Robert S. Jones
Chairman of the Board
AXA Advisors, LLC

Jerald Hampton
Chief Executive Officer
AXA Distributors, LLC

August 9, 2004

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

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

Dear Ms. Sweeney,

This letter is submitted by AXA Advisors, LLC ("AXA Advisors") and AXA Distributors, LLC ("AXA Distributors") in response to the solicitation of comments by the National Association of Securities Dealers, Inc. ("NASD") with respect to its Notice to Members 04-45 regarding a proposed rule (the "Proposed Rule") that would impose specific sales practice standards and supervisory requirements on NASD members for transactions in deferred variable annuities ("variable annuities").

Background

AXA Advisors and AXA Distributors (together, "we" or "our") are registered broker-dealers under Section 15(b) of the Securities Exchange Act of 1934 and members of the NASD. Both AXA Advisors and AXA Distributors are wholly-owned subsidiaries of AXA Financial, Inc. ("AXA Financial"). AXA Financial is a diversified financial services company. Its principal operating subsidiaries, in addition to AXA Advisors and AXA Distributors, include The Equitable Life Assurance Society of the U.S. ("Equitable Life"), MONY Life Insurance Company, MONY Life Insurance Company of America, U.S. Financial Life Insurance Company, the Advest Group, Alliance Capital Management L.P. and Enterprise Capital Management. Through its insurance subsidiaries, AXA Financial is one of the country's leading issuers of variable annuities.

AXA Advisors distributes variable annuities, other fixed and variable insurance products, mutual funds and other investment products through approximately 5,000 registered representatives nationwide. In addition to products issued by Equitable Life and other AXA Financial affiliates for which it acts as principal underwriter and distributor, AXA Advisors also distributes, through its retail sales force, insurance and investment products issued and/or managed by dozens of the country's leading financial services firms.

AXA Distributors distributes fixed and variable annuity and life insurance products issued by Equitable Life, for which it acts as principal underwriter and/or general agent, on a wholesale basis through a broad range of national and regional securities firms, banks, and other broker-dealer distributors.

Proposed Rule

We appreciate the opportunity to comment on the Proposed Rule. At the outset, we wish to acknowledge the constructive evolution of the NASD's thinking with regard to the proposal, and in particular, the decision to model much of the proposal on the best practices guidelines set forth in NASD Notice to Members 99-35 ("NTM 99-35") instead of NASD Rules 2860 and/or 2865 as initially announced. Moreover, we unreservedly concur that member firms must maintain effective procedures to assure that recommendations with regard to variable annuities are suitable, that transactions involving variable annuities are appropriately supervised and that variable annuity purchasers are provided with all appropriate disclosures necessary to promote a thorough understanding of the product purchased. While we are not convinced that there is a factual basis to conclude that current regulatory requirements are inadequate in this regard, in general we are supportive of the provisions of the Proposed Rule to the extent that they simply seek to codify the best practice requirements of NTM 99-35.[1]

We cannot, however, support those provisions of the Proposed Rule that would: (1) seek to mandate that member firms develop and utilize a supplemental point-of-sale risk disclosure document in addition to the prospectus required to be delivered pursuant to the federal securities laws; (2) impose more onerous principal review requirements – particularly with regard to turnaround time – than apply to other securities generally; (3) require member firms, with regards to an exchange or replacement, to provide the customer *in writing* "a summary of all significant differences" between the existing and proposed new contracts; or (4) compel the delivery of the prospectus prior to effecting a transaction. Such provisions, we submit, are highly impractical and would impose very substantial additional burdens on member firms without meaningfully enhancing the protection of investors. Indeed, we believe that such provisions, if adopted, have the potential to so substantially burden the distribution of variable annuities that they could meaningfully limit consumer access to such products.

Variable Annuities

Variable annuities are among the most innovative and flexible financial products in the marketplace today. Principally designed to assist investors who are accumulating funds for retirement, they typically offer a range of investment options, including portfolios investing in stocks and/or bonds, as well as, in many cases, fixed interest and/or fixed maturity options that offer principal protection.

