

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

RE: NTM 04045

Dear Ms. Sweeney:

This letter will outline our comments regarding the NASD proposed new rule governing the purchase, sale or exchange of deferred variable annuities. Sterling Financial Partners is a financial intermediary organization that provides advice to insurers, broker-dealers and similar organizations with respect to annuities and other insurance products.

Our specific concern with the proposed new rule involves Paragraph (b)(2) that relates to exchange or replacement of variable annuity contracts. The proposed new rule does not take into consideration suitability issues relating to the exchange or surrender of existing variable annuity contracts where the contract owner's basis in the contract exceeds the current contract value.

With respect to sale or surrender, we believe that any suitability consideration should include whether the contract holder's basis exceeds the current contract value. Owners of variable annuity contracts that have a value that is below the basis in the contract can surrender or sell such a contract and, subject to the normal limitations applicable to miscellaneous tax deductions, deduct the amount of the loss on the contract from their taxable income for Federal income tax purposes. This loss may be of sufficient magnitude to justify the sale or surrender of the contract.

With respect to exchanges, suitability considerations should recognize that a "tax-free" exchange of a variable annuity that is in a loss position precludes realizing a tax loss now in favor of maintaining a higher basis to possibly reduce taxes at some future point. Suitability screening should recognize that a sale or surrender of the contract now will generally be more appropriate.

In view of these important tax considerations, we respectfully request that any suitability criteria take them into consideration when finalizing the proposed new rule.

Sincerely
Brian E. Hawley
Principal
Sterling Financial Partners