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SECTION
RULE 24f-2
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

DIVISION OF
INVESTMENT MANAGEMENT

November 8, 1989

Dear Sir/Madam:

This letter provides general guidance to insurance companies filing post-effective amendments in connection with the offering of variable life and variable annuity contracts. These comments represent the informal views of the staff of the Office of Insurance Products and not necessarily those of the Commission. They are intended only to assist registrants in the preparation of disclosure documents and are not to be considered of precedential value in any court or other official action.

This letter is divided into two parts. The first part deals with substantive matters and the second part deals with procedural matters that may arise during your preparation of post-effective amendments.

SUBSTANTIVE COMMENTS

A. Recent Developments

1. High Yield Bond Disclosure

A recent Commission release discusses appropriate disclosure by certain registrants as to participation in high yield, highly leveraged or non-investment grade loans and investments. See Management's Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures, Release Nos. 33-6835, 34-26831, IC-16961 (May 18, 1989). That release also discusses appropriate disclosure by investment companies that invest, or are permitted to invest, all or a portion of their portfolios in high-yield or non-invest grade securities.

In addition, the Division of Investment Management (the "Division") recently circulated a letter supplementing the

Commissions release. 1/ See Letter attached. Accordingly, we recommend the following:

a) Underlying Funds: Underlying funds of insurance company separate accounts, registered on Form N-1A, should consult the release and the letter to ensure compliance with their disclosure obligations.

b) Managed Separate Accounts: Managed separate accounts, registered on Form N-3, should consult the release and the letter to ensure compliance with their disclosure obligations to the same extent required by underlying funds.

c) Registered Guaranteed Investment Contracts: The Commission release addresses disclosure obligations of certain financial institutions participating in high-yield financing, highly leveraged transactions or non-investment grade loans and investments. That release should be consulted by insurance companies registering fixed annuity contracts under the Securities Act of 1933.

2. Tax Disclosure

The Technical and Miscellaneous Revenue Act of 1988 ("TAMRA"), as well as the 1986 amendments to the Internal Revenue Code, altered certain tax matters relating to variable annuity and variable life insurance contracts. 2/ Prospectuses and/or SAI tax disclosure reflecting these changes should be updated accordingly.

Specifically, registrants should review contracts that may be classified as modified endowment contracts. The staff recommends the following:

a) For single premium variable life contracts that could

1/ Please be advised that the staff anticipates receiving a no-action letter seeking clarification on certain matters raised in the letter. Any such staff clarification should be consulted by registrants.

2/ Registrants should also note that on March 2, 1989, the Internal Revenue Service issued final regulations on investment company diversification requirements for variable life insurance and variable annuity contracts under Internal Revenue Code Section 817(h).

be classified as modified endowment contracts, registrants should consider including the following prospectus disclosure:

Cover Page

- A statement that the contract is or may be a modified endowment contract.

- If the contract is classified as a modified endowment contract, a statement that any policy loan, partial withdrawal or surrender may result in adverse tax consequences and/or penalties.

Summary Page

- A brief definition of a modified endowment contract, including a description of the "seven-pay" test, or an appropriate cross-reference to the definition.

- A statement that the amount of certain distributions made during the insured's lifetime, such as policy loans, partial withdrawals or surrenders, that exceed the contractowner's investment in the contract might be included in the owner's gross income ("income-first basis"), and that a 10% penalty tax may be imposed on such income distributed before the contractowner attains age 59-1/2.

- A cross-reference to the tax disclosure contained in the prospectus.

Tax Section

- A detailed explanation of the tax implications of modified endowment contract status.

b) For flexible premium variable life insurance contracts that could be classified as modified endowment contracts, the registrant should indicate whether it has adequate safeguards established for monitoring whether a contract may become a modified endowment contract. If the company has not established adequate safeguards, the staff would recommend the same summary page disclosure as above.

3. Single Premium Variable Life Contracts

The staff recently issued a no-action letter concerning the ability of a single premium variable life contract to rely on Rule 6e-3(T). See Equitable Variable Life Insurance Company (pub. avail. Aug. 9, 1989).

4. Office of Disclosure and Review's Industry Comment Letter

The Division intends to circulate an industry comment letter to assist registrants of public mutual funds in their preparation of post-effective amendments. Registrants of variable insurance products should consult that letter for relevant comments.

5. Life Insurance Product's Depositor Financial Statements

The staff would not recommend withholding acceleration of the effective date of the registration statement filed on Form S-6 if the financial statements of the depositor (life insurance company) are not updated in conformity with the requirements of Rule 3-12 of Regulation S-X, 3/ provided that (1) the registrant makes a written request to the staff explaining in detail the basis for excluding the financial statements; (2) the request is approved by the staff; and (3) the registrant inserts the following statement in the prospectus:

> The most current financial statements of the Company (depositor) are those as of the end of the most recent fiscal year. The Company does not prepare financial statements more often than annually and believes that any incremental benefit to prospective policyholders that may result from preparing and delivering more current financial statements, though unaudited, does not justify the additional cost that would be incurred. In addition, the Company represents that there have been no adverse changes in the financial condition or operations of the Company between the end of the most current fiscal year and the date of this prospectus.

