

MICHIGAN STATE  
UNIVERSITY  
COLLEGE OF LAW

November 19, 2013

**Via Email Only**

Elizabeth M. Murphy, Secretary  
Securities and Exchange Commission  
100 F Street NE  
Washington, DC 20549-1090  
[rule-comments@sec.gov](mailto:rule-comments@sec.gov)

**RE: SR-FINRA-2013-045 – Proposed Rule Change  
To Revise the Series 6 Examination Program**

Dear Ms. Murphy,

On behalf of the Investor Advocacy Clinic at Michigan State University College of Law, we write to support SR-FINRA-2013-045. The Financial Industry Regulatory Authority (“FINRA”) has proposed meaningful improvements to the Series 6 Examination Program (the “Series 6”). While FINRA’s proposed revisions will do much good, we write to ask that FINRA ensure the exam and outline thoroughly cover mutual fund switching and certain issues with variable annuities.



**A. Mutual Fund Switching**

Although FINRA has specifically stated “it is a violation of securities law when a broker recommends switching funds only to earn a commission from the sale or purchase,”<sup>1</sup> it is unclear whether the revised Series 6 will adequately cover issues concerning mutual fund switching. At present, Section 2.3 of the Proposed Outline covers many important aspects of mutual fund transactions without specifically emphasizing mutual fund switching. Because the Series 6 question bank is not available for public review, the Securities and Exchange Commission (the “Commission”) should ensure that the questions adequately address harms caused by improper mutual fund switching.

Improper mutual fund switching causes real harms. It may trigger unnecessary tax consequences by causing investors to prematurely realize gains or losses. Investors may also needlessly pay sales charges for switching between functionally identical funds. Furthermore, investors may be burdened by a longer holding period to avoid a sales charge. The revised Series 6 should address the possible switching costs: (i) higher annual expenses or taxes (ii) contingent deferred sales charges and (iii) holding periods.

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<sup>1</sup> FINRA, *Customer Advisory Centers: Not Your Typical Securities Firm Call Center*, <http://www.finra.org/Investors/ProtectYourself/InvestorAlerts/TradingSecurities/p016176>

## B. Variable Annuity Issues

FINRA has issued numerous alerts about variable annuity exchanges and variable annuities in tax-deferred accounts. Many of the same concerns about mutual fund switching also extend to variable annuity exchanges. Indeed, FINRA has issued at least five Notices to Members alerting representatives about suitability, obligation, and conflict of interest concerns regarding annuities and variable annuity exchanges.<sup>2</sup> It is unclear whether the “conversion privilege” in 2.3 of the Proposed Outline adequately addresses these issues. The Commission should scrutinize the proposed Series 6 question bank to ensure that the questions adequately cover this issue.

It is also unclear whether Section 2.3 of the Proposed Outline warns about annuities in tax-deferred or qualified accounts. Because a variable annuity’s primary purpose is tax-deferral, special considerations must justify any recommendation that an investor purchase a variable annuity within a tax deferred account.

Placing high cost variable annuities within tax-deferred accounts seriously harms investors and undercuts efficient capital allocation. Most variable annuities needlessly increase the expense of any tax-deferred account. They limit a client’s investment options while providing no additional tax savings. Furthermore, if the variable annuity is within a traditional IRA, the government requires that withdrawals begin no later than the April 1 that follows their 70½ birthday, regardless of any surrender charges the annuity might impose.<sup>3</sup> Mandatory early withdrawals may force investors to incur high surrender charges.

Indeed, FINRA itself has recognized these harms. In an Investor Alert, FINRA stated that, “most investors should consider annuity products only after they make their maximum contributions to their 401(k)s and other before-tax retirement plans.”<sup>4</sup> The Investor Alert also explicitly states that investing in a variable annuity within a tax-deferred account may not be a good idea because variable annuities will provide no additional tax savings. Such investments “will, however, increase the expense of the IRA, while generating fees and commissions for the broker or salesperson.”<sup>5</sup> If not already, these considerations should be emphasized in the revised Series 6 and reflected in the Proposed Outline and heavily covered in the Series 6 question bank to check known abuses associated with the sale of variable annuities.

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<sup>2</sup> NASD Notice to Members 99-35, 04-45, 96-86, 00-44, and 07-43, <http://www.finra.org/Industry/Regulation/Notices/1999/p004408> <http://www.finra.org/Industry/Regulation/Notices/2004/p003008> <http://www.finra.org/Industry/Regulation/Notices/1996/p004696> <http://www.finra.org/Industry/Regulation/Notices/2000/p003581>

<sup>3</sup> FINRA, *Variable Annuities: Behind the Hard Sale*, <http://www.finra.org/investors/protectyourself/investoralerts/annuitiesandinsurance/p005976>

<sup>4</sup> *Id.*

<sup>5</sup> *Id.*

Elizabeth M. Murphy, Secretary

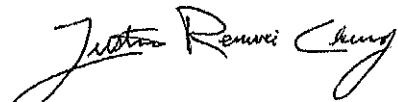
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### **Conclusion**

We support FINRA's decision to update the Series 6 and ask that the SEC closely review the Series 6 question bank to ensure that the exam adequately covers mutual fund switching and certain abuses associated with variable annuities.

Respectfully Submitted,



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