February 28, 2007

I am writing to you on behalf of MWA Financial Service Inc. to share my concerns about Amendment No. 3 to SR-NASD-2004-183 ('Proposed Rule') filed by the NASD on November 15, 2006. The Proposed Rule would result in the adoption of a new rule, Conduct Rule 2821, to create recommendation requirements (including a suitability obligation), principal review and approval requirements, supervisory procedure requirements, and training requirements tailored specifically to transactions in deferred variable annuities ('VAs').

Because my firm has significant concerns about the provisions of the Proposed Rule, we urge the SEC to solicit additional comments from the industry before adopting the Proposed Rule. My concerns include the following:

1. It is unreasonable for the SEC to expect the reg reps to "determine" (sounds like certainty and finality), which no one can reasonable do. I also believe the SEC language is setting the industry up for a fall. It will put us in a "catch 22", the investors will not be protected by the "determine" language. The final determiner of suitability will be the NASD or the SEC and it will be well after the fact. Hindsight is always very enlightening, unfortunately no rep, I know, has a crystal ball nor can they read their customer's mind. They can however, collect the facts, know their customer and have a reasonable basis to recommend a transaction is suitable based on the information provided by the customer.
Suitability Standard - Paragraph (b)(1)(A) of the Proposed Rule prohibits a registered representative from recommending the purchase or exchange of a VA unless he/she 'has determined that the transaction is suitable in accordance with Rule 2310.' This new language raises the bar for suitability determinations by requiring the registered representative to determine his recommendation is suitable, rather than simply having 'reasonable grounds for believing that the recommendation is suitable' as required by Rule 2310. As a result, we believe the language in this paragraph should be amended to read as follows:

(b) Recommendation Requirements
(1) No member or person associated with a member shall recommend to any customer the purchase or exchange of a deferred variable annuity unless such member or person associated with a member has a reasonable basis to believe
(A) that the transaction is suitable in accordance with Rule 2310.

2.Obligation to Inform Customers of Various Features of VA Products - Subsection (b)(1)(A)(i) of the Proposed Rule prohibits a member from recommending the purchase or exchange of a VA to a customer unless, among other things, it has a reasonable basis to believe that the customer has been informed, in general terms, of 'various' features of VAs including specific features which are delineated in the Proposed Rule. The use of the word 'various' in this provision creates an unacceptable level of ambiguity. The prior proposal required the disclosure of 'material' features of VAs. This language is preferable and should be reinserted into the Proposed Rule

3.Product Specific Suitability Criteria - Paragraph (b)(2) of the Proposed Rule provides that a member must make reasonable efforts to obtain certain product specific suitability information about the customer prior to recommending a VA purchase or exchange. Although we support the NASD's listing of the specific suitability criteria necessary to support a recommendation, we are concerned that certain product specific criterion listed by the NASD is either unclear or irrelevant to a suitability determination. We have the following specific concerns about the suitability criteria delineated by the rule:

.Investment Experience - NASD's inclusion of 'investment experience' as a criterion for determining suitability should be clarified. Is it the NASD's intention that it apply to the VA itself, the sub-accounts or both? Without some guidance, the industry is exposed to future interpretation without precedent or notice. Further, is it the NASD's perspective that no prior investment experience renders a purchase recommendation unsuitable?

.Intended Use of the Deferred Variable Annuity - We are concerned about the use of the term 'intended use of the VA?' How is this different from the customer's investment objective? Is either estate planning or tax deferral a legitimate "intended use" or would the NASD require a more detailed analysis? We would ask that the NASD elaborate on the meaning of this term or remove it completely from the rule.

.Existing Assets - The Proposed Rule has been amended to require the financial advisor to make reasonable efforts to obtain information concerning the customer's 'existing assets (including investment and life insurance holdings).' This language is overly broad in that it could potentially require representatives to obtain information about assets that have no impact on the suitability of their recommendation (e.g., automobiles or jewelry owned by the customer). We would recommend that the requirement be amended to obligate the representative to make reasonable efforts to obtain information concerning the customer's 'investable assets.'

