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September 10, 2008

ELECTRONIC SUBMISSION VIA COMMISSION'S SITE

Florence E. Harmon
Acting Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549

Re: **File Number S7-14-08 Indexed Annuities and Certain Other Insurance Contracts Proposed Rule, File No. 33-8933**

Dear Ms. Harmon:

This letter is being submitted on behalf of the US domiciled AEGON companies, which include:

Transamerica Life Insurance Company
Transamerica Occidental Life Insurance Company
Monumental Life Insurance Company
Transamerica Financial Life Insurance Company
Western Reserve Life Assurance Company of Ohio
Merrill Lynch Life Insurance Company
ML Life Insurance Company of New York

The AEGON companies market life insurance, annuities, pensions and supplemental health insurance, as well as reinsurance and mutual funds, and related investment products throughout the U.S. and in certain countries in Europe and Asia. The AEGON companies comprise one of the largest life insurance and pension organizations in the U.S., based on admitted assets, have more than 20 million policy and certificate holders, and distribute their products through approximately 100,000 agents and broker-dealers across the country. For 2007, our US companies' combined annuity considerations totaled over $7.75 billion; this figure includes sales of Indexed Annuities [referred to hereafter as IAs] in the amount of $11 million for the same period.

We support improved disclosure and marketing standards for indexed annuity products and believe that enhancing producer training on indexed annuities would improve customer understanding of these often complex products and reduce instances of inappropriate or unsuitable sales. We have actively worked with the insurance commissioners of the NAIC, including Iowa and other states, to help improve this marketplace.

However, we also believe that Proposed Rule 151A, which requires the registration of all "indexed annuities and certain other insurance contracts" with the SEC, will not achieve these objectives. For these reasons and those discussed below, we must oppose Proposed Rule 151A.

1. <u>Rule Proposal Requires Product Registration But Does Not Offer Options to Improve Consumer Disclosure</u>

The proposed rule suggests that there is a need for improved disclosures and consumer protections in the sale of indexed annuities and that these benefits will be provided by the federal securities laws. We support the goals of improved disclosure and consumer protection; however, we have struggled to understand how the proposed Rule 151A, which appears to be designed to "flip a switch" to simply require the registration of all products offered going forward, will accomplish these goals.

Under the proposed rule, registration would result in the development and delivery of prospectuses to consumers. As the SEC staff is aware, many consumer studies, including those conducted by the American Association of Retired Persons (AARP), have concluded that investors do not read prospectuses. In fact, the Commission has issued several rule proposals in the last several years designed to improve prospectus disclosures of products already subject to SEC regulation and registration. [See Point of Sale Disclosure Requirements and Confirmation Requirements for Transactions in Mutual Funds, College Savings Plans, and Certain Other Securities, and Amendments to the Registration Form for Mutual Funds initially published for comment in January of 2004, re-proposed for comment in the first quarter of 2005. See also, Enhanced Disclosure and New Prospectus Delivery Option for Registered Open-End Management Investment Companies, originally proposed 11/2007, re-proposed 7/31/2008.]

We believe that prospectuses do provide important disclosures to consumers, however, as the SEC staff also has acknowledged, they frequently lose consumers in a quantity of unnecessary disclosures. The annuity disclosure materials developed by the state insurance regulators, and those developed by the industry that are in the testing process, would appear to do a better job of disclosing information relevant to consumers of these products.

The proposed rule would also require insurers to register "indexed and certain other insurance contracts" that fall within the rule on a Form S-1, the catch all registration form for securities for which no other form is authorized or prescribed. The form would require discussion of use of proceeds, information regarding the determination of an offering price and dilution, financial information regarding the insurer's operations and financial condition, among other things. Much of this information would not appear to be useful to a consumer considering an annuity product offering an indexed interest credit.

Specifically, the proposed rule states that requiring registration would improve disclosures re:

costs (such as surrender charges); the method of computing indexed return (e.g. applicable index, method for determining change in index, caps, participation rates, spreads); minimum guarantees, as well as guarantees or lack thereof, with respect to the method for computing indexed return; and benefits (lump sum, as well as annuity and death benefits).

All of the above-listed information is already required to be disclosed in the contracts themselves [delivered to the contract owner] and in state mandated annuity disclosure brochures and state mandated replacement forms, where applicable. Most indexed annuity companies also voluntarily provide point of sale "Statements of Understanding" that are signed by the customer and contain detailed information about the product to be purchased.

There are many other state laws/regulations with disclosure requirements applicable to IA contracts, including:

- Unfair Trade Practices Act (prohibiting the making, publishing, or disseminating to the public in any format, any advertisement, announcement or statement containing any assertion, representation or statement regarding the business of insurance or regarding any insurer in conduct of its insurance business, which is untrue, deceptive or misleading). Has been adopted in some form in almost all states.

