

PARK AVENUE Securities

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Via Electronic Mail

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Barbara Z. Sweeney
NASD
Office of the Corporate Secretary
1735 K Street, NW
Washington, D.C. 20006-1500

Re: Comment on Proposed Rule Governing the Purchase, Sale or Exchange of Deferred Variable Annuities – NASD Notice to Members 04-45

Dear Ms. Sweeney:

Park Avenue Securities LLC (“PAS”)¹ appreciates the opportunity to comment on the NASD’s proposed Rule to impose specific sales practice standards and supervisory requirements on members for transactions in deferred variable annuities as discussed in Notice to Members 04-45 (“NTM 04-45”).

NTM 04-45 states that “[i]n general, NTM 99-35 served as the basis for the proposed rule.” PAS supports the “best practice” guidelines in NTM 99-35 and agrees that a proposed rule that would codify those guidelines into the NASD’s Conduct Rules is appropriate and timely in light of current concerns. However, the proposed Rule goes significantly beyond those guidelines and would impose obligations which are impractical, burdensome, unclear and unwarranted. We will briefly list our objections below.

Proposed Point of Sale Risk Disclosure Brochure – We believe that this potential requirement would lessen, rather than enhance, the quality of disclosure to variable annuity purchasers and would be burdensome and impractical as well. PAS distributes a large number of deferred variable annuities, many of which are issued by non-affiliated insurers. The proposed Rule would require PAS to be responsible for developing, reviewing and distributing numerous Risk Disclosure Brochures with significant attendant expense and risk. In the event of a prospectus revision or other change affecting the risk disclosure issues – including any tax change or any state law change affecting variable insurance products such as “free look” provisions – these documents would have to be reviewed, updated and changed as necessary. PAS compliance and supervisory procedures would be required to ensure that the current documents which meet the requirements of the proposed Rule have been given to customers along with the prospectus and any other required documents. This would prove burdensome, impractical and very costly without a commensurate benefit to investors. First, the proposed Rule directs broker-dealers, not insurers, to ensure that the documents comply with the standards set forth in the proposed Rule. The proposed Rule could therefore result in a lack of uniformity across different broker-dealers who distribute the same annuities resulting in certain confusion for the investing public. Second, the information required in the proposed Rule, other than the provision relating to a specific state’s “free look” rules and the provision relating to principal review, is entirely contained within the prospectus under current rules. The SEC, the insurance industry and numerous trade groups have worked together for a long time to enhance the quality of the prospectus disclosures regarding variable products. It is not clear just why the NASD believes that the results of those efforts are

¹ PAS is a broker-dealer that is indirectly owned by The Guardian Life Insurance Company of America, a New York mutual life insurance company (“Guardian”), and is registered with the United States Securities and Exchange Commission and a member firm of the NASD. Substantially all of the approximately 2,800 registered representatives of PAS are also career force insurance agents of Guardian.

inadequate or whether the benefits of “dumbing down” the prospectus in certain limited respects outweigh the consequences. Finally, we believe that the proposed Rule is premature in light of the SEC’s pending point of sale disclosure proposal.

Rather than require broker-dealers to create, maintain and distribute a new document using information the SEC currently requires insurance firms to disclose, PAS believes the NASD should consider as an alternative the brochures already developed by the NASD (“Variable Annuities – Beyond The Hard Sell” and “Should You Exchange Your Variable Annuity”) or the SEC (“Understanding Your Variable Annuity”), all of which are already posted on the internet, and which reflect the sort of critical information regarding these products which the NASD and the SEC believes the investing public should have.

Content of Principal Review – PAS has no objection to the content of principal review in the proposed Rule, with two exceptions. First, the proposed Rule would require the principal to know the replacement/exchange rates of both the customer and the agent/representative. This information goes well beyond what is contained within an application and the related paperwork and, in the case of a customer or an agent who is new to the broker-dealer, not necessarily reflected in any books and records kept by the broker-dealer. Such information is more logically reviewed in post-trade surveillance, rather than in pre-trade suitability review. Second, the proposed Rule would require some action by the principal in cases of purchases in a tax-qualified account. PAS believes that issue is one more appropriately dealt with through disclosure (i.e., the prospectus) than through principal review. Many variable annuity applications include a confirmation signed by the customer that a prospectus has been delivered and may also contain specific acknowledgment that purchases of a variable annuity in a tax-qualified account are made for benefits the contract provides other than the tax deferral. Apart from examining the paperwork submitted with an application, there is little else a reviewing principal ought to do to ensure that there is no concern in this regard.

