EVERSHEDS SUTHERLAND

THE Committee OF Annuity Insurers
www.annuity-insurers.org

Eversheds Sutherland (US) LLP
1114 Avenue of the Americas, 40th Floor
New York, NY 10036-7703

D: +1 212.389.5000
F: +1 212.389.5099

April 15, 2020

Via E-Mail
rule-comments@sec.gov

Vanessa A. Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File No. SR-FINRA-2020-007;
Proposed Rule Change to FINRA's Suitability, Non-Cash Compensation and Capital Acquisition Broker (CAB) Rules in Response to Regulation Best Interest
Release No. 34-88422

Dear Ms. Countryman:

We are submitting this letter on behalf of our client, the Committee of Annuity Insurers (the "Committee"),[1] in response to the U.S. Securities and Exchange Commission's ("SEC") notice: *Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of a Proposed Rule Change to FINRA's Suitability, Non-Cash Compensation and Capital Acquisition Broker (CAB) Rules in Response to Regulation Best Interest*.[2] The Proposing Release solicits comments on proposed changes to FINRA Rules 2111 (Suitability), 2310 (Direct Participation Programs), 2320 (Variable Contracts of an Insurance Company), 2341 (Investment Company Securities), and 5110 (Corporate Financing Rule—Underwriting Terms and Arrangements), and Capital Acquisition Broker (CAB) Rule 211 (Suitability) (collectively, the "Proposed Rule Change") to align with the requirements of Regulation Best Interest ("Reg BI").[3]

BACKGROUND

On June 5, 2019, the SEC adopted Reg BI to establish a standard of conduct for broker-dealers and natural persons who are associated persons of a broker-dealer (together referred to as "broker-dealer") when they make a recommendation to a retail customer of any securities transaction or investment strategy involving securities.[4] The SEC stated that Reg BI will improve investor protection by enhancing the obligations that apply when a broker-dealer makes a recommendation to a retail customer, and reducing the potential harm to retail customers from

[1] The Committee is a coalition of many of the largest and most prominent issuers of annuity contracts. The Committee's 32 member companies represent more than 80% of the annuity business in the United States. The Committee was formed in 1981 to address legislative and regulatory issues relevant to the annuity industry and to participate in the development of insurance, securities, banking, and tax policies regarding annuities. For over three decades, the Committee has played a prominent role in shaping government and regulatory policies with respect to annuities at both the federal and state levels, working with and advocating before the SEC, CFTC, FINRA, IRS, Treasury Department, and Department of Labor, as well as the NAIC and relevant Congressional committees. A list of the Committee's member companies is attached as Appendix A.

[2] 85 Fed. Reg. 16974 (Mar. 25, 2020) (the "Proposing Release").

[3] *Id.*

[4] Final Rule; Regulation Best Interest: The Broker-Dealer Standard of Conduct (June 5, 2019), 84 FR 33318 (July 12, 2019) ("Reg BI Adopting Release").

Eversheds Sutherland (US) LLP is part of a global legal practice, operating through various separate and distinct legal entities, under Eversheds Sutherland. For a full description of the structure and a list of offices, please visit www.eversheds-sutherland.com.

conflicts of interest that may affect the recommendation.[5] In light of Reg BI, which is scheduled to take effect on June 30, 2020, FINRA proposes to amend its suitability and non-cash compensation rules to provide clarity on the standard that applies when a broker-dealer makes recommendations and to address perceived inconsistencies with Reg BI.

The Committee is providing comments only on FINRA's stated basis for revising the non-cash compensation provisions applicable to Variable Contracts (FINRA Rule 2320) of the Proposed Rule Change. FINRA's current non-cash compensation rules permit non-cash compensation arrangements, such as sales contests, to be based on the sales of certain defined products like Direct Participation Programs (FINRA Rule 2310), Variable Contracts (FINRA Rule 2320), and Investment Company Securities (FINRA Rule 2341), subject to certain conditions. FINRA proposes to modify its rules governing non-cash compensation arrangements to specify that any non-cash compensation arrangement permitted by those rules must be consistent with the requirements of Reg BI.

Further, FINRA also proposes to eliminate provisions in FINRA Rule 2320 that require internal incentive non-cash compensation arrangements for variable contracts to be based on total production and equal weighting of securities sales. (Similar requirements apply to internal incentive non-cash compensation arrangements for investment company securities.) According to FINRA, "firms generally would no longer be permitted to sponsor or maintain internal sales contests based on sales of securities within a product category within a limited time, even if they are based on total production and equal weighting."[6] This requirement also would apply to the non-cash compensation provisions governing gifts, business entertainment and training or education meetings.

The Proposing Release and Proposed Rule Change suggests that FINRA views its current rules for these products, including rules limiting incentive programs based on total production/equal weighting, as not meeting Reg BI's Conflict of Interest Obligation, which requires broker-dealers to establish, maintain, and enforce written policies and procedures reasonably designed to identify and eliminate any sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sales of specific securities or *specific types of securities within a limited time period*.

COMMITTEE COMMENTS

The Committee appreciates the opportunity to submit comment in response to the Proposed Rule Change. The Committee also supports FINRA's efforts to align its rules with the requirements of Reg BI. The Committee offers the following comment in response to the Proposed Rule Change as it applies to FINRA Rule 2320 related to non-cash compensation arrangements for variable contracts.