- Life Insurance and Annuity Advertising Model Regulation has been adopted in some form in a majority of states and requires:

    - disclosing guaranteed interest rates in the same size text/with equal prominence as non-guaranteed rates,

    - prohibits the use of certain terms associated with investments, such as "investment", "plan", "savings", "deposit", etc.,

    - advertisements for annuities must disclose surrender charges and periods,

    - can not compare annuities to certificates of deposit or make analogies between annuity cash value and savings plans,

    - must include a description of surrender charges, amounts and schedules and this information can't be relegated to footnotes

  The proposed rule then would appear to offer consumers another layer of the same disclosures currently mandated by the states. Respectfully, this would not appear to be improved disclosure, only duplicative disclosure.

2. <u>Scope of Proposed Definition is Too Broad</u>

Covers Other Fixed Annuities and Funding Contracts

The reach of the proposed rule is extremely broad, impacting not only indexed annuities, but other contracts that currently rely on section 3(a)(8). Examples of products affected would appear to include:

- Annuities with market value adjustment features calculated with reference to U.S. Treasury securities, bonds or the insurance company's general account performance.

- Guaranteed investment contracts offering floating interest rate guarantees tied to Treasuries or other government securities, and other stable value products funding 529 plans and retirement plans.

- Depending on how broadly "by reference to the performance of a security" is interpreted, discretionary excess interest contracts that specify in the contract or in marketing materials that the declared rate of interest is calculated by reference to certain general account holdings or other securities.

- Every annuity (and potentially every insurance) contract where interest credited is based "in whole or in part" on a securities index and where it is more likely than not that amounts payable will exceed guaranteed payout amounts.

Even traditional participating policies with dividend formulas which have an investment or inflation adjusted component arguably might be subject to the rule depending upon the formula and the information publicly available about the formula.

If the proposal proceeds, consistent with judicial precedent and prior rule making, the SEC should consider narrowing the focus of its rule to those IAs that do not offer guarantees of principal and accumulated interest. (See discussion below re: investment risk).

Indexed Life Insurance

The proposal also invites comment on whether **<u>indexed life insurance</u>** should be covered by the rule. AEGON would respectfully oppose this expansion of the rule.

Inasmuch as the concerns cited by the staff (e.g. the need to protect older Americans from abusive sales practices and securities fraud, "free lunch" seminars) in connection with the marketing and sale of indexed annuities, don't appear to exist with indexed life insurance, and life insurance products offer other benefits not discussed by or addressed in the staff's rule proposal, the scope of the rule should not be expanded to life insurance products.

3. Proposal Provides No Improved Standards for Marketing Materials

The proposed rule release states that registration would subject issuers and sellers to liability for false and misleading statements under the federal securities laws. State insurance regulators already have this power under the states' laws governing the advertising content and, in many cases, require the filing of advertising materials. States' attorneys general also have authority to bring actions for violation of state unfair trade practice laws. Indeed, the SEC also has the authority and ability to investigate and to take action against issuers of these products that are not entitled to rely upon exemptions under the existing federal securities laws.

To the extent that an issuer offers a product, including an annuity or indexed annuity contract that falls outside of Section 3(a)(8) of the Securities Act or existing Rule 151 or into the definition of a "security", without registering the product, the Securities and Exchange Commission currently also has the authority to bring a civil action enjoining the insurer from issuing the product without registration. The SEC has pursued this remedy in the past See SEC v. VALIC, 359 U.S. 65 (1959), SEC v. United Benefit Life Insurance Company, 387 U.S. 202 (1967). To the extent that the issuer of the unregistered security makes material misrepresentations or omits material information from sales materials, the SEC currently also has the authority to bring an action under Section 17(a) of the Securities Act or Section 10(b) of the Exchange Act.

The proposed Rule 151A does not address or set standards for marketing equity indexed annuities other than to propose that annuities be registered as securities. There currently are FINRA and SEC rules governing variable annuities and mutual funds. There are none for fixed or IAs. The only existing SEC rule regulating the content of advertising materials for the newly registered annuity products, would appear to be the general antifraud provisions promulgated under Section 17(a) of the Securities Act of 1933 and Section 10(b) promulgated under the Securities Exchange Act of 1934. State insurance laws applicable to fixed annuities provide the only product-specific marketing standards that are or will be applicable to these products once the "switch" is flipped requiring registration. Also, there appears to be an underlying assumption that FINRA will have sufficient staff, qualified and trained to assumed responsibility for the review and approve these materials. Issuers who currently file product materials voluntarily with FINRA have experienced a degree of frustration with comments received, demonstrating a lack of understanding of the product features.

