July 19, 2006

Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

RE: File No. SR-NASD-2004-183

Dear Ms. Morris:

On June 28, 2006, the Securities and Exchange Commission (the "Commission") published a notice and solicited comments on proposed NASD Rule 2821, "Members' Responsibilities Regarding Deferred Variable Annuities," filed with the Commission on December 14, 2004, as amended by Amendment No. 2 filed on May 4, 2006.[1]

This letter of comment on the proposed rule is respectfully submitted by the National Association for Variable Annuities ("NAVA").[2]

NAVA has worked with NASD and SEC staff on the rule since it was first proposed in 2004, and previously filed comments on August 6, 2004, September 19, 2005, and December 22, 2005. In our prior comment letters, we noted that NAVA and the annuity industry were committed to working with regulators to ensure that variable annuities are sold appropriately. More recently, in May 2006, NAVA participated in the Annuity Roundtable sponsored by the NASD and the Minnesota Department of Commerce, and is presently working with the ACLI to develop new disclosure documents for both variable and fixed annuities. NAVA and the annuity industry are also supporting the adoption of the NAIC's Annuity Disclosure Model Regulation and the expansion of its Senior Protection in Annuity Transactions Model Regulation to cover purchasers of all ages.

We are pleased that the current proposal has adopted many of the comments made by NAVA and other industry groups and participants. However, we continue to be concerned that singling out one product, deferred variable annuities, for specific and

[1] Release No. 34-54023 (June 28, 2006) (the "Release").
[2] NAVA is a not-for-profit organization dedicated to the growth and understanding of annuity and variable life insurance products. NAVA represents all segments of the annuity and variable life industry with over 350 member organizations, including insurance companies, banks, investment management firms, distribution firms, and industry service providers.

more stringent suitability requirements could inhibit the sale of an important investment that is helping millions of Americans save for and live in retirement.

While the latest amendments to the rule have addressed most of our principal concerns, we have the following comments in regard to several provisions in the current rule.

**Recommendation Requirements**

Section (b) of the proposed rule would impose specific recommendation requirements that would have to be met before a registered representative could recommend the purchase or exchange of a deferred variable annuity. Section (b)(1)(B) would require that the representative have a reasonable basis to believe that "the customer would benefit from the unique features of a deferred variable annuity (e.g., tax-deferred growth, annuitization or a death benefit)." We have two concerns here. First, while some features of a deferred variable annuity are unique to the product, such as the guaranteed death benefit and various forms of living benefits, other features that can make it an attractive and suitable investment, including some of those enumerated, are not unique only to deferred variable annuities. For example, there are other investments that can provide tax deferral, and fixed annuities also offer both tax-deferred growth and the option to annuitize. For these reasons, we recommend that the word "unique" be deleted from the rule.

Second, we recommend that "would" benefit be changed to "could" benefit. As we explained in our comment letter dated September 19, 2005 in regard to the previous requirement that there be a determination that the customer have a need for the features of a deferred variable annuity, many of the insurance features of a deferred variable annuity may or may not be utilized, depending on factors that are unknown at the time of purchase, such as future market performance. We believe that the use of the word "would" implies an element of certainty that may subject variable annuity sellers to claims years later.

Section (b)(2) would require representatives to make reasonable efforts to obtain extensive information from a customer prior to recommending the purchase or exchange of a deferred variable annuity. As we pointed out in previous letters, many of the specified items are vague, redundant and unnecessary, and go well beyond the customer account information required for all securities by Rule 17a-3(17) of the Securities and Exchange Act of 1934. "Financial situation and needs" in particular are vague concepts and superfluous since liquid net worth must also be obtained. A requirement that the representative inquire about the customer's "insurance holdings" has been changed to "life insurance holdings." However, this is still information that has not heretofore been required by NASD rules, nor, in our opinion, relevant as to whether a deferred variable annuity may be suitable for a particular customer. We recommend that this item of customer information be deleted.

**Principal Review and Approval**

Section (c) of the proposed rule dealing with principal review and approval has been modified several times and now would require that a registered principal review and approve all purchases or exchanges of a deferred variable annuity no later than two business days following the date when a member or person associated with a member transmits a customer's application to the issuing insurance company for processing.

We appreciate the SEC and NASD staff's consideration of industry comments in regard to the previous version of rule 2821, as amended by Amendment No. 1 on July 8, 2005, which required that the principal review and approval be completed prior to transmission of the application to the insurance company. As NAVA and others pointed out, a principal pre-approval requirement could in many cases delay the investment of customers' purchase payments and result in an emphasis on speed of review over quality and thoroughness.