Proposed Amendments to Non-cash Compensation Rules. The Committee believes that FINRA should clarify its stated basis in the Proposing Release for the proposed amendments to the non-cash compensation rules in light of a conflict between the SEC's guidance in the Reg BI Adopting Release related to the phrase "specific types of securities" as used in the context of Reg BI's Conflict of Interest Obligation, and FINRA's apparent view of that phrase and its impact on its current non-cash compensation rules. As stated above, Reg BI's Conflict of Interest Obligation requires broker-dealers to establish, maintain, and enforce written policies and procedures reasonably designed to:

> Identify and eliminate any sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sales of specific securities or *specific types of securities* within a limited time period.[7]

[5] Reg BI Adopting Release at 33318-19.
[6] Proposing Release at 16976.
[7] Reg BI at § 15l-1(a)(2)(iii) (emphasis added).

In the Reg BI Adopting Release, the SEC refers to mutual funds and variable annuities as "general categories of securities," and, in contrast, refers to "stocks of a particular sector or bonds with a specific credit rating" as examples of "specifically identified types of securities."[8] Since the text of Reg BI prohibits limited period sales contests if they involve "specific types of securities," it seems difficult to comprehend that variable annuities, in the SEC's view, are both "general categories of securities," but also "specific types of securities" that are subject to the limited period sales contest prohibitions under the Conflict of Interest Obligations of Reg BI. What seems more consistent with what the SEC had in mind with respect to variable contracts and mutual funds would be to apply the limited period sales contest prohibition to specific types of variable annuities or funds within those general product categories (e.g., large cap equity mutual funds).

As mentioned above, in the Proposing Release, FINRA states that under its *current* non-cash compensation rules, firms may conduct sales contests based on sales of "specific types of securities," which may not meet the Conflict of Interest Obligation under Reg BI. Notably, in the Proposing Release, FINRA concludes that product categories such as those covered under FINRA Rule 2320, variable contacts, would be viewed under Reg BI's prohibition on sales contests as a "specific type of security" that is not permitted to be the subject of a limited period sales contest. The Proposing Release states:

> FINRA's current non-cash compensation rules permit internal firm sales contests that may not meet this standard, since they permit contests based on *sales of specific types of securities (such as mutual funds or variable annuities)*.[9]

In making that statement, FINRA has effectively converted the language restricting limited period sales contest for "specific types of securities" under Reg BI to a restriction on limited period sales contests that are for a "product category." In fact, when the language is examined side-by-side, there is a direct conflict between the language that the Reg BI Adopting Release uses to describe mutual funds and variable annuities ("general categories of securities") and FINRA's description of mutual funds and variable annuities in the Proposing Release ("specific types of securities") The Committee believes that FINRA's conclusion that variable contracts should be viewed as constituting a "specific type of security" under Reg BI is fundamentally inconsistent with how the SEC describes and interprets that phrase under the Reg BI Adopting Release.

CONCLUSION

In short, FINRA's statements in the Proposing Release have effectively expanded the prohibition on limited period sales contests beyond that imposed under Reg BI. In light of the SEC's guidance that appears in the Reg BI Adopting Release, the Committee recommends that the adopting release or any regulatory notice issued related to the Proposed Rule Change indicate that the rules governing non-cash compensation are intended to align in all respects with the intent of Reg BI with respect to what constitutes a "specific type" of security.

The Committee appreciates the opportunity to provide these comments on the Proposed Rule Change. Please do not hesitate to contact Clifford Kirsch (212.389.5052 or

---

[8] Reg BI Adopting Release at 333936 (emphasis added) ("[w]e recognize that some associated persons may focus their business on certain *general categories of securities* (e.g., mutual funds, variable annuities, bonds, or equities) and that broker-dealers may provide compensation or other incentives related to such sales…. [T]his requirement is not designed to prohibit broker-dealers from providing such incentives, provided that they do not create high-pressure situations to sell a *specifically identified type of security* (e.g., stocks of a particular sector or bonds with a specific credit rating) within a limited period of time, such that the associated person cannot make a recommendation in the retail customer's best interest.")

[9] Proposing Release at 16976.

CliffordKirsch@eversheds-sutherland.com) or Eric Arnold (202.383.0741 or EricArnold@eversheds-sutherland.com) with any questions or to discuss this comment letter.

Respectfully submitted,

EVERSHEDS SUTHERLAND (US) LLP

BY: /s/ Clifford Kirsch

Clifford Kirsch

BY: /s/ Eric Arnold

Eric Arnold

FOR THE COMMITTEE OF ANNUITY INSURERS

Appendix A

THE COMMITTEE OF ANNUITY INSURERS

AIG
Allianz Life
Allstate Financial
Ameriprise Financial
Athene USA
AXA Equitable Life Insurance Company
Brighthouse Financial, Inc.
Fidelity Investments Life Insurance Company
Genworth Financial
Global Atlantic Financial Group
Great American Life Insurance Co.
Guardian Insurance & Annuity Co., Inc.
Jackson National Life Insurance Company
John Hancock Life Insurance Company
Lincoln Financial Group
Massachusetts Mutual Life Insurance Company
Metropolitan Life Insurance Company
National Life Group
Nationwide Life Insurance Companies
New York Life Insurance Company
Northwestern Mutual Life Insurance Company
Ohio National Financial Services
Pacific Life Insurance Company
Protective Life Insurance Company
Prudential Insurance Company of America
Sammons Financial Group
Security Benefit Life Insurance Company
Symetra Financial Corporation
Talcott Life Insurance Company
The Transamerica companies
TIAA
USAA Life Insurance Company