NATIONAL ASSOCIATION OF SECURITY DEALERS V. 1958 Term Nos. 237
VARIABLE ANNUITY LIFE INSURANCE CO.
SECURITIES AND EXCHANGE COMMISSION V. 290
VARIABLE ANNUITY LIFE INSURANCE CO.
Cert to CA-DC Madden, Miller & Danaher.

Facts: The questions here are whether the variable annuity contracts (or policies) issued by resps are securities subject to registration requirements of the Securities Act of 1933, and whether the resps, as issuers thereof, are subject to regulation by the Investment Company Act. Suit was instituted by the SEC to restrain the further issuance of the contracts in question without compliance with those statutes. EALIC intervened as a defendant; NASD as a plaintiff. The dist. ct. held for resps, holding the contracts covered by the securities statutes, but that the McCarran-Fergueson Act exempted these companies from regulation. CA-DC affirmed on the ground that these companies were insurance companies and thus exempt from the securities statutes. It didn't mention the McCarran Act. The Securities Act (§3a8) exempts from registration "any insurance or endowment policy or annuity contract issued by a corporation subject to "supervision by a state insurance commissioner." The Investment Company Act (§2a17) defines Insurance companies, which are exempt from coverage, as companies "organized as insurance companies whose primary and predominant business activity is the writing of insurance…" The McCarran Act subjects the "business of insurance" to the regulation of the states.

VALCC and EALIC are chartered insurance companies regulated by the D C insurance commissioner. While they can sell life insurance, most of their business is in variable annuities. The latter is a plan whereby an investor makes fixed payments for a certain amount of time, after which he ceases payments and receives annuities for the rest of his life. He can withdraw his interest at any time before the annuity period begins. His interest is represented by accumulation units, which are his share of the variable annuity funds received by the company and invested in common stocks. The annuity is originally set at a fixed amount determined by the assumed value of the fund at the time the annuities begin; but the amount fluctuates if the fund is of a different value at that time. There can be no withdrawal of investment after the annuities begin.

Pets contend that the contracts are securities; that they are not insurance contracts because there is no risk shifted to the companies (rather the risk is shifted to the other investors, since if one investor lives beyond his life expectancy the annuities of other participants will be reduced). CA-DC held that the resps were insurance companies and the contracts in question insurance policies because the DC commissioner subjected them to regulation. Pets contend it is improper to leave the determination whether these companies are subject to federal control to state agencies, since different states have reached different conclusions. E.g., Conn. has held that variable annuities are not insurance policies. Pet argues that to be exempt from the two securities statues there must be state regulation, and the contracts or companies involved must be insurance or insurance companies.

Comment: Despite argument to the contrary by reaps I think there is no doubt that these contracts are "securities" in the general sense. SEC v. Howey, 328/293. The only question is whether they are also something else which would permit their exemption. This presents, I think, a substantial question which this Court should decide before these companies get too big. There certainly is confusion among the different states as to the nature of these contracts. Pets

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assert that if the result below stands, mutual funds and open end investment companies now regulated by the Investment Company Act would add such annuities to their contracts so as to slip out from SEC regulation. Resps state that if they are subjected to Investment Company Act regulation it will mean their destruction, since they couldn't meet the requirements of that Act. I think a good argument can be made that if the securities acts do not exempt these contracts and companies then the McCarran Act does not do so. The purpose of the McCarran Act was to nullify the effect of the Southeast Underwriters Case. But since the securities acts were in force before that case, and if these contracts were not exempt from those acts, if can be argued that the McCarran Act did not intend to remove from federal regulation activities in the nature of insurance which were previously covered by such regulation.

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