In August of 2005, the SEC began an 18 month sweep examination of indexed annuity issuer materials and forms. To date, the staff has made no recommendations regarding needed improvements to product/distributor materials or existing disclosures. The proposed rule recommends no specific disclosures that were missing from the reviewed materials.

If the proposed rule moves forward, we respectfully suggest that a better alternative to address the Commission's concerns re: consumer

understanding/producer marketing of these products would be to provide further interpretive material regarding when the marketing of a fixed annuity crosses the line into emphasizing the investment aspects over the insurance features. For example, the SEC could flag, as inappropriate, material that:

- Describes "market returns or market growth" instead of "interest crediting rates tied to market returns or market growth"
- Implies the customer is investing in stocks, the stock market or a stock market index.
- Fails to disclose the impact of a decline or lack of change in the market indices.
- Fails to disclose the impact to interest crediting rates of sustained declines in market indices.

4. Suitability Requirements Currently Apply to These Products

The proposed rule provides that registration would benefit investors because sellers of IAs would be required to register as broker-dealers and associate with a broker-dealer through a networking arrangement. This structure, it is argued, would impose suitability and supervisory requirements upon the sales of these products. Federal securities laws in place requiring the supervision of securities products have not prevented inappropriate sales of mutual funds, variable annuities, 529 plans or many other products.

Approximately 33 states currently have requirements for suitable recommendations of annuity transactions that apply to producers and issuers of these products, including requirements that insurers supervise the suitability of recommendations to purchase IA products. States are enforcing these newly enacted laws and have demonstrated the willingness and ability to pursue inappropriate sales of fixed annuity products through their state securities regulators, state insurance regulators and state Attorneys General.

5. The Staff's Investment Risk Analysis Is Incomplete

The Commission's rule proposal is premised on the notion that individuals who purchase indexed annuities are exposed to and bear a significant investment risk (i.e. the volatility of the underlying securities index) when the amounts payable by the insurer are "more likely than not to exceed the amounts guaranteed under the contract." The Commission characterizes this risk as "the unknown, unspecified, and fluctuating securities linked portion of the return."

In fact, interest earnings and principal are guaranteed and the major risk component of equity investing, a negative return, is eliminated with the IA. IA contract holders receive a guaranteed interest credit in amounts at least equal

to, often exceeding the minimum nonforfeiture rate set by state insurance laws (in today's interest rate environment, this rate has been set by the states at 1.5%). Unlike variable annuities, IAs do not provide for the pass through of the performance of any of the issuing insurance company's underlying assets, or for that matter, any assets. Contract holders have "no interest in and are not affected by investment gains or investment losses of the insurance company, unless those losses are so great that they threatened the solvency of the insurer." [1] There is a guaranteed floor that ensures contract holders will not lose their principal.

There is also the potential for an additional interest credit, paid out periodically and guaranteed over the life of the contract according to a formula that is locked in prior to the interest crediting period (including any caps on interest paid and any participation rate), and is known in advance by the contract owner. The index value portion of the formula is a snapshot of a market index (exclusive of dividends or capital gains earned on the actual securities comprising the index), at a predetermined point in time (e.g. point to point, an average of values at a specific point each month etc.). The contract value does not rise or fall with periodic market swings during the interest crediting period. Instead, interest is paid at the end of the period upon the value of the contract at the beginning of the interest crediting period in accordance with a contractually guaranteed formula and accumulates throughout the life of the contract, on top of the interest credited under the minimum nonforfeiture, guaranteed rate of interest. [2] The insurer must annually or, in accordance with a schedule outlined in the contract, pay whatever the equity formula dictates which may be unbounded or subject to a cap, which is known to the customer and determined in advance of the interest crediting period.

Insurers issuing IAs bear the risk of guaranteeing contract owner principal and interest earnings. Insurers also bear the risk of disintermediation for equity annuities – the risk from increased contract owner surrenders in a climate of increasing interest rates. As interest rates increase, contract owners have an incentive to surrender their current insurance contracts to purchase new contracts with higher interest rates. Because of the guaranteed values, the risk of liquidating investments at decreased market values is the responsibility of the insurer. Insurers must pay these surrenders by selling their fixed income securities at depressed market value.

The Supreme Court's test to determine whether a contract is an "annuity" within the meaning of Section 3(a)(8) is a facts and circumstances test reviewing the

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1 Olpin v. Ideal National, 419 F.2d 1250 (10th Cir. 1969).

