

SEC Adopts New Rule 498A for Variable Contracts

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On March 11, 2020, the U.S. Securities and Exchange Commission adopted new Rule 498A under the Securities Act of 1933, as amended, and related form and rule amendments. The new rule and amendments are intended to modernize disclosures for investors about variable annuities and variable life insurance contracts (together, “variable contracts”) by, among other things:

- Adopting a layered approach to disclosure designed to provide investors with key information on a contract’s terms in a concise format, with access to the contract’s related statutory prospectus and statement of additional information (SAI) upon request
- Permitting insurance companies and distributors to satisfy the prospectus delivery obligations of Section 5 of the Securities Act for variable contracts via a summary prospectus
- Permitting insurance companies and distributors to satisfy their prospectus delivery obligations for the mutual fund investment options underlying variable contracts by posting the funds’ prospectuses to a website
- Updating the disclosures provided to investors on Forms N-3, N-4 and N-6, the registration forms for variable contracts

New Summary Prospectus Option

Rule 498A creates two new types of variable contract summary prospectuses: “initial summary prospectuses” to be provided to new investors and “updating summary prospectuses” to be provided each year to existing contract holders. An initial summary prospectus includes a key information table summarizing the contract’s fees and risks, an overview of the contract, and more detailed disclosures regarding fees, purchases, withdrawals and other contract benefits. An updating summary prospectus includes a short description of changes to the contract that occurred during the prior year as well as the key information table from the initial summary prospectus. Both an initial and updating summary prospectus must include an appendix providing certain information on the mutual fund investment options underlying the variable contract.

Rule 498A requires that the variable contract’s statutory prospectus and SAI be publicly accessible,

free of charge, and at a website or hyperlink specified on the cover page of a summary prospectus. An investor who receives a variable contract summary prospectus must also be able to request the contract's statutory prospectus and SAI — in paper or electronic format — free of charge.

Prospectus Delivery Requirements for Underlying Mutual Funds

Rule 498A also permits insurers or distributors to make available online the prospectuses, SAIs and shareholders reports of the mutual fund investment options offered under the variable contract.

Amendments to Registration Forms and Compliance Dates

Insurers could begin relying on Rule 498A to satisfy prospectus delivery obligations beginning on July 1, 2020, and may do so going forward if the registrant is also in compliance with the amendments to Forms N-3, N-4 or N-6. Although the use of summary prospectuses to satisfy prospectus delivery obligations is optional, because the amendments to Forms N-3, N-4 and N-6 are designed to update and enhance the disclosure regime for variable contracts, all initial registration statements and post-effective amendments on Forms N-3, N-4 or N-6 must comply with the amendments to those forms beginning on January 1, 2022. Beginning on January 1, 2023, registrants must submit to the SEC certain disclosures in variable contract statutory prospectuses in Inline eXtensible Business Reporting Language (Inline XBRL) format.

Key Takeaways

Rule 498A will allow insurers to use a new concise selling document and to generate significant cost savings — the same cost savings that the mutual fund industry has experienced since 2009 — as they will no longer be required to provide investors with printed statutory prospectuses that may be 100 pages or more in length. Whether or not an insurer determines to use summary prospectuses, however, insurers should begin to develop timelines and project plans to comply with the new prospectus disclosure requirements adopted with Rule 498A. Tasks will include updating prospectuses in accordance with the new disclosure requirements of Forms N-3, N-4 or N-6, coordinating with underlying funds to amend participation agreements, and developing and maintaining compliance procedures for websites.

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