

September 8, 2005

**VIA FEDEX**

Jonathan G. Katz, Secretary  
Securities and Exchange Commission  
100 F Street, NE  
Washington, D.C. 20549-9303

Re: File No. SR-NASD-2004-183  
Deferred Variable Annuity Rule

Dear Mr. Katz:

Please accept the following as the comments of the Public Investors Arbitration Bar Association ("PIABA") to the above-referenced rule filing (the "Proposed Rule").

PIABA strongly supports the NASD proposal for increased regulation of the sale of deferred variable annuities.

As the SEC and NASD have repeatedly recognized, this complex, expensive, insurance-based product is often sold as a tax-deferred vehicle to invest in mutual funds to people who are unable to understand it and for whom it is fundamentally unsuitable. Clients of PIABA members have been victimized repeatedly by sales pitches representing deferred variable annuities to be a common way to invest in mutual funds; comparing deferred variable annuities to CD's; selling tax-deferred variable annuities to accounts that are already tax-deferred; unnecessarily replacing existing deferred variable annuities for elderly clients; and even arranging mortgages for clients without funds to generate money to buy deferred variable annuities. Often clients do not understand annuitization, nor do they understand the death benefit or surrender charge. Sub-accounts are often invested in unsuitable mutual funds.

Because of their incredible profitability to salespersons and firms alike, deferred variable annuity abuses are not just due to individual rogue brokers. The wrongdoing is widespread and has been institutionalized. Brokers are trained to push deferred variable annuities on the general public. Publications by the NASD identifying abuses and recommending "best practices" to the industry have been ignored by many firms. Supervision often is lax to nonexistent. There are simply too many brokerage firms and sales persons who cannot resist the economic opportunity represented by deferred variable annuities.

The deferred variable annuity product itself is problematic in that it is a very complex product which few investors can understand and incorporates negative features including annual expense charges and illiquidity. Indeed, many sales persons as well as supervisory personnel have a flawed understanding of the product. The complexity of the product and its negative features, combined with a high commission structure and resulting sales abuses, strongly justify separate rules regulating sales practices as well as a separate suitability standard.

#### Best Practice Standards Must Be Mandatory

Regulation of deferred variable annuities can no longer be based on NASD "best practice" recommendations or guidelines. Despite regulatory efforts, widespread sales abuses are continuing. The incentive to sell is apparently overwhelming and irresistible. Special mandatory regulation is essential, including strict supervision confirmed in writing.

#### Sub-account Abuses/Reallocation Problems

The problems with deferred variable annuities also extend to the separate accounts. Often the separate accounts themselves are invested in a manner which is unsuitable for the financial needs and investment objectives of investors. Further, registered representatives pay little attention or fail to follow up, often allowing the accounts to flounder in unsuitable investments. PIABA therefore believes that specific attention should be paid to the broker's obligation to oversee and reallocate sub-accounts. We understand the NASD proposal does not

apply to reallocation of sub-accounts. PIABA believes that an investor's risk of loss due to the failure to reallocate sub-accounts is of equal, if not greater, significance than losses which may be generated through initial sub-account investments. Accordingly, PIABA believes that there is no basis for excluding reallocation of sub-accounts from the Proposed Rule.

Proposed Requirements Governing Recommendations,  
Including Suitability Obligation

PIABA supports the specific requirements proposed by the NASD concerning recommendations, as well as the independent suitability obligation tailored to deferred variable annuities.

PIABA recognizes that deferred variable annuities present unique issues concerning suitability which justify an independent suitability obligation designed for the product. The commission structure provides a substantial incentive for registered representatives to aggressively market these products and ignore fundamental responsibilities to customers. An independent suitability obligation is therefore well justified.

Similarly, the separate principal review and approval obligations which require a registered principal review and approval of the transaction prior to transmitting a customer's application for processing are appropriate. Principal review at this stage in the sale process is important because it will give greater assurance that unsuitable transactions are not consummated.

PIABA also supports the obligation on the part of broker-dealers to establish and maintain specific written supervisory procedures which are reasonably designed to achieve compliance with the rule. Under current standards, it is not unusual for broker-dealers to have no written procedures which would address the issues presented through the sale of deferred variable annuities. Because of the uniqueness of the product and, as stated above, its complexity and high commission payout, special procedures for supervision are appropriate.

PIABA further supports the NASD's proposal of an independent training component tailored to the sale of deferred variable annuities.

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In cases observed by PIABA members, it is not uncommon for registered representatives to have an incomplete and mistaken understanding of the deferred variable annuity product. This lack of understanding also has been demonstrated in the registered principals responsible for supervision of the product sales. It is essential that all brokerage personnel who are involved in sale and supervision of these products have a thorough understanding of their material features.

Very truly yours,

Rosemary J. Shockman  
President

RJS:dlr