2 Olpin v. Ideal National, 419 F.2d 1250 (10th Cir. 1969) finding that certain endorsements to life insurance policies were not securities despite the fact that the endorsements provided for a payment on death or after a specified period from a "bonus fund." The Tenth Circuit concluded that the endorsements were not securities, because, even though the endorsement did not specify the fixed amount of the benefit that would be paid to the policyholder, the endorsement did provide the factors from which specified amounts were to be derived and paid to the policyholder. Under the policy, the insurer was obligated to pay an amount that could be mathematically calculated regardless of the investment performance of amounts the insurer set aside to fund its obligation.

a) degree of investment risk under the product; and b) the degree of marketing emphasis placed upon investment aspects of the product. The investment risk portion of the test requires an analysis of risk borne by the issuer as well as the investor.

6. **Impact of Proposal Upon Issuers and Distributors is Grossly Understated**

Insurance Companies

Under the proposed Rule 151A, many products currently available to consumers and approved by the states and sold for years can no longer be sold. Issuers will have to revise current contracts and re-file them with all fifty-one jurisdictions' insurance commissioners, as well as with the SEC. This requires the commitment of substantial resources, both financial and time, which costs appear vastly underestimated by the drafters of the proposed rule.

The rule proposal would subject insurers not currently subject to SEC regulation to prospectus and registration statement development, filing and distribution. This would require companies to either hire or contract with outside counsel for the expertise to prepare and file these materials at a cost of tens of thousands of dollars per contract. The rule proposal estimates it will take 60,000 hours of in-house company personnel time at a cost of $10mm internally and $72mm in outside law firm expenses (at a cost of $400/hour) to file the required S-1 to register the product to file the 400 or so existing indexed products. The per-hour estimate does not reflect market rates for SEC counsel, the estimates of time involved are low for people unfamiliar with the SEC registration process, and the interaction that will be required with the staff on these newly created securities products.

Form S-1 upon which insurers would be required to register IAs requires registrants to present the selected financial data on the basis of the accounting principles used in its primary financial statements but in such case must present this data also on the basis of any reconciliations of such data to United States generally accepted accounting principles and Regulation S-X made pursuant to Rule 4-01 of Regulation S-X. Insurance companies who are US subsidiaries of a larger, publicly traded company may not issue/maintain GAAP financial statements, and thus will incur either the cost of preparing and maintaining parallel statements or request No Action relief.

Agents/Agencies

The proposal provides no estimates on how much it would cost or how long it would take insurance agents or agencies to register with FinCEN to continue to sell these products. The SEC/FINRA registration process for agents takes between 90 and 120 days at best. The process can take from six months to a year, if certain letters are misfiled or the filing is in a busy district like New York, or the applicant is inexperienced. There is a $250 filing fee per state (per rep); a $3,000 NASD membership fee; a fidelity bond (beginning at $500); the

cost of a mandated annual audit, which could range from $2,500 to $10,000 or more; as well as the cost of mandated continuing education, which averages $50 to $60 per representative.

The proposed rule assumes that many agencies will enter into networking arrangements but does not acknowledge that in 2006, the SEC's Division of Market Regulation revoked a No Action letter issued to M. Financial in connection with its networking arrangement with an unaffiliated broker-dealer and, in the process, advised the industry that only those arrangements established in a manner similar to the First of America No Action Letter (involving agency networking arrangement with an affiliate broker-dealer) would be permitted going forward. Insurance agencies without an affiliate broker-dealer would not appear to be able to take advantage of the networking arrangement.

7. **Proposal Creates Unacceptable Litigation Risks**:

The SEC's position that all contracts offered for sale as of the effective date of the rule proposal must be registered as securities, including contracts currently offered/sold in reliance upon existing exemptions will subject insurers to significant civil litigation risk. Insurers will be exposed to class action lawsuits alleging securities fraud and other theories of liability, by contract owners emboldened by the staff's position that all such contracts should have been registered as securities.

Additionally, an insurance company that registers a product, but whose product fails to return a greater than minimum interest rate, faces exposure for having made material misrepresentations to every contract owner that purchased the product.

8. Extension of Comment Period is Necessary:

The SEC staff last solicited comments on the status of equity indexed products under the federal securities laws in 1997. An 88 day comment period is not enough time to provide thoughtful comments and suggestions on the more than forty (40) requests for comment in the 96 page release. Many of the issuers and distributors of these products are not currently subject to state or federal securities regulation, as such, the rule proposal has far reaching implications for insurance regulators, companies, producers and consumers. We respectfully request that the staff extend the comment period an additional 180 days to permit state regulators, insurers, producers and consumers to evaluate the implications of registration and to explore alternative solutions to the issues that the staff believes necessitate an immediate and sweeping response.

Thank you for the ability to comment on this proposed Rule.

Very truly yours,

Diana Marchesi
Director of State Government Relations
Transamerica Life Insurance Company

cc: The Honorable Luis A. Aguilar
The Honorable Kathleen L. Casey
The Honorable Christopher Cox
The Honorable Troy A. Paredes
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