6. Variable Annuity Fee Table

On January 23, 1989, the Commission issued a release amending Forms N-3 and N-4 to require the consolidation of all expense information in a table located near the front of the prospectus. See Investment Company Act Release No. 16766. The following points may be of interest in preparing registration statements for the upcoming year:

a) A separate account investing in a portfolio company with multiple series may include a single table in its Form N-4 registration statement instead of individual tables for each

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3/ In pertinent part, Rule 3-12 of Regulation S-X requires the updating of financial statements in a filing where such statements are as of a date 135 days or more prior to the date the filing is expected to become effective.

series. For example, portfolio company annual expenses for the various underlying funds can be reflected in matrix form as follows:

[Portfolio Company] Annual Expenses
(as a percentage of [portfolio company] average net assets)

	Fund A	Fund B	Fund C	Fund D
Management Fees	____	____	____	____
Other Expenses	____	____	____	____
Total Annual Expenses	____	____	____	____

Registrants also may want to use a matrix format in the Example.

b) The expense figure listed in the Example should include the percentage of the annual contract fee that is deducted from a $1,000 investment. Only where the average account size is $1,000 should the entire annual contract fee be included in the figure. If the average account size is $3,000 and the annual contract fee is $30, only 1/3 or $10, of the contract fee is included in the estimate of expenses that a contractowner would pay on a $1,000 investment.

c) The staff has taken a no-action position regarding the calculation of the annual contract fee in the fee table example for issuers of variable annuity contracts that offer both fixed and variable funding operations within a single contract, provided it is done in one of the two alternative ways set forth in the letter. See American Council of Life Insurance (pub. avail. Apr. 21, 1989).

B. Charges

1. Administrative Expenses

Rules 6e-3(T)(c)(4)(iv) and 6e-2(c)(4)(iv) provide exemptive relief from certain provisions of the 1940 Act to permit the deduction of administrative expense charges from separate account assets in connection with variable life insurance contracts. Rule 26a-1 provides similar relief for variable annuity contracts. Registrants relying on these rules may continue to deduct administrative expense charges only so long as the amounts collected meet the requirements set forth in these rules. Disclosure of these administrative expense charges should state that the charges have been set at a level to recover no more than the actual cost associated with administering the contract.

2. Withdrawals

Administrative fees for withdrawals are limited to a maximum of 2% of the amount withdrawn (subject to the at-cost standard). The staff will raise redeemability issues on deductions that

exceed this requirement. See Investment Company Act Release No. 15651, at note 74 (Mar. 30, 1987).

3. Fees and Charges Associated with Variable Life Contracts

All of the fees and charges attributable to a contract, including sales load, should be set forth not further back than page three of the prospectus. (See Form S-6, Instructions as to the Prospectus, Instruction 2, Presentation of Information). Disclosure should include fees and charges assessed against the separate account, as well as those assessed against the underlying portfolio company.

4. Disclosure Regarding Sales Load "Shortfall"

The registrant must disclose in the prospectus whether the sales load imposed on a variable life or variable annuity contract is designed to recover all distribution costs associated with the contract. If not, the registrant must disclose how it will recover the shortfall (e.g., from the general account assets consisting of, among other things, amounts derived from mortality and expense risk charges).

C. Miscellaneous

1. Use of Simplified Underwriting

If an insurance company intends to use simplified underwriting that would result in the actual or guaranteed cost of insurance charges exceeding the maximum allowed by the 1980 CSO Tables, provide Summary Page disclosure of the following: (1) a statement indicating the amount by which the actual or guaranteed cost of insurance charges will exceed the maximum allowed by the 1980 CSO tables; and (2) a statement that the cost of insurance charges (which may be viewed as substandard risk charges) are generally higher for healthy individuals when this method of underwriting is used. (Note that unless the registrant can substantiate a claim that the portion of the charge exceeding 100% of the 1980 CSO is properly attributable to a substandard risk charge, it must be treated as sales load).

2. Mixed and Shared Funding

Where a fund underlying variable contracts sells its shares to both variable annuity and variable life insurance separate accounts of the same insurance company or of affiliated insurance companies ("mixed funding"), or to variable annuity or variable life insurance separate accounts of unaffiliated insurance companies ("shared funding"), the fund's prospectus must disclose the risks involved in mixed and/or shared funding. This disclosure should include a statement indicating that if a

material irreconcilable conflict arises between separate accounts, a separate account may have to withdraw its participation in the fund.

