



REMARKS OF

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U.S. SECURITIES AND EXCHANGE COMMISSION**

**VARIABLE ANNUITIES AND LIFE INSURANCE:
PRODUCTS OF THE '90'S ?**

VARIABLE PRODUCTS & ASSET MANAGEMENT CONFERENCE

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- * The views expressed herein are those of Commissioner Beese and do not necessarily represent those of the Commission, other Commissioners, or the staff.

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I think we would all agree that the variable insurance industry has come a long way since the College Retirement Equities Fund or "CREF" sold the first variable annuity contract in the United States in 1952, or since the Equitable Assurance Company sold the first variable life insurance contract in this country in the late 1970s. Despite a difficult regulatory history, the industry has persevered and is today very much alive in this country.

Variable contracts have endured because they are useful consumer products that offer something unique to the American public, and they could become a big part of the business of many U.S. life insurance companies. Indeed, it may very well be, as some are predicting, that variable contracts will be the financial product of the '90s, like mutual funds were in the '80s.

But for this to occur, both the regulators and the regulated must do their part. No doubt, the tangled web of regulations facing this market can explain in part the moderate growth of variable insurance in the U.S. At the SEC, the Division of Investment Management has made several excellent recommendations to amend the '40 Act, in hopes of permitting greater flexibility in pricing and distributing these products.

At the same time, these recommendations go hand in hand with the Division's efforts to improve the quality of disclosures provided to current and

prospective purchasers of variable products. The resiliency of variable insurance and its recent success may be linked to the growing recognition that these products do play or should play an important role in the financial planning for many Americans.

Variable annuity contracts now represent a primary means of retirement planning for many people, and a supplemental means for others. For many families and businesses, variable life also figures prominently in the planning for unexpected financial losses caused by a sudden death.

The opportunities for the continued growth of this industry are enormous as increasing numbers of consumers come to recognize the benefits of investing in variable insurance. These can be complex products, however, only offering tremendous advantages for those willing to trade off certain potential disadvantages.

Before variable insurance can become a household name in this country, the industry will have to step forward to educate their potential customers about the pros and the cons of their product. I firmly believe that for this market, an educated consumer can be the industry's best friend. With favorable market conditions and the recent changes in the tax code, the industry is poised for an explosion in sales. I would hope that as the industry

takes advantage of these favorable conditions, it will also take the time to lay a proper foundation to sustain future efforts to expand.

By easing the restrictions governing the pricing and distribution, and informing investors about the specific nature of the products they are purchasing, I believe the industry can set the stage now for a prolonged period of future growth.

Recommendation For the Pricing and Distribution of Variable Products

In its May 1992 Report, the Division of Investment Management recommended amending the Investment Company Act of 1940 to permit greater flexibility in the pricing and distribution of variable insurance products. Insurance companies had complained that the Investment Company Act and rules, as currently applied to variable products, make it difficult for variable contracts, particularly variable life policies, to be priced competitively with other fixed insurance policies.

Moreover, these companies noted that such regulation makes it difficult to compensate salesmen selling variable life products on an equal basis with commissions paid for selling fixed products, without causing a significant strain on a company's capital and surplus. As a result, these companies argued, sales

of variable products are not as high as they would otherwise be and are sold by a relatively small number of life insurance companies.

Over a two year period, the staff of the Division of Investment Management considered these problems as well as some of the difficulties the Commission had encountered in regulating variable insurance.

For example, the staff noted that because of the hybrid nature of these products and the fact that the contracts' insurance elements are left to state insurance regulation, the Commission has had difficulty imposing meaningful controls over the contracts' investment elements. Moreover, the hybrid nature of these products and the desire to regulate only the contracts' insurance elements have led to a very complex form of regulation, as evidenced in two highly technical rules -- rules 6e-2 and 6e-3(T).

To address these concerns, the Division concluded that variable insurance charges should no longer be regulated by focusing on each individual charge assessed under a contract. For example, under current regulation, there are limits on the amount and manner of deducting sales loads, and on the level of administrative expenses that may be assessed.

The Division recommendations would require that variable charges be looked at in the aggregate and be subject to an overall standard of reasonableness.

The Division also recommended that the Commission have discretionary rule-making authority to establish standards for determining the reasonableness of aggregate contract charges. Significantly, the Commission would have clear jurisdiction over all contract charges, including insurance-related fees. Jurisdiction over insurance-related charges is a point that the industry has always contested, but it has expressed a willingness to concede this point if the Division's recommendation becomes law.

I applaud the Division's recommendation and strongly urge its enactment. In my opinion, the additional pricing and distribution flexibility it will provide to issuers of these products will go a long way towards making us a nation of INVESTORS rather than simply SAVERS. The recommendation will ensure that variable contracts become much more available to the American public and thus afford the means for many more Americans to plan adequately for their retirement as well as their overall personal financial needs. Moreover, the Division's proposal will yield benefits to investors without affecting the valuable protection the federal securities laws currently provide to such persons.

The Division's recommendation should further the goal of investor education because it would lead to the design of less complex and more readily understandable products. Regulating the overall level of charges should provide variable insurance issuers with the flexibility to design and market products that are less complex and more standardized. This should make it easier for their salesmen to explain these products and easier for consumers to understand how variable insurance operates. If consumers understand the investment and insurance attributes of these products, they may feel more comfortable exploring the various investment options available to them.

Because of greater commission parity, salesmen will be more inclined to sell variable insurance. For many investors, this may make variable insurance an attractive alternative to fixed interest rate products. Investors may also find it easier to choose among the variable insurance products that are available and, perhaps, the investment options under those products. Facilitating product comparison should stimulate competition and enhance the quality and diversity of variable insurance products available to investors. I also believe that increased competition will continue to ensure that charges under these contracts remain reasonable. In the end, I believe that giving investors the opportunity to better understand these products may enable them to better plan to meet their retirement needs.