However, in some instances, two days may not be sufficient for completion of the principal review. For example, customer outreach has become an increasingly important part of principal review and, due to difficulties in reaching customers or obtaining additional information, may not always be accomplished in two days. Under the requirement as presently written, such transactions would have to be cancelled by the broker-dealer in order to meet the two day deadline even though information to support the recommendation may be obtained shortly thereafter. Accordingly, we recommend that the rule require principal review and approval to be performed "promptly." This would ensure that reviews are performed timely and not occur long after an insurance company has issued the variable annuity contract, while at the same time providing enough time for thorough, high quality suitability analyses.

We request clarification on how the revised principal review provision should be construed in the case of recommendations made by a captive or in-house sale force. Historically, captive agencies have been the most popular distribution channel through which variable annuities are sold. In 2005, captive agents accounted for 35% of all variable annuity sales.[3] In those instances when a deferred variable annuity is recommended by a captive agent, we assume that the rule will not be interpreted to mean that the application has been transmitted to the insurance company at the same time it is obtained by the agent, but, rather, transmittal occurs when the application is actually sent by the agent or agency to the company.

Section (c) also sets out specific factors that the reviewing principal must consider in determining whether to approve a transaction. Section (c)(1)(A) would require the principal to consider the extent to which the customer would benefit from the unique features of a deferred variable annuity. For the same reasons we articulated above in regard to section (b)(1)(B), we recommend that the word "unique" be deleted and "would" replaced with "could" in this section as well.

[3] See *2006 Annuity Fact Book*, National Association for Variable Annuities, 2006.

Under the proposed rule, the registered principal would also have to consider the extent to which the amount of money invested would result in undue concentration in a deferred variable annuity or deferred variable annuities in the context of the customer's overall investment portfolio. We find this requirement to be overly vague and of little assistance in evaluating the suitability of a deferred variable annuity purchase. Rather, we believe that the more relevant and important criteria in this regard is the consideration of the extent to which the customer's liquidity needs make the investment inappropriate which is required by section (c)(1)(B). Accordingly, we recommend that section (c)(1)(C) be deleted.

Section (c)(1)(D) sets out other considerations if the transaction involves an exchange of a deferred variable annuity, including in subsection (ii) the extent to which the customer would benefit from any potential product enhancements and improvements. Such product enhancements could include, for example, new forms of death and living benefits. While we agree that the benefits of product enhancements or improvements offered by the new deferred variable annuity contract should be considered by the principal, we believe that the standard should be the extent to which the customer "could" benefit from the enhancement or improvement. This change is consistent with the changes we recommended above to sections (b)(1)(B) and (c)(1)(A). Whether a customer, in fact, benefits from an enhanced insurance feature such as the principal protection provided by living benefits, can in some ways only be determined years later and will depend on future market performance.

The Release recognizes that the NASD noted that firms may use automated supervisory systems, or a mix of automated and manual supervisory systems, to comply with the rule. The Release further sets out specific, minimum, requirements for a principal to approve the criteria used, audit and update the system, review exception reports and remain responsible for each transaction's compliance with the rule. Finally, the NASD noted that a principal would be responsible for any deficiency in the system's criteria. These comments imply that firms that utilize such automated systems will have a single principal who performs these tasks. We believe firms should have the ability to designate several principals to be responsible for various parts of the automated supervisory system. This would be consistent with the requirements of NASD Rule 3012 which provides that each member shall designate and specifically identify to NASD one or more principals who shall establish, maintain, and enforce a system of supervisory control policies and procedures.

**Supervisory Procedures**

Section (d) sets out requirements for additional written supervisory procedures reasonably designed to achieve compliance with the standards set forth in the rule and to require a registered principal to consider the items enumerated in paragraph (c). It then adds an additional factor that the registered principal must consider which is not included in paragraph (c), that the principal consider whether the associated person effecting the transaction has a "particularly high rate of effecting deferred variable annuity

exchanges." We believe that this type of information is more appropriately collected and analyzed in the context of exception reports which is what many firms already do. We do not believe it is an appropriate factor for a suitability review of a particular transaction which should be analyzed on the basis of the facts and circumstances of the particular transaction and customer in question, not on the basis of the record of the representative. Accordingly, we recommend that this requirement be deleted.

Again, we appreciate the opportunity to comment. If we can answer any questions or be of further assistance, please contact me at (703) 707-8830, extension 20, or Judith Hasenauer at (954) 545-9633. Ms. Hasenauer chairs NAVA's Regulatory Affairs Committee.

Sincerely,

Michael P. DeGeorge

Michael P. DeGeorge
General Counsel