 1989); North Shore Savings and Loan Ass'n. (pub. avail. Dec. 8, 1988); Wells Fargo Bank, N.A. (pub. avail. Sept. 7, 1988).

In State Street, the staff noted that the positions taken in the earlier letters were based largely on the general representation that plan assets would not be used for any purpose other than the exclusive benefit of participants except to the extent that plan assets were required to remain subject to the claims of general creditors of the employer to preserve the plan's eligibility under Code Section 457. The staff also stated its belief that this general representation no longer provided an adequate basis for no-action relief without specific additional restrictions on the ability of an employer to withdraw assets similar to those described in State Street.

MassMutual notes that the State Street restrictions prevented the employer/sponsor of an Old Section 457 Plan from using plan assets for its own purposes and effectively enabled the assets to be held for the exclusive benefit of plan participants and beneficiaries. MassMutual asserts that the amendment of Code Section 457 by the Job Protection Act provides assurance that New Section 457 Plans provide protections to plan participants and beneficiaries similar to those provided by Qualified Plans and Section 414(d) Plans, as to which exemptions from registration are available under Section 3(a)(2) of the Securities Act.

MassMutual's counsel is of the opinion that New Section 457 Plans are substantially similar to Section 414(d) Plans in purpose and effect. This opinion is based on similarities between the plans, most importantly, that New Section 457 Plans and Section 414(d) Plans share the requirement that all assets and income be held for the exclusive benefit of the plan's participants and beneficiaries.

MassMutual argues that the staff's reasoning in State Street demonstrates the availability of the federal securities laws exemptions in connection with State and local government plans under Code Section 457 that satisfy the requirements of a Section 414(d) Plan as set forth under Section 3(a)(2) of the Securities Act. Specifically, the plan must be established for the exclusive benefit of its participants and their beneficiaries; and it must be impossible, prior to the satisfaction of all liabilities with respect to the participants and beneficiaries, for any part of the plan's corpus or income to be used for, or diverted to, purposes other than the exclusive benefit of the participants and beneficiaries. MassMutual asserts that the New Section 457 Plans to which MassMutual proposes to issue group annuity contracts will satisfy these requirements.

In light of the foregoing, we would not recommend enforcement action to the Commission under Section 7 of the Investment Company Act if MassMutual offers and sells interests in the Separate Accounts to New Section 457 Plans without registering the Separate Accounts as investment companies in reliance on Section 3(c)(11) of the Investment Company Act.⁷ The Division of Corporation Finance has asked us to inform you that it would not recommend enforcement action to the Commission under Section 5 of the Securities Act or

⁷ MassMutual does not seek, and we are not providing, any assurances as to the applicability of Securities Act Section 3(a)(8) to the offer or sale of group annuity contracts funded through MassMutual's general investment account.

Section 12 of the Exchange Act if MassMutual, in reliance upon your opinion as counsel that the exemptions under Section 3(a)(2) of the Securities Act and Section 3(a)(12) of the Exchange Act are available, offers group annuity contracts to New Section 457 Plans without registration under these Acts. The Division of Market Regulation has asked us to inform you that it concurs in this position with respect to the Exchange Act. The Divisions' positions are based on the facts and representations in your letter. You should note that any different facts or circumstances might require a different conclusion. Furthermore, this response represents only the Divisions' positions on enforcement action and does not express any legal conclusions on the questions presented.

Status of Prior Letters

New Section 457 Plans

In light of the amendment of Code Section 457 by the Job Protection Act, which extended an "exclusive benefit" requirement to Code Section 457 State and local government plans, the staff believes that specific additional restrictions on the ability of an employer to withdraw assets similar to those described in State Street are no longer necessary. Therefore, this letter, rather than State Street, represents the staff's position on enforcement action in cases where New Section 457 Plans, *i.e.*, plans complying with the "exclusive benefit" requirement of Code Section 457(g), as amended by the Job Protection Act, are included in a bank collective trust or insurance company separate account.

Old Section 457 Plans

In State Street, the staff indicated that it would not recommend enforcement action to the Commission if, for Old Section 457 Plans, *i.e.*, plans not complying with the "exclusive benefit" requirement of Code Section 457(g), banks and insurance companies continued to rely on the no-action letters issued prior to State Street until August 1, 1997. The staff also stated that, after that date, banks and insurance companies wishing to continue including Old Section 457 Plans in their collective trust funds or separate accounts should, for new contracts, enter into an agreement similar to that described in State Street with the sponsor of each Old Section 457 Plan, and, for existing contracts, use reasonable efforts to amend plan documents and/or supporting contracts to conform to the State Street requirements.

The Job Protection Act provided a transition rule for Old Section 457 Plans in existence on the date of enactment. Those Old Section 457 Plans are not required to comply with the "exclusive benefit" requirement until January 1, 1999.

Subsequent to issuing State Street, the staff has informally advised requestors that it would not recommend enforcement action to the Commission if banks and insurance companies including Old Section 457 Plans in their collective trust funds or separate accounts, respectively, during the period from August 1, 1997, through December 31, 1998, continue to rely on the staff's no-action letters issued prior to State Street. The staff was persuaded that

the process of amending plan documents and contracts and securing state regulatory approvals of contract forms to comply with State Street during the interim period from August 1, 1997 (the State Street compliance date), to December 31, 1998 (the date after which Old Section 457 Plans must become New Section 457 Plans to comply with Code Section 457), could impose undue costs and burdens. This informal advice represents the staff's position on enforcement.

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