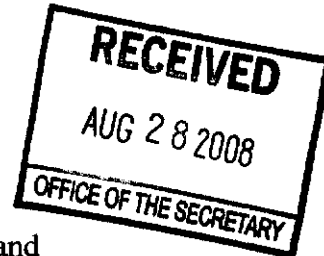
S7-14-08 1233

G. Brooks Euler, CLU, ChFC, CFP
1043 Watauga Court
Thompsons Station, TN 37179

8/22/08

Secretary, Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090
File Number S7-14-08



Dear Secretary, SEC:

I would like to make a comment on your proposed Rules Change regarding 151A and 12h-7 concerning the classification of Indexed Annuities. I support the SEC's proposed changes. Indexed Annuities are really disguised securities and should be classified as securities.

The basic form of an annuity is a single premium annuity. It is an insurance contract where the annuitant pays a premium, for example $100,000, and the insurance company guarantees the annuitant a monthly income for the rest of their life. The monthly payment is based on the annuitant's age and sex. There is no "investment" risk in this type of contract, because the insurance guarantees the monthly payment, backed up by their assets. This type of annuity was exempted from the 1933 Act.

The Equity Indexed Annuity (EIA) or now called Indexed Annuity (IA) is an accumulation vehicle, which allows an "investor" to pay a single premium or a series of premiums, over time, and the annuity assumes that the money will accumulate, at an interest rate, determined by a complicated formula, designed by the insurance company. The Equity Indexed formula has a base measurement of a common equity (securities-linked returns) such as the S&P 500 Index. Many of these products use other security index measurements, also. The use of a security index, like the S&P 500, causes the indexed annuity to be a security.

The sales people who market these Indexed Annuities use a common "sales" pitch of 'how would you like to have your money grow, with the S&P 500 Index, with no risk to your principal'. The first dishonesty problem you will encounter is that the IA excludes the dividends from the S&P 500 Index calculation. The index is composed of real companies, that do pay dividends. Almost all media information, on how the S&P 500 Index is doing, includes dividends. Over a 20 Year period of time, dividends account for about 40% of the Indexes performance. Excluding dividends is grossly misleading. The average investor and unregistered sales person has no way of understanding of how excluding dividends affects the performance of the IA. That dividend exclusion, exposes the IA investor to investment risks.

In addition to removing dividends, each company has a surrender charge, if the investor cashes out early. The surrender charges for Indexed Annuities range from 6% to 18%

over a specified number of years. If the investor, annuitant, surrenders their contract during the surrender period, sometimes from 6 to 16 years, the annuitant could lose some of their premium and any interest earned. Some companies have "vesting" periods. The surrender percentage and length of surrender time create a risk of loss for the investor.

The IA calculation for crediting of earnings (interest crediting) then uses several formulas, designed by each company, to calculate any interest earned/credited, in a given annuity contract's year. In calculating the "interest" credited to the IA, companies use several averaging methods (the net effect of averaging is to reduce the interest earned). In addition, Indexed Annuities use different contract years such as, "point to point", "annual reset", and "high water mark". These create more risk. In addition, the Indexed annuity has limits of how much interest can be "credited" in a given year. They do this by using "interest CAP rates", "participation rates", spreads/margin/asset fees, and other formulas for determining interest rate crediting. This creates more risk for the IA investor. The calculations are complicated and, almost all insurance agents, do not know the formula. If they did, they would not be able to explain it to a customer. Since the value of the purchasers investment depends on the movements of a securities-linked index, they are securities.

These IAs are generally sold by unregistered (not licensed for securities) insurance agents, who have very little knowledge of the securities markets, and they cannot properly explain how the selected index will work within the IA. Since the S&P 500 Securities-Linked Index Annuity refers to a type of security, and is sold using the history of the S&P 500 Index, they are a security, as defined by The Supreme Court in the SEC v. Howey Co. In SEC v. Variable Annuity Life Insurance Co., a variable annuity was found to be a security, by the Supreme Court. There is legal history in classifying an annuity as a security. The IA companies argue that there is no risk to these products. That statement is misleading, since you can lose money in an IA. So, there is risk of loss, if an investor surrenders during the surrender period, and potential loss due to the investor not fully participating in the S&P 500 Index. Purchasers of these annuities assume the investment risk for investments that are more likely than not to fluctuate and move with securities markets. Thus, the value of the purchaser's investment is more likely than not to depend on movements in the underlining securities (S&P500 Index) index and makes the IA a security. If the IA is linked to a securities-linked index, it should be a security and regulated as a security.

Indexed Annuities are very complicated investments and, generally, sold to unsophisticated investors without securities regulation safeguards afforded to purchasers of similar investments. If insurance agents and stock brokers told investors of how the Indexed Annuity shaves the value of the index returns and extraordinary costs, the potential investor would stand a better chance of knowing of what they were buying. There must be full disclosure that the IA, interest return, would more closely resemble a regular fixed annuity or a bank CD. No registered representative, insurance agent, or retail investor, and few financial advisors, could understand the IA complex formulas and hidden costs. There should be a requirement that a comparison be made of an IA investment to a history of what the average bank CD or the average fixed annuity would

have done over the last 10 & 20 years. The purchaser must be told of the surrender charges and their effect on the total value of the IA at the end of each contract year. The IA sales person must disclose the complete interest rate calculation with actual examples of real investments in the index being used (S&P 500), both in up and down markets over 10 and 20 periods of time, with and without dividends. There must be examples of participation rates, cap rates, that go down, over a period of time (10 & 20 years), and what the IA investment would have done in these years. There must be an example of how the averaging of the index returns affect the real rate of returns using real investments like the Vanguard 500 Index Fund or an Indexed linked ETF over 10 & 20 years. The IA company cannot chose the best years that just favor them. There should be a real example (using a S&P 500 mutual fund or ETF) of how the impact of dividends and monthly averaging effect the investment returns over the last 10 & 20 years. These IAs should not be sold to seniors, on a mass marketing basis, lunch or dinner seminars, but only after a legitimate individual fact finding interview. The sales person must make an attempt to find out if the IA investment is suitable for a senior through obtaining all financial information, such as all assets and liabilities.

If your proposal is adopted, the following should be considered to help the investor better understand what they are buying:

+ Limit surrender charges to no greater than 5%
+ Limit surrender periods to no longer than 5 years
+ Guarantee participation rates that will not go down, after the sale
+ Guarantee "Cap" Rates that will not go down, after the sale
+ No premium "bonus" should be allowed, except as an immediate cash payment to customer and not credited to the IA
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