Closely linked to the Division's recommendation is its undertaking to implement measures to improve the information provided to purchasers, and prospective purchasers, of variable products in prospectuses and other forms of sales literature. Specifically, the Division intends to develop a form that is particularly suited to the offer and sale of variable life policies. An important part of this task is to ensure some level of comparability among illustrations used in the offer and sale of these products.

It must be emphasized that work on this project is not dependent upon the eventual enactment of the Division's recommendation concerning variable contract charges. In fact, the Division has already begun work on this task, after receiving an informal submission from the ACLI a few months ago.

The proposed form is intended to make variable life insurance disclosure more meaningful and understandable for consumers. Standardized disclosure and illustrations should also foster product comparison and competition for consumer dollars. I am told that the staff is making significant progress with the proposed form and may be in a position to make a recommendation to the Commission in the near future.

I am also hopeful that these recommendations will stimulate competition among variable insurance product issuers to design products to meet consumers' growing and diverse investment needs. A market solution, in the form of heated competition, will also ensure that variable insurance product fees and charges remain reasonable.

I also note that the Office of Insurance Products is engaged in a continuing dialogue with the NASD in connection with variable insurance product advertising. One goal of these discussions has been to ensure that the variable contract charges, especially charges assessed at the separate account level, are considered in presenting investment performance in sales literature. Hopefully, cooperation between the two regulators will help eliminate misleading advertisements and ensure a level of comparability among advertisements.

Again, ensuring some measure of comparability in calculating investment performance will facilitate investment decision-making for many investors who must choose between variable annuities and the investment options they offer.

The Division's recommendations are steps in the right direction. Indeed, their efforts to enhance the quality of variable life insurance disclosure and

variable insurance advertisements should result in more user-friendly disclosure, disclosure that investors won't have to spend countless hours poring over in trying to understand. This disclosure should allow investors to more easily choose an investment option that will adequately fund their retirement needs.

Defined-contribution plans

Perhaps nowhere is the need for this type of user-friendly information more apparent than in the defined-contribution market. At present, a great many American workers eligible for these plans are inadequately planning for their futures. About one in four employees do not even participate in their defined-contribution plan. Even among those that do, some use them as auxiliary savings accounts, expecting to withdraw money as needed to pay for big-ticket items like houses, cars, and braces. Certainly, unless individuals have alternative sources of retirement funding, not contributing, or withdrawing pension plan assets early, is nothing more than leasing your current lifestyle from the last third of your life.

But equally important, defined-contribution plans require more than just saving for retirement: they also require good investment strategy. Under these types of plans, employees are responsible for the investment decisions

that determine how well they will live in retirement. For today's employees, understanding how to build and manage an investment portfolio is no longer a luxury, but a necessity.

Looking at how employees invest their plan assets, however, it seems that they may not fully appreciate the task at hand. Many appear to be making asset allocation decisions seeking safety above all else, rather than considering whether their investment strategy will eventually fund their retirement adequately.

Clearly, employees need help educating themselves about investing and how to make the best investment decisions when selecting among the available investment alternatives.

That's why I have been very supportive of the Division's recommendation that the SEC propose amendments to the federal securities laws: first, to cover those interests in pooled investment vehicles held by participants in defined-contribution plans; and second, to require delivery of prospectuses and semiannual and annual reports to the plan participants.

My support for these recommendations comes with a caveat, however. I am quite sensitive to the criticism that the Division's recommendations will add

more regulations and more cost, but have only a limited effect because employees simply will not read or use the bulky disclosures provided.

If the amendments are ultimately to achieve their purpose, I believe they must be written such that the prospectus/reports delivery requirements for this segment of the market can be satisfied by using standardized, short-form, summary prospectuses and reports. In this way, we insure that employees receive the most important information in a user-friendly format designed for easy comparability.

For example, the amended laws could provide that the delivery requirements are met by providing the same or similar information mandated by a single-page advertising prospectus, but in a uniform Morningstar/Value Line-style format. With some plans now offering multiple numbers of investment options, this refinement to the Division's recommendations would greatly reduce compliance costs and vastly improve the quality of the disclosure. For those employees wishing to see more detailed information, the amendments could also require that full prospectuses and periodic reports be made available.

Moreover, for the amendments to work in practice, any new disclosure rules we put into place would have to take into account the obligations imposed

by Labor's new 404(c) rules. These new rules are a good first step in getting more disclosure to employees, and we must be certain not to overburden employers with two different sets of rules.

At the same time, Labor's rules do have certain shortcomings, and I believe the Division's recommendations, refined as I have suggested, will go a long way towards addressing these shortcomings and providing plan participants the help they need to successfully plan their financial future.

Of course, information alone is not enough. You can not empower without enlightenment. I submit to you that it is in the best interests of the insurance industry to work toward a larger program of educating employees so they are capable of evaluating the suitability of their investment alternatives.

Educated consumers will be more likely to invest to fully fund their retirement needs. This can only enhance the reputation of your products as retirement planning vehicles and the reputation of your industry in general. For this reason, I applaud all the voluntary efforts to make prospectuses understandable and "user friendly" tools for retirement planning, not lengthy documents chock full of legalese.

Conclusion

I believe that the old adage "brevity is the sole of wit" has merit for variable insurance products. Brevity or simplicity, through prospectus disclosure or variable insurance advertisements, is not only the sole of wit but it is the most effective means to communicate the benefits of insurance products to consumers and to educate them so they may become investors.

For you in the variable insurance industry, this famous sports motto has never been more true: Your future is in front of you. By taking care now to help your current and potential customers understand and appreciate the unique products you have to offer, you can assure that for your industry, the best is yet to come.