---

[1] NASD reports that part of the impetus for the Proposed Rule is the recent rise in customer complaints received by the Securities Exchange Commission (the "SEC") and NASD itself. We find this reported trend particularly puzzling since it seems to be at odds with our own experience and also appears to be inconsistent with statistics derived from published NASD Disciplinary Actions. Based on statistical analysis done by the American Council of Life Insurance, we understand that, on an annual basis, only 8% of the NASD published disciplinary actions over the past 8 years involve or are related to insurance or annuities. Only 2% of that 8% involves suitability, meaning that of the total published disciplinary actions by the NASD these suitability actions represent .16% of the NASD's total disciplinary actions. We submit that these percentages are especially noteworthy when considering that registered representatives working for broker-dealers associated with life insurers account for over 50% of the NASD's 765,000 registered representatives.

Although tax law changes have reduced, on a relative basis, some of their tax advantages, variable annuities continue to permit investors the opportunity to transfer funds among investment options on a tax-free basis and to accumulate funds on a tax-deferred basis.[2] However, what truly sets variable annuities apart from other investments today is the range of innovative income, accumulation, withdrawal and death benefit guarantees they offer – guarantees that are not available in any other investment product. These guarantee features, some or all of which are offered by a large percentage of the most popular variable annuities in the market, allow investors the opportunity to invest in a range of stock and bond investment options knowing that *regardless of market performance* they are assured of guaranteed minimum levels of income beginning at a future date and/or the ability to withdraw (or be able to pass at death) at least the full principal invested, and typically more.

Such benefits, many of which didn't exist until relatively recently,[3] have become increasingly popular with investors, many of whom are confronting the confluence of longer life expectancies, earlier retirements, continued declines in employer-provided defined benefit pension plans and increasing concerns over the future of Social Security. Changing demographics, particularly the aging of the baby boomers, is also driving consumer demand for variable annuities. Between 2000 and 2025, the number of Americans aged 65 or older is expected to nearly double. A larger and larger percentage of such individuals will retire without the benefit of a traditional defined benefit pension plan providing income for life. Instead, a growing percentage will simply receive a lump sum payout at retirement from a company-provided or self-directed defined contribution pension plan. Experts agree that most recipients of these lump-sum distributions will be ill-equipped to effectively manage the payouts to produce the necessary resources to last for their lifetime. Due to the unique capabilities of insurance companies to manage longevity risk, annuities are the <u>only</u> financial product that can provide an income stream that can't be outlived.

Accordingly, and without minimizing the importance of assuring that annuity purchasers understand what they are buying and that their annuity purchases are suitable, we submit that investors would not be well-served by regulations which unnecessarily impair their ability to access the very products that exploit those unique capabilities. We fear that several aspects of the Proposed Rule may well have such affect. Those aspects are discussed below.

---

[2] Of course, the portion of annuity distributions reflecting investment gains are generally taxed at ordinary income rates which can be higher than capital gains rates which may apply to some or all of the distributions from mutual funds or other investments.

[3] Unlike mutual funds, which, except for the introduction of share classes have offered few if any additional features over the past 50 years, variable annuities have seen an enormous growth in feature/functionality in recent years. Such changes have included dramatic enhancements to death benefits which were previously limited to return of invested principal but which now include a variety of options in certain contracts that, e.g., can serve to protect unrealized appreciation in account value and/or to provide a specified minimum annual increase in death benefits regardless of account performance. Other changes in recent years have been the development of guaranteed minimum income benefit features that assure investors that they will be able to obtain a specified minimum lifetime income stream beginning at some point in the future regardless of market performance in the interim. Still other features provide various levels of principal protection by either assuring that investors can withdraw at least the full principal amount invested (subject to certain annual restrictions) and/or provide a guarantee of minimum account values as of a future date, again without regard to market performance. In our experience, these and other new features – which are only available in variable annuities and have only become available relatively recently – are in large part responsible for the continuing growth in popularity of variable annuity contracts. Moreover, we also believe that the development of these new features, most of which did not exist in contracts issued as recently as seven or eight years ago, helps explain the continuing strong demand by owners of older generation variable annuity contracts to upgrade to contracts to the more feature-rich versions currently being offered.