4.Principal Review Standard - Paragraph (c) of the Proposed Rule requires a registered principal to 'review and determine whether he or she approves of the purchase or exchange of the deferred variable annuity.' The Proposed Rule goes on to say that 'a registered principal shall approve the transaction only if the registered principal has determined that there is a reasonable basis to believe that the transaction would be suitable' based upon the suitability criteria delineated in the recommendation requirements of the rule. This language obligates the registered principal to make a separate suitability determination thereby placing him in the same shoes as the financial advisor making the sale without the benefit of meeting with the client to discuss their financial situation and objectives. This appears to be a significant deviation from the requirements of 3010(d)(1) which states in relevant part:

Each member shall establish procedures for the review and endorsement by a registered principal in writing, on an internal record, of all transactions... Such procedures should be in writing and be designed to reasonably supervise each registered representative. Evidence that these supervisory procedures have been implemented and carried out must

be maintained and made available to the Association upon request.

As a result, we believe the language in the Proposed Rule paragraph should be amended to read as follows:

(c) .a registered principal shall consider the factors delineated in paragraph (b) of this rule in considering whether to approve or disapprove of the purchase or exchange of the deferred variable annuity.

My firm wholeheartly agrees with the above statement. Our principals do not have the luxury of meeting face to face with the clients and therefore can only make a reasonable decision based on the information provided.

5.Time Frame for Principal Review and Approval - The Proposed Rule requires a registered principal to review and determine whether he approves of a VA purchase or exchange within two business days of the date the member transmits the customer's application to the issuing insurance company. The registered principal is granted three additional business days, for a total of five business days, if it is necessary in the course of the review to contact the customer or financial advisor. This limited review period is problematic for member firms and seems to have been arbitrarily adopted. While we understand that the NASD believes that requiring completion of the principal review within this time frame is necessary for the protection of investors, we fail to understand how investors would be harmed if another appropriate time frame were adopted. Should the Proposed Rule be adopted, many independent broker-dealer firms (IBDs) may require original VA applications, client checks, and other transaction documents to be forwarded to their home office compliance department for review and approval prior to transmission to the issuing insurance company. This procedure would provide the home office with greater control over the principal review process and the ability to insure compliance with the time frame for such review. This procedure, however, has the potential to cause IBD firms who act as introducing broker-dealers to run afoul of custody of funds rules if they attempt to make use of the full principal review time frame. As a result, IBD firms adopting this procedure are limited to a single business day for principal review. This appears entirely unreasonable and contrary to the investor protection goals of the Proposed Rule. In addition, compliance with the Proposed Rule will require member firms to track the date of transmittal and approval thus creating additional recordkeeping burdens. As a result, we would suggest that the Proposed Rule b e revised to require the completion of principal review within a reasonable time-period (not to exceed the expiration of the free look period) following the date the member transmits the VA purchase or exchange to the issuing insurance company.

6.Variable Annuity Exchange Supervisory Procedures - Paragraph (d) of the Proposed Rule requires member firms to 'implement surveillance procedures to determine if the member's associated persons have rates of effecting deferred variable annuity exchanges that raise for review whether such rates of exchanges evidence conduct inconsistent with the applicable provisions' of the Proposed Rule. We object to this requirement because the information may be unavailable to member firms due to a client's reluctance to share

such information or the legitimate privacy policy concerns of the prior broker-dealer or insurance company. As a result of these concerns, the NASD should amend the Proposed Rule by stating that it is the registered principal's obligation to consider prior VA exchange information if it is available to him at the time of his review. However, if the SEC and NASD choose not to amend the Proposed Rule in this fashion, we would ask that they provide additional clarif ication concerning its requirements. Specifically, what does the term 'rate of . exchanges' mean? Does the NASD mean to refer to a percentage of the financial advisor's total VA business or instead to a percentage of the financial advisor's customer base? What is the relevant period for measuring the rate of exchanges? What is the yardstick by which a financial advisor's rate of exchanges should be compared to determine whether it is high? What is a member to do if it believes the individual exchange transactions to be suitable although they have occurred at a high rate? Finally, this provision is particularly troublesome as it seems to infer that broker-dealers have the technology available to be able to monitor this exchange activity. In our experience, they simply do not.

