Brokerage Unlimited, Inc.
Special Bulletin

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U.S. Court of Appeals Vacates SEC Rule 151A

SEC's judgment on Fixed Indexed Annuities "arbitrary and capricious".

On July 12, 2010, the United States Court of Appeals for the District of Columbia vacated SEC Rule 151A. The rule, which was scheduled to take effect on January 12, 2011, would have treated fixed indexed annuities as securities for federal regulatory purposes. In other words, these products would have been treated as securities, and sellers of these products would have been required to hold federal securities licenses.

Background:

The Securities Act of 1933 (Act) governs the offer or sale of any security through interstate commerce. However, the Act exempts any annuity contract that is subject to state insurance laws. In January 2009, the SEC adopted **Rule 151A**, which was intended to treat fixed indexed annuities as securities on a prospective basis for contracts issued on or after January 12, 2011.

Rule 151A would have made fixed indexed annuities subject to all of the requirements of the Act. One of those requirements would have been that any person soliciting the sale of a fixed indexed annuity contract would be required to hold a valid federal securities license.

One issuer of fixed indexed annuities petitioned the Court to review **Rule 151A**, arguing the SEC failed to consider the effect of the rule upon efficiency, competition and capital formation, as required by Section 2(b) of the Act. The Court agreed that under Section 2(b) of the Act, the SEC *"is required to consider and determine whether an action is necessary or appropriate in the public interest, and the SEC shall also consider, in addition to the protection of investors, whether the action will promote efficiency, competition and capital formation."*

The Court concluded the SEC's analysis in this regard was incomplete and failed to *"determine whether, under the existing regime, sufficient protections existed to enable investors to make informed investment decisions and sellers to make suitable recommendations to investors."*

The Court further ruled, *"The SEC's failure to analyze the efficiency of the existing state law regime renders arbitrary and capricious the SEC's judgment that applying federal securities law would increase efficiency. The SEC's flawed* *efficiency analysis also renders its capital formation analysis as arbitrary and capricious. The SEC's conclusion that Rule 151A would promote capital formation was based significantly on the flawed presumption that the enhanced investor protections under Rule 151A would increase market efficiency. This analysis fails with the failure of its underlying premise."*

While the Court's ruling will prevent **Rule 151A** from taking effect as scheduled, the SEC may adopt a similar rule again in the future provided the SEC conducts the analysis required by Section 2(b) of the Act.

For more information, please contact your Broker-Dealer firm or Izzy Myers, CLU, ChFC, AEP at imyers@brokerageunlimited.com.
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