Principal Concerns

I. *Risk Disclosure Document*

The Proposed Rule would require members to provide customers with a current prospectus and a "separate, brief, and easy-to-read (written in "plain English") risk disclosure document that highlights the main features of the particular variable annuity transaction." We understand that it is the NASD's expectation that such document would be approximately 2-3 pages in length. While no doubt well-intentioned, such requirement is both highly impractical and, in our view, manifestly ill-advised. For starters, as NTM 04-45 acknowledges, "deferred variable annuities are complex instruments." We respectfully submit that it is incongruous to think that it will be feasible for distributors to produce a such a brief, easy-to-read, risk disclosure document that highlights the main features of what the NASD itself acknowledges is such a complex product.

Further, requiring each distributor to produce a risk disclosure document for each variable annuity product it sells is highly impractical and profoundly inefficient. We submit that the typical member firm does not have "on staff" persons skilled in drafting disclosure documents. Particularly for smaller member firms – a category that includes the vast majority of NASD members – the costs of engaging such persons could be prohibitively expensive. Faced with such costs, it is eminently foreseeable that a firm would opt to reduce, if not eliminate altogether, the annuity products it chooses to offer – to the ultimate detriment of its customers. Moreover, requiring dozens if not hundreds of distributors to each produce a risk disclosure document for the same product involves a tremendous duplication of effort, and invites a wide divergence in quality and consistency from firm to firm.[4] And, it's not just member firm resources that are implicated by such requirement. Since such disclosure documents would be designed for use with the public, almost certainly some form of regulatory or self-regulatory review would be required. Even if the NASD remains unpersuaded that such an inefficient use of the limited resources of member firms is unwise, we submit that it cannot be as sanguine with regard to its own scare resources.

In addition to being unwise, however, we also believe that such requirement is unnecessary. We reach this conclusion, not because we don't see some merit in a summary explanation of the key attributes of variable annuities, but rather because something very similar to what the Proposed Rule would require each member firm to individually create *already exists*. Indeed, much of what the Proposed Rule would require in the risk disclosure document is already set forth in summary fashion in the forepart of the prospectus, in what is typically captioned the "prospectus summary" section and the accompanying SEC-mandated fee table. Such prospectus summary and fee table, which together can run six or more pages, commonly provide an abbreviated description of the features, benefits, costs and risks of the product. Of course, the way in which the summary and fee table accomplish so much in such a short space is to make fairly liberal use of cross references to more detailed discussions appearing elsewhere in the prospectus – a time-honored approach, which is both practical and pragmatic in the context of an integrated disclosure document. Moreover, we would submit, it is a format with which consumers are readily familiar from the non-financial aspects of their lives. Whether it is the owner's

[4] Additionally, given the SEC's pending rule proposal also requiring point of sale disclosure, distributors would potentially not only be confronted with several separate and overlapping requirements, but also be responsible for the preparation of the respective documents commensurate with such requirements.

manual of a new car, DVD player, computer, etc., consumers have come to understand that the first few pages will likely consist of the executive summary or other short-form introduction to the more detailed description that follows. Given our belief that consumers already have an intuitive sense of how to deal with lengthy documents, we suggest it would be far more constructive to encourage member firms to help consumers make use of the summary information *that already exists* than to require every member firm to recreate it.