The separate account prospectus should include disclosure or provide a cross-reference to the fund's risk disclosure regarding mixed and/or shared funding.

A separate account investing in a fund under a shared funding arrangement should ensure that a copy of the shared funding participation agreement has been filed as an exhibit to the separate account's registration statement.

3. Variable Life Illustrations

The following points should be considered in preparing variable life illustrations:

a) All separate account expenses, as well as the underlying fund expenses, must be reflected in the illustrations. For funds past the start-up stage, an amount no less than the actual operating expenses incurred should be used. The staff considers the start-up period to be one year after the fund has commenced operations/sales. For funds adding a new series, it would be appropriate to estimate expenses that will be incurred in that new series, so long as the estimate is reasonable, i.e., they should be consistent with or conform to the actual expenses incurred by the other series.

b) For underlying funds with multiple series, a simple average of the investment advisory fees of the underlying fund(s) must be reflected in the illustration.

c) In the narrative, disclose the existence and operation of any expense reimbursement arrangement. The narrative must disclose the amount of expenses that would have been incurred absent the reimbursement agreement, and the likelihood that the expense reimbursement agreement will continue past the current year, as well as the effect of discontinuing the agreement.

d) An actuarial opinion pertaining to the illustrations should be filed with each post-effective amendment.

4. Allocations of Initial Purchase Payments for Variable Annuity Products During The Free Look Period

The staff recently has issued three no-action letters concerning the allocation of an initial purchase payment for a variable annuity contract to a money market subaccount during the

free look period. See Fidelity Investments Variable Annuity Account I (pub. avail. Dec. 8, 1987), LBVIP Variable Annuity Account I (pub. avail. Jan. 22, 1988), and MONY America Variable Account A (pub. avail. Oct. 26, 1988).

5. Section 403(b) No-Action Letter

The staff has taken a no-action position relating to compliance with Section 403(b)(11) of the Internal Revenue Code and Sections 22(e), 27(c)(1) and 27(d) of the 1940 Act for registrants offering variable annuity contracts. See American Council of Life Insurance (pub. avail Nov. 28, 1988). The conditions in the no-action letter include, among other things, prospectus and sales literature disclosure requirements and certain registration statement representations. Representations may be made in Part C of Forms N-3 or N-4.

Please provide appropriate disclosure regarding the redemption restrictions imposed by Section 403(b)(11).

PROCEDURAL COMMENTS RELATING TO FILING POST-EFFECTIVE AMENDMENTS

1. Updating Requirement

Section 10(a)(3) of the Securities Act of 1933 ("1933 Act") requires that any prospectus used more than nine months after the effective date of the registration statement contain information as of a date not more than sixteen months prior to such use. Therefore, any separate account and its sponsor/depositor wishing to maintain a continuous public offering must file a post-effective amendment to the registration statement of the separate account (and, where appropriate, its underlying portfolio company) containing updated financial statements and other information. Rules 485 and 486 under the 1933 Act govern this process.

2. Updating Procedures

Rule 486 specifies the procedures for updating the registration statement of any separate account registered under the 1940 Act either as a unit investment trust ("trust account") or as a management investment company ("management account"). Rule 485, as relevant here, specifies the procedures for updating the registration statement of any management investment company serving as an underlying portfolio company for a trust account ("underlying portfolio company").

The registrant is responsible for determining whether any changes in its registration statement warrant filing a post-

effective amendment under paragraph (a) of Rule 485 or Rule 486 rather than under paragraph (b) of these rules.

Staff review of amendments filed under paragraph (a) rather than paragraph (b) of Rules 485 or 486 will be facilitated if, in addition to providing a redlined copy, the transmittal letter enumerates the material changes requiring the amendment to be filed under paragraph (a) rather than under paragraph (b).

The staff will attempt to provide timely comments on post-effective amendments filed pursuant to Rules 485(a) or 486(a). If the registrant has not received comments within 45 days after filing, it would be appropriate to inquire of the staff as to the status of the post-effective amendment. Registrants printing disclosure documents before comments have been provided do so at their own risk.

Post-effective amendments filed pursuant to paragraph (b) of Rules 485 or 486 must include the appropriate certification of the registrant on the signature page and be accompanied by counsel's representation that the post-effective amendment does not contain disclosure that would render it ineligible to become effective pursuant to paragraph (b). See paragraph (e) of Rules 485 and 486.

Filings must be sent directly to the Commission and should not be addressed or sent to members of the staff.

Rule 497(b) requires that ten copies of the prospectus, in the exact form in which it is being used, be filed with the Commission within five days after the effective date. Rule 497(c) specifies that investment companies filing on Forms N-1A, N-3, or N-4 must file ten copies of both the prospectus and the Statement of Additional Information ("SAI") in the exact form in which it is used.

