Fixed Annuity Trends: Distribution Matters

By DANNY FISHER

WHEN LOOKING AT FIXED annuity trends, it's important to first acknowledge the differences in the 4 primary distribution channels. They are summarized in the accompanying list (see box). We'll review them here and then see where the headwinds in this market are blowing.

As new products are developed, trends in each group follow the same path: Annuities sold by professional agents and wire houses tend to improve yields and options to policy owners when compared to annuities sold in other channels.

The bank group tends to copycat more. If company A offers a particular type of annuity and company B doesn't, then company B will copy the product from company A and try to increase their market share. There seems to be very little creativity in this group.

The companies who develop annuities for the commission hounds tend to think more is better. Their attitudes seem to be, "If the commission is already extremely high, then let's increase the commission to an absurdly high level and get more agents to sell our products. We can pay higher commissions by extending the surrender penalty period and pay lower yields to the policy owner."

Now for the trends. Consumers desire (and are more likely to purchase) the Multi-Year Guarantee (MYG) annuities. In these products, the length of the rate guarantee period matches the length of the surrender penalty period. These annuities are also known as CD-types annuities.

MYG contracts may come with or without a first year rate bonus, market value adjustment, and a "Renew, Remove or Rollover" (RRR) clause. An RRR clause simply means at the end of the rate period, clients are forced to Renew for another period, Remove the money from the annuity, or Rollover to a new annuity.

Rather than having an RRR clause, some MYG annuities convert to a portfolio-type annuity, where the rate is free to float up or down and the funds are 100% liquid for as long as the policyowner owns the contract.

The trend in MYG contracts is to do away with the first year bonus. For example, 4.20% guaranteed for 5 years is much easier to explain than 5% for 1 year and 4% guaranteed in years 2 through 5. Although the 5-year average yield is still 4.20%, clients tend to forget they knew the rate was going to drop in year 2–and they get mad when it changes.

OPINION

> **ANNUITY DISTRIBUTION**
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> **THE KEY CHANNELS**
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> ■ **Professional agents:** They prefer to sell high quality, consumer oriented annuities with a lower commission schedule, resulting in higher average yields to policy owners.
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> ■ **Wire houses:** They offer annuities that are similar to the annuities offered by professional agents, but their policies are normally proprietary products available only from their firm.
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> ■ **Banks and savings & loans:** This group normally sells higher commission annuities with higher rated companies, creating a type of market chasm between themselves and the first 2 groups. The annuities sold in the bank/ S&L tend to have slightly lower average yields to policy owners.
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> ■ **Agents who sell based on the highest commissions:** This group tends to represent the "bottom feeders", so to speak. They offer annuities that have surrender penalties of 10 years or longer and that tend pay very low average yields to the policy owners.
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> *Source: Danny Fisher, Fisher Annuity Index, Dallas*

As for new annuity design, 2 trends are prevailing today, as follows:

- More annuities are being developed with a Market Value Adjustment (MVA). In today's economic environment, an MVA clause is almost mandatory to protect the insurer from rising rates.
- New contracts are more likely to be owner-driven as opposed to annuitant-driven. (The owner-driven annuities trigger death proceeds at the death of the owner, not the annuitant. If owner and annuitant are different and the annuitant dies first, the owner names a new annuitant. Annuitant-driven annuities trigger death proceeds at the death of the annuitant.) In my view, no company should design a new annuity that isn't owner-driven, as these contracts are easier to understand, provide more flexibility to the policyowner, solve lots of commission problems, and most importantly, conform more easily to the tax code.

Another important trend to watch in the future is for contractual minimum guaranteed rates to increase as rates rise. Due to the extremely low current rate environment, many companies have lowered the minimum rates, but as rates rise, the higher minimum rate contracts will be reintroduced to the market. Not because insurers want to do so, but competition will demand it.

Due to the low rate environment, most of the shorter-term MYG annuities, with guarantees running 3 years and less, were removed from the market, but will reappear as rates rise.

Still another trend: Annuity applications are becoming much longer and more complicated with more insurers requiring signatures on disclosure statements.

As an agent, I believe disclosure statements are good. I want the client to sign a statement that he/she understands the key features of the contract, which helps to protect the insurer and me from groundless lawsuits. On the other hand, there is such a thing as overkill. I've seen disclosure statements that require the policyowner to sign 2 or 3 times, plus initial up to 15 different times. That is totally unnecessary.

One of the most difficult ideas I've tried to convey to insurers is: The easier an annuity is to explain, the easier it is to sell. The easier it is to sell, the more is sold. The more sold, the higher the profits.

It's refreshing when a company asks for ideas from their clients and agents on how to make products and forms better and easier to understand. Unfortunately, that doesn't happen very often and that's a trend that needs to change. NU

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