Such an approach would have the added benefit of obviating one of the most significant objections to the risk disclosure document – the potential exposure that it would impose on member firms for substantive product disclosures – liability that today, for all practical purposes, is borne by the issuer. Requiring member firms to take on such liability would, we submit, set a terrible precedent. Moreover, the very specter of such liability – particularly 10b-5 liability based on omissions of material facts [5] – will render it even less likely that the member-created risk disclosure document will be brief or easier to understand than a prospectus (which, of course, is already required to conform to "plain English" guidelines). Indeed, as noted above, the reason that the prospectus summary can be as short as six pages is that much of what it says is qualified by cross references to more detailed disclosures occurring later in the body of the prospectus. Given that the risk disclosure document will not be part of the prospectus, member firms may well be more reluctant to rely on external cross-references to supply important supplemental information. And the consequence of their reluctance, predictably, will be longer and longer "summary" documents. [6]

II. *Principal Review*

[5] Rule 10b-5(2) of the Securities Exchange Act of 1934, as amended.

[6] Although, for the reasons noted above, we are strongly opposed to the creation of yet another disclosure document, if separate, supplemental disclosure were deemed to be a regulatory imperative, we submit that it would be far more efficient to mandate that such document be issuer-created. Recognizing that the NASD lacks jurisdiction over issuers, we submit that such a result could best be achieved by the Securities Exchange Commission through appropriate rulemaking. One way in which to approach this could be to amend Investment Company Form N-4 (which governs the content of registration statements for variable annuities) to incorporate, with appropriate modifications, the prospectus summary standards of Item 2 of Form N-6 (the form applicable to variable life contracts) which provides in pertinent part:

> **Risk/Benefit Summary: Benefits and Risks**
>
> Include, in plain English . . . a concise description of the Contract, including, but not necessarily limited to, the following information:
>
> (a) *Contract Benefits*. Summarize the benefits available under the Contract, including death benefits, withdrawal and surrender benefits, and loans.
>
> (b) *Contract Risks.* Summarize the principal risks of purchasing a Contract, including the risks of poor investment performance, that Contracts are unsuitable as short-term savings vehicles, the risks of Contract lapse, limitations on access to cash value through withdrawals, and the possibility of adverse tax consequences.
>
> (c) Portfolio *Company risks.* A statement to the effect that a comprehensive discussion of the risks of each Portfolio Company may be found in the Portfolio Company's prospectus.

Not only would this create more uniform standards for the prospectus summary section of variable annuity prospectuses, such summary section, together with the fee table already required to be included in the prospectus, could also be separately delivered to satisfy the risk disclosure document requirements of the Proposed Rule. And, since it would be part of an SEC-filed registration statement, arguably no incremental regulatory review would be required. Again, while we believe that a compelling argument would continue to exist as to the utility of providing duplicative disclosure at point of sale, such an approach would significantly lessen our other concerns and objections.

NASD's Proposed Rule would also require that a registered principal review and approve a transaction no later than one business day following the date of execution of the deferred variable annuity application. Given that the bulk of variable annuity sales continue to be made via paper applications which are required to be physically routed for both supervisory and processing purposes, and given the level of information that the Proposed Rule would require accompany the proposed application (which seemingly would be both important and time-consuming for a supervisor to review as part of the transaction approval process), and further given the likelihood that an appropriate supervisory review process may well identify issues that require at least some additional inquiry and follow-up (possibly including customer contact), we find such a requirement wholly impractical.

Moreover, we question why the NASD feels it is necessary to single out variable annuities for such treatment. Currently, NASD Rule 3010 (d)(1) requires principals to review, endorse and document their reviews and endorsement of all transactions without imposing a stringent time deadline**.** We are unaware of any demonstration of customer harm that would be assuaged by this new requirement. Indeed, the NASD already imposes stringent prompt forwarding and processing requirements designed to assure that customer funds are promptly transmitted and applied, and that customer transactions are promptly executed. Further, as the NASD has repeatedly acknowledged, life insurance and annuity contracts uniquely provide purchasers the added protection of a "free look" right, which allows purchasers to examine their contract for at least 10 days *after delivery* and get their money back for any reason.

For all of the foregoing reasons, therefore, we see no justification for imposing such an artificially short deadline on the principal review process. Instead, to the extent any further specificity were deemed necessary (and we don't think it should be), we would suggest that it be to require principal review prior to issuance and delivery of the contract.