7.Training - In general terms, we support the NASD's desire to increase the knowledge and awareness of financial advisors and principals who are involved in the sale or approval of VA transactions. These are complex products and their features and internal costs vary widely. It is important for representatives and principals to fully understand the product features to ensure they meet the client's specific needs. Nevertheless, we remain concerned about the Proposed Rule's requirement that member firms develop training policies and programs 'reasonably designed to ensure' that financial advisors and registered principals involved in the sale and supervision of VA products comply with the requirements of the Proposed Rule and understand the material features of VAs. Unfortunately, even the best training policies and materials will not "ensure" such understanding. Instead the obligation to understand the material features of the product a financial advisor sells to his clie nt is inextricably bound up in NASD Conduct Rule 2310's requirement that a member make suitable recommendations to his client. Therefore, there is no apparent need for this additional training requirement that will merely create new books and records obligations for member firms. In addition, we note that several recent NASD rule proposals (e.g., the gifts and business entertainment proposal contained in NtM 06-06) have sought to impose separate and unique training requirements. We believe that the NASD should refrain from educational mandates and instead rely upon the firm element continuing education provisions of NASD Conduct Rule 1120. This approach allows NASD member firms to evaluate and prioritize their financial advisors' training needs and design a program that is appropriate to the task. The NASD would then have the opportunity to review the firm's training program for compliance with the minimum standards outlined in Rule 1120. If the firm's financial adviso rs engage in a significant volume of VA transactions, the training program would be required to focus significant attention to the general investment features and risk factors associated with these products. If, however, the firm's financial advisors do not sell VA products, or have not been the subject of VA related complaints or arbitrations, training assets could be dedicated to training on more relevant topics. In this way, IBD firms can more effectively allocate their training resources to address the unique needs of their firms.

8.Unintended Consequences - We fear that the Proposed Rule will ultimately harm customers by raising the barriers to their access to VA products. Singling out VAs for more stringent suitability requirements is likely to inhibit the sale of this important financial product. Financial advisors may unconsciously 'choose' to offer less suitable products because of the additional paperwork, procedures, and supervisory review involved in the sale of VAs. The result may very well be that VAs become less available to those who could benefit from them as legitimate vehicles for tax-deferred savings, estate, and retirement planning. We recognize that there have been some serious abuses involving the sale and exchanges of VAs. However, we do not believe the sales abuses have occurred because the NASD's rules and enforcement mechanisms were not strong enough to prevent them. Therefore, we urge the NASD to place additional emphasis on the enforcement of the existing Conduct Rules. In addition, we believe that more meaningful disclosures to customers via sponsor-created prospectuses or a disclosure document suggested by the NASD's Annuity Roundtable working groups will ultimately help to eliminate most sales practice abuses.

As a result of these concerns, we urge the SEC to solicit additional industry comment before adopting the Proposed Rule.

The majority of this letter is written by FSI, however I want you to know it is supported and endorsed by MWA Financial Services and we have the same concerns about this proposal. If indeed, investor protection is the goal, then draft the rule to protect the customer and not to provide the NASD with the vagueness and ambiguity, which will inevitably end in enforcements which rely on hindsight. Give us rules which will guide us to do the right thing for the customer and not hang us if we did not interpret them to the NASD's satisfaction.

Sincerely,

Ms. Pam Fritz
Chief Compliance Officer
MWA Financial Services