



NASAA

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VIA EMAIL: rule-comments@sec.gov

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

RE: File No. SR-NASD-2004-183: Proposed Rule Governing the Purchase, Sale, or Exchange of Deferred Variable Annuities

Dear Mr. Katz:

This letter is submitted by the North American Securities Administrators, Inc. (NASAA) in response to the latest amendments to the Proposed Rule Governing the Purchase, Sale, or Exchange of Deferred Variable Annuities. We appreciate the opportunity to comment on certain aspects of the proposed rule, as detailed above.

A. The Proposed Rule Should Cover All Variable Annuity Transactions, Not Just Deferred Variable Annuity Transactions

NASAA supports the proposal of a rule dealing specifically with Variable Annuities, but believe that the proposed rule should cover all variable annuity transactions, not just deferred variable annuity transactions. For many years now, variable annuities sales practice violations have been in our Top Ten Scams, Schemes and Scandals. Sales practice violations and supervision practice and procedures to prevent sale practice violations regarding the sale or exchange of Variable Annuities have been a major concern for all securities regulators.

NASAA is particularly concerned that that the proposed rule should also cover the sale of an immediate variable annuity as well as a deferred variable annuity for many reasons. A member must have the same reasonable basis of fact in recommending this type of variable annuity. The customer has the same legal right to be informed of the costs and risks associated with the purchase of an immediate variable annuity. We believe that NASD members have the same legal responsibilities of principal review, documentation and supervisory requirements as specified in Rule 3010 and 3110 for an immediate variable annuity. Because NASAA's view is that the requirements and legal responsibilities surrounding immediate and deferred variable annuity transactions are equivalent, the proposed rule should expressly include provisions governing all variable annuity transactions.

B. Exemption for Tax-Qualified, Employer-Sponsored Retirement or Benefit Plans

Proposed Rule 2821(a) (1) does not apply to deferred variable annuity transactions made in connection with tax-qualified, employer-sponsored retirement or benefit plans that either are defined as a "qualified plan" under Section 3(a) (12) (C) of the Exchange Act or meet the requirements of Internal Revenue Code Sections 403(b) or 457(b) unless a member makes recommendations to the plan's individual participants. NASAA is supportive of this change. This provision is vitally important in cases in which the plan sponsor, trustee or custodian is unsophisticated or primarily relies upon the recommendations of the member or associated persons.

C. Risk Disclosure Document

The revised rule no longer requires a “(s) eparate, brief and easy to read (written in “plain English”) risk disclosure document...” which would be provided to the client prior to affecting any sale. NASAA would recommend that a risk disclosure document be required. The plain-English disclosure of Variable Annuities is of utmost importance.

Because variable annuities are indeed complex investment products and there has been a high rate of customer complaints indicating that investors did not understand the features of variable annuities, NASAA supports the provision that a separate risk disclosure document should be provided in addition to the prospectus. A potential investor is more likely to read the brief and easy-to-read disclosure document compared to the prospectuses; thus, a risk disclosure document that discloses specific and general information should be more beneficial to a potential investor.

The purpose of a risk disclosure document is to inform prospective investors about the risks and facts that may have an adverse impact on their investments. Product specific information is essential because it helps potential investors understand the complicated features of each specific product such as market risks, fees, liquidity and taxes. General information about the risks and facts about the variable annuities being offered is just as important because such information allows reasonable investors to make informed decisions and determine whether such products are suitable investments. Among the general information included in the risk disclosure document should be: a) advantages and disadvantages of investing in variable annuities; b) other products that may be suitable for the investor; c) the distributors’ policies on combating excessive trading; and methods of pricing.

D. Recommendation Requirements

NASAA agrees with and commends the NASD for including the requirement under proposed Rule 2821 (b) (1) (C) that the member or associated person has a reasonable belief that the customer has a need for the features of a variable annuity as compared with other investment vehicles and that the registered principal under proposed Rule 2821(c) (1) (A) reviews for such comparison. See also, proposed Rule 2821(d)(1). NASAA believes that unless such comparisons are made, the customer would be unable to make an informed decision regarding the purchase or exchange of the variable annuity product.

E. Principal Review Should Include a Periodic Review of the Associated Person’s Production Report for Variable Annuities

NASAA notes that the revised deadline of principal review under this amendment to proposed Rule 2821(c)(1) would allow for a two-day review period after transmitting a customer’s application for a deferred variable annuity to the issuing insurance company for processing. This provision requires a registered principal to review and determine whether he or she approves the purchase or exchange of the deferred variable annuity, regardless of whether the transaction has been recommended, is of vital importance to investor protection. This new deadline would ensure that the principal has enough time to do a complete review of the application while still preserving the customer’s free look period.

NASAA also agrees with and commends the NASD for including under proposed Rule 2821(c)(1)(D) that the Registered Principal’s review must consider such things as surrender charges on the replaced policy, the impact of new surrender schedules, loss of benefits, increased fees, and previous exchanges by that customer. NASAA also applauds the NASD for requiring that members implement procedures to screen for and require a registered principal’s review of a deferred variable annuity transaction where the associated person effecting the transaction has a particularly high rate of effecting deferred variable annuity exchanges. However, NASAA also reiterates our belief that the registered principal should review the total sales and production of variable annuities of the associated person(s) to detect unsuitable sales and other potential abuses. This would permit the

registered principal to detect possible patterns of sales practice violations that reviews on a sale-by-sale basis may not reveal.

NASAA believes that it is appropriate to require members to review both recommended and non-recommended variable annuity transactions, as is proposed by the new rule. The complexity of the product and abuses by associated persons necessitate principal review of all variable annuity transactions.

F. If Hypothetical Illustrations are Used, the Rule Should Require Illustrations That Are Not Misleading

NASAA reiterates our concern that the proposed rule should include a provision that specifically addresses the use of hypothetical illustrations in variable annuity transactions. NASAA shares the NASD's concern that some tax-deferral illustrations may rely upon incorrect or misleading assumptions. NASAA members have also experienced problems with agents improperly using general mutual fund illustrations instead of illustrations regarding specific variable annuity sub-accounts, i.e., using the net asset value (NAV) of the parallel retail mutual fund instead of the accumulated unit value (AUV) of the variable annuity sub-account in illustrating a hypothetical performance.

The problem arises because investments through a variable annuity sub-account and through the retail mutual fund are not the same. Consequently, customers are likely to be misled about, among other things, the expenses associated with the variable annuity and the sub-account(s). The proposed rule should require member firms to review on an ongoing basis marketing communications that use hypothetical illustrations. Even absent a specific rule, firm training policies and programs should ensure that hypothetical illustrations fully and fairly disclose all of the material features of variable annuities and sub-accounts.

Thank you for your consideration of NASAA's views on these issues. If you have any questions regarding these comments contained in this letter, please do not hesitate to contact Tanya Solov, Director of the Illinois Securities Department and Chair of NASAA's Broker-Dealer Section (tsolov@ilsos.net), or John Cronin, Chair of the Broker-Dealer Variable Annuities Project Group (jcronin@bishca.state.vt.us).

Sincerely,

A handwritten signature in black ink, appearing to be 'Patricia D. Struck', with a long horizontal line extending to the right.

Patricia D. Struck
President, North American Securities Administrators Association
Wisconsin Securities Administrator