III. *Replacement Comparison*

The Proposed Rule would also require member firms, in the context of effecting an exchange or replacement of a variable annuity, to additionally provide the customer *in writing* "a summary of all significant differences" between the existing and proposed new contracts. While we absolutely concur that replacement transactions in variable annuities recommended by members and their associated persons – like switches in any other securities – must be suitable and must be appropriately supervised, we must again question why the NASD is singling out variable annuities for such a burdensome supplemental written disclosure requirement. Our experience suggests that the substantial majority of variable annuity replacements occur at some point after the expiration of the surrender charge period on an existing contract, meaning on average 7-10 years after purchase. Surely, the NASD is aware of industry statistics that suggest that average holding periods for other investments, including mutual funds, is substantially shorter. Yet, there seems to be little interest in requiring members to provide comparisons prior to effecting a transaction in other such other securities.

We submit that such incongruity is even more striking when considered against the backdrop of the dramatic changes in feature/functionality that, as noted above (see footnote 3), have occurred in variable annuities over recent years. Indeed, most of the features that are driving sales of variable

annuities today simply were not available (and continue not to be available) on products issued 7-10 years ago. Again, as noted above, this is certainly not true for mutual funds, yet no similar burdensome requirement is sought to be imposed on them (or for that matter on any other security). Particularly in the absence of a demonstrated and substantial pattern of abuse, we urge the NASD to reconsider the requirement of a *written* comparative summary or, at a minimum, limit the requirement to transactions that are sought to be effected prior to the expiration of the surrender charge period on an existing contract.

IV. *Prospectus Delivery Requirements*

We would also like to take this opportunity to endorse the views expressed by the Committee of Annuity Insurers (the "Committee") in its response to the Proposed Rule. Specifically, we underscore the Committee's position on the impracticality, for at least some member firms, of requiring prospectus delivery prior to effecting a transaction and concur that such a requirement is inconsistent with federal securities laws and paternalistic and will likely result in severely restricting member firms' ability to competitively meet the demands of its telephone customers. Particularly in light of the unique free-look provisions described above, permitting member firms the option to continue to deliver the prospectus not later than coincident with the confirm would not compromise the protection of investors. Indeed, unlike far riskier and far more complex securities (e.g., initial public offerings of new companies or interests in structured finance investments), the free-look feature allows variable annuity purchasers at least 10 days to review their investment decision and to change their minds.

Conclusion

AXA Advisors and AXA Distributors fully concur that member firms must maintain effective procedures to assure that recommendations with regard to variable annuities are suitable, that transactions involving variable annuities are appropriately supervised and that variable annuity purchasers are provided with all appropriate disclosures necessary to promote a thorough understanding of the product purchased. While we question whether there truly is a demonstrated showing that the current regulatory requirements are inadequate to provide the NASD with an appropriate basis to proceed against member firms or registered representatives who fall short of these standards, in general we support the provisions of the Proposed Rule to the extent that they simply seek to codify the best practices requirements of NTM 99-35. However, while we appreciate and share the NASD's concern that variable annuity investors receive proper disclosure, for the reasons noted above, we believe that the requirement that member firms separately prepare and deliver a summary risk disclosure document is unnecessary, unduly burdensome, impractical and inefficient, and further would not meaningfully contribute to the protection of investors. In addition, again as noted above, we think that the requirement that principal review and approval occur within one business day of the signing of an application is unduly and unnecessarily short and cannot practically be achieved. Finally, we believe that it is unnecessary and inappropriate to single out variable annuities for disparate and more stringent treatment with regards to replacement comparison and prospectus delivery requirements.

Again, we appreciate the opportunity to offer comments on the Proposed Rule and the consideration that the NASD may give to the views expressed in this letter. If the NASD has any questions or wishes to discuss any of the comments further please contact Windy L. Lawrence at 212-314-2399.

Sincerely,

Robert S. Jones
Chairman of the Board
AXA Advisors LLC

Jerald Hampton
Chief Executive Officer
AXA Distributors LLC