3. Effective Date and Request for Acceleration

Registrants relying on the automatic effective date provided by Rules 485(a) and 486(a) should note that a filing made on March 2 will have a May 1 effective date. Generally, an acceleration request is necessary only if a post-effective amendment, filed pursuant to Rules 485(a) or 486(a), must become effective before the earliest automatic effective date, which is the sixtieth day following filing, or a later date between the sixtieth and eightieth day after filing, if such date is specified on the facing page of the post-effective amendment. A request for acceleration will be necessary if a post-effective amendment is filed after March 2 requesting a May 1 effective date.

Registrants that file after March 2 should be aware that due to heavy staff workload during the months of March and April, there is no assurance that the staff will be able to accelerate the filing. If acceleration is necessary, the registrant should notify the staff as soon as possible of the reason why the filing cannot be made by March 2, the nature of the material changes, and an estimate of the date the filing will be made.

In accordance with Rule 461 of Regulation C under the 1933 Act, requests for acceleration of the effective date of a registration statement shall be made in writing by both the registrant and the principal underwriter.

4. Responding to Staff Comments

To expedite review of post-effective amendments, the following steps should be followed:

a) When drafting a written response to staff comments, the registrant should respond to each comment individually by repeating the staff comment, stating the response, and making a cross-reference to any changes in the registration statement.

b) Prompt responses to staff comments and, if required, prompt filing of subsequent amendments, will greatly facilitate the process. If an amendment to the registration statement is required, it should be marked to highlight the changes.

c) If the registrant believes that no change in the registration statement is necessary or appropriate in response to any staff comment, this opinion, along with the basis for the opinion, should be submitted to the staff in writing. The staff reserves the right to comment further on any subsequent amendments or letters.

5. Selective Review

The staff encourages registrants to review Investment Company Act Release No. 13768 (Feb. 15, 1984), governing procedures for selective review. If the registrant believes that selective review is appropriate, a request for selective review should be made in the transmittal letter accompanying the filing. The request for selective review should include: (i) a statement whether the disclosure in the amendment has been reviewed by the staff in some other context; (ii) a statement identifying prior filings that the registrant considers similar to, or intends as precedent for, the current filing; (iii) a summary of the material changes made in the current registration statement from the previous filings; and (iv) any specific areas that warrant

particular attention. The registrant should provide the staff with a red-lined courtesy copy of the current filing marked to show the changes from the previously reviewed filings.

6. Rule 24f-2 Requirements

Rule 24f-2(a)(1) of the 1940 Act requires that any post-effective amendment to a registration statement that has registered an indefinite number or amount of securities in reliance on Rule 24f-2 must include: (a) a statement to the effect that the issuer has registered an indefinite number or amount of securities in accordance with Rule 24f-2 ("24f-2 Notice"), and (b) the date on which the 24f-2 Notice for the issuer's most recent fiscal year was filed or will be filed, or a statement that the issuer need not file a Rule 24f-2 Notice because it did not sell any securities pursuant to the Rule 24f-2 declaration during the most recent fiscal year.

When preparing the 24f-2 Notice, carefully review the method of fee calculation described in paragraph (c) of Rule 24f-2. Note that the registration fee calculation can be based on the actual price of sales less redemptions and repurchases only if the 24f-2 Notice is filed within two months after the close of the registrant's fiscal year. If the Rule 24f-2 Notice for a company with a fiscal year-end of December 31 is not received by the Commission by February 28, redemptions cannot be netted against sales in calculating the fee. All 24f-2 Notices must include an opinion of counsel stating whether the securities being registered were legally issued, fully paid, and non-assessable.

If a registrant proposes to cease its operations, it must file a post-effective amendment terminating the declaration and file the Rule 24f-2 (Final) Notice prior to its cessation of operations. If a final Rule 24f-2 Notice is not timely received, a registrant will be unable to use the netting procedures.

7. Exhibits to Registration Statements

Registrants filing amendments to registration statements must list all exhibits, lettered or numbered for convenient reference. See Item 24 of Form N-1A, Item 24 of Form N-4, Item 28 of Form N-3, and Instructions as to Exhibits of Form S-6. See also Rule 483 of the Securities Act of 1933. Where the exhibits are incorporated by reference, reference must be made in the list of exhibits as to where the documents can be found.

8. N-SAR Filing Requirements

Registrants are reminded of their annual and semi-annual requirement to file their N-SAR report. See Rules 30a-1 and

30b1-1 of the 1940 Act. The staff intends to monitor these filings to assure that registrants comply with these requirements.

We trust that this letter will assist you in preparing your forthcoming filings.

Sincerely yours,

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