Timing of Principal Review – The proposed Rule simply sets an impossibly high standard by requiring a one-day review. Like many other broker-dealers, PAS representatives may work from remote or “detached” locations and submit applications and related paperwork to the representative’s branch office or office of supervisory jurisdiction for principal review. The paperwork is subsequently submitted to the PAS home office principal. If the information necessary for review (such as the client’s investment background) is not a part of the application, additional time may be required to complete the review process. Given the distribution channels and operations standards affecting deferred variable annuities, as well as contract delivery and “free look” provisions established by state law, PAS believes that no set time period should be a part of any ultimate Rule.

Standards for Principal Review – Broker-dealers affected by NTM 99-35 have now had almost five years of experience utilizing its guidelines. PAS supports a regulatory approach that leaves it up to each broker-dealer to develop and maintain specific procedures that follow the guidelines included in NTM 99-35. PAS invites senior NASD representatives to engage the industry, including insurers, in an open dialogue prior to any rulemaking regarding setting specific standards with regard to age, contribution relative to income or net worth, marital status or tax bracket, etc. For many of these factors, we believe that there is a need for flexibility on a case-by-case basis.

Creation and Review of a Principal Exchange Replacement Document – PAS submits that requiring on such a document a “summary of all significant differences” in “contractual provisions, guarantees, death benefits, withdrawal provisions and/or tax treatment” goes well beyond most state replacement forms, and thus would become a required document in most cases of replacement or exchange. Again, this would be time-consuming, expensive and lead to non-uniform results as different broker-dealers make different (and potentially risky) judgments of what a “significant” difference is. In addition, because the proposed Rule contains no definition of “exchange” or “replacement”, the result would put broker-dealers at risk to the extent the NASD subsequently adopts (or examines for) a functional definition broader than a given state’s insurance law or regulation.

Other Comments on the Proposed Rule – PAS offers three additional comments on the proposed Rule. First, NTM 04-45 contains no discussion of distribution channels or group sales. If the NASD deems it appropriate to specifically regulate deferred variable annuities then suitability standards ought to reflect issues germane to, e.g., distribution through “wholesale” broker-dealers and group sales such as through ERISA-qualified retirement plans. PAS submits that in such cases the NASD ought to clarify just who is responsible for suitability determinations and the content of those determinations. Given that the underlying predicate for the proposed Rule cited in NTM 04-45 relates to customer complaints and observations cited in the recent Joint Staff Report, PAS believes the NASD’s concerns relate predominantly to deferred variable annuity sales made to individual persons by a registered representative outside the employee benefits context. Second, the proposed Rule relates to “purchases” as opposed to initial purchases, and PAS believes that the NASD should clarify that the specific sales practice standards and supervisory requirements it seeks to impose relate only to initial purchases. Finally, the proposed Rule covers only deferred variable annuities. Yet the discussion of the product’s “complexity” relates to all annuities, not just deferred variable annuities. If deferred variable annuities are to be singled out for specific sales practice standards and supervisory

requirements, there exists a possibility that replacements or new sales may be driven to other products such as equity indexed annuities, which given the applicable regulatory framework can be much more difficult for broker-dealers to supervise and may be much less advantageous to investors than a deferred variable annuity. The NASD should give very careful consideration to the possibility that if adopted as written the proposed Rule puts deferred variable annuities at a competitive disadvantage compared to other products that are just as complex and could have as a consequence an increase in replacements, exchanges or new sales involving such products with no obvious demonstration that such activity is in investors' best interests.

PAS appreciates the opportunity to comment upon the proposed Rule and looks forward to a meaningful and open dialogue with the NASD, the insurance industry and the SEC to better coordinate regulatory efforts and ensure that variable annuity sales are not associated with inappropriate sales practices or poor supervision.

Very truly yours,

Joanne B. Mack
President, Park Avenue Securities, LLC