

Contract, 23 of which invest in Principal Variable Contracts Fund, Inc. ("Principal Fund"), an open-end management investment company registered under the Act (File Nos. 811-01944 and 002-35570). There currently are 47 Divisions available under the Accumulator and Prinflex Contracts, 25 of which invest in Principal Fund. There currently are 39 Divisions available under the Survivorship Contract, 25 of which invest in Principal Fund. There currently are 41 Divisions available under the FBA Contract, 26 of which invest in Principal Fund. There currently are 25 Divisions available under the Premier Contract, all of which invest in Principal Fund. The only Divisions affected by this application are the MicroCap Divisions of VL Separate Account and Separate Account B which invest solely in the MicroCap Account and the SmallCap Division of those two Separate Accounts which invest solely in the SmallCap Account. MicroCap Account and SmallCap Account are referred to collectively as the "Funds."

4. The Contracts permit transfers of accumulated value from one Division to another. The total amount transferred each time must be at least \$250 under the FVL Contract or \$100 under the FVA, Survivorship, Accumulator, or Prinflex Contracts, unless a lesser amount constitutes the Contract's entire accumulated value in a Division. Transfers between Divisions under the Premier Contract are not subject to a minimum amount or any charge. A transaction charge of \$25 is imposed on each transfer of accumulated value among Divisions under the FVL Contract exceeding four per policy year. A transaction charge of \$30 is imposed on each transfer of accumulated value among Divisions under the FVA Contract exceeding twelve per policy year. No transaction charge applies to transfers under the Prinflex, Accumulator or Survivorship Contracts.

5. Applicants propose a substitution of shares of the SmallCap Account for shares of the MicroCap Account held by the MicroCap Divisions of VL Separate Account and Separate Account B.

6. Principal Management Corporation ("PMC"), a registered investment adviser under the Investment Advisers Act of 1940, as amended ("Advisers Act"), and an indirect, wholly-owned subsidiary of Principal Financial Group, Inc., serves as the investment adviser for the Funds. Pursuant to sub-advisory agreements, the MicroCap Account is managed by Goldman Sachs Asset Management ("GSAM"), a registered investment adviser under the Advisers Act, and the SmallCap Account is

managed by Invista Capital Management, LLC ("Invista"), a registered investment adviser under the Advisers Act. Invista is an indirect, wholly-owned subsidiary of Principal Life.

7. The MicroCap Account's investment objective is to seek long term growth of capital primarily by investing in value and growth oriented companies with small market capitalizations. Under normal market conditions, the MicroCap Account invests at least 80% of its net assets plus any borrowings for investment purposes (measured at the time of purchase) in a broadly diversified portfolio of equity securities in microcap U.S. issuers (including foreign issuers that are traded in the United States). These microcap issuers will generally have market capitalizations of less than \$1 billion at the time of investment. The expense ratio of the MicroCap Account for 2002 was 1.25%. The MicroCap Account has no 12b-1 plan. The total return of the MicroCap Account was -16.89% for the year ended December 31, 2002, and the average annual total return for the life of the Account through December 31, 2002, was -5.54%.

8. The SmallCap Account's investment objective is to seek long term growth of capital by investing primarily in equity securities of both growth and value oriented companies with comparatively smaller market capitalizations. Under normal market conditions, the SmallCap Account invests at least 80% of its assets in common stocks of companies with small market capitalizations (those with market capitalizations similar to companies in the Russell 2000 Index) at the time of purchase. The expense ratio of the SmallCap Account for 2002 was 0.97%. The SmallCap Account has no 12b-1 plan. The total return of the SmallCap Account for the year ended December 31, 2002, was -27.33%, and the average annual total return for the life of the Account through December 31, 2002, was -5.95%. There are no fee waiver or expense reimbursement provisions with respect to either Fund.

9. Applicants believe that the substitution will better serve the interests of contractowners because it will eliminate an investment option under the Contracts that has never been able to attract significant contractowner interest and will provide contractowners with an investment in an account that has similar, although not identical, investment objectives and policies as well as a lower expense ratio. Applicants also believe that the substitution should benefit contractowners by providing economies

of scale that result from investing in a much larger account. Applicants represent that the substitution will take place at the relative net asset values determined on the date of the substitution in accordance with section 22(c) of the Act and rule 22c-1 thereunder. Applicants represent that there will be no financial impact to any contractowner. The substitution will be effected by having the MicroCap Divisions redeem their shares of the MicroCap Account for cash at the net asset value calculated on the date of the substitution and purchase shares of the SmallCap Account for cash at net asset value on the same date. In the alternative, the substitution may be effected by having a partial "in-kind" redemption with the MicroCap Divisions receiving from the MicroCap Account securities that are eligible investments for the SmallCap Account and that have a value equal to the net asset value of the shares of the MicroCap Account being redeemed and then contributing these securities to the SmallCap Account in exchange for shares of the SmallCap Account having a net asset value equal to the value of the securities contributed (the "In-Kind Transaction"). In connection with the completion of the substitution, Principal Life will withdraw its seed money from the MicroCap Account and terminate the MicroCap Account. In addition, Principal Life will combine the MicroCap Division with the SmallCap Division.

10. Applicants represent that the proposed substitution was described in supplements to the prospectuses for the Contracts ("Stickers") which were filed with the Commission on August 16, 2002, and mailed to contractowners. The Stickers gave contractowners notice of the substitution, described the reasons for engaging in the substitution, and informed contractowners that no amounts may be transferred to the MicroCap Division on or after May 31, 2003. In addition, the Stickers informed affected contractowners that they will have an opportunity to reallocate accumulation value, prior to the substitution, from the MicroCap Division, or for 60 days after the substitution, from the SmallCap Division to another Division available under the Contracts, without the imposition of any transfer charge or limitation and without counting the transfer as one of the annual free transfers (the "Free Transfer Right").

11. Each contractowner has been provided a prospectus for the SmallCap Account. Within five days after the substitution, Principal Life will send to contractowners written confirmation