A Conversation with Jackson National's CEO

By Kerry Pechter *Thu, Apr 7, 2016*

'If a guy is getting ready to lose his house, and the VA account is the only liquidity he's got, he's not going say, 'But our guarantee is in the money so we won't touch it,' said Jackson National chief Barry Stowe about his firm's record 2015 VA sales--and the risks that success could bring.

In 2015, when the variable annuity industry shrank overall, Lansing, Michigan-based Jackson National Life sold $23.11 worth of its Perspective II and Elite Access variable annuity contracts, according to the LIMRA Secure Retirement Institute.

That didn't break MetLife's all-time record of $28.44 billion set in 2011, when $159.3 billion in VAs were sold. But it was a new record for Jackson National, beating its 2014 record of $23.08. It was more than double the $11.51 billion in individual VAs that runner-up Lincoln Financial Group sold in 2015, representing a 17.4% share of the $133 billion in VAs sold last year.

To hear Jackson National's thoughts on its record year, especially in the context of the DOL fiduciary rule, RIJ spoke with Barry Stowe (right), chairman and CEO of Prudential plc's North American Business Unit, which includes Jackson National Life, National Planning Holdings and PPM America. Here's a record of our conversation, which took place before the issuance of the final DOL fiduciary rule:

RIJ: Although overall VA sales have been dropping in the last few years, Jackson National keeps selling more, with over $66 billion in 2013 through 2015. And even though investment-only VAs are the latest trend, you still sold about $13 billion worth of your income-rider VA in the first nine months of 2015, compared with about $3.5 billion of the investment-only Elite Access product.

Stowe: This is the best year we’ve had. Our variable annuities sales are still largely Perspective II. The investment-only VAs have been an interesting story, but it’s Perspective II, with its minimum withdrawal guarantee and death benefit, that make the variable annuity an important product with real social value.

RIJ: Do you think advisors were trying to buy in ahead of the DOL fiduciary rule in 2015?

Stowe: We think the rule actually slowed down sales. The lack of clarity around what the rule change will mean has spooked some advisors. In particular, there’s been a lack of clarity on the issue of grandfathering. Everyone is assuming that the DOL wouldn’t go so far as not to grandfather-in prior sales of variable annuities. [Without grandfathering], advisors with contracts in place would have to go in and re-paper those sales. We don’t think DOL would do that. We’ve gotten feedback that some advisors, but not a huge number, say they won’t sell any variable annuities until they have more certainty. They don’t want to be in the position of selling 30 more VA contracts and then have to re-sell them. Once we get clarity, and if past sales are grandfathered, then we might see people coming back and saying, ‘Let’s do it.’ [**Editor’s note:** It appears that past sales are “grandfathered” under the final rule.]

RIJ: How do you think the Best Interest Contract requirement will affect VA sales?

Stowe: Some of our competitors have said that the BIC will cut their sales by 40% or 50%. My sense is that we won’t see an impact of that magnitude. Jackson has a track record of being nimble and adaptable. We have an attitude that we can turn this to our commercial advantage. We can help advisors figure out the best way to handle the BIC. But without having seen a [final version of the] rule, it’s impossible to say.

RIJ: Any thoughts on why the DOL decided to put variable annuities ‘under the BIC,’ and not fixed annuities—especially when VA sales are so much higher?

Stowe: It’s a mystery why they would single out this product. The VA is the product most suited to address the needs of the enormous population of boomers who have under-saved and aren’t prepared for a retirement that could last for 20 or 30 years. These consumers need certainty around income for life, and the VA is the only product that allows policyholders to get upside but also guarantees a floor. If the product gives them half-again what they’re getting from Social Security, for instance, that’s enormously valuable.

RIJ: The DOL seems to view the VA as complex and expensive.

Stowe: I think there's a lack of understanding of the product. There's a view that it's a mutual fund portfolio that costs 300 bps a year, in an insurance wrapper. And [since you can get mutual funds for a lot less], that seems like a rip off—especially if the only advantage is a tax advantage. Clearly there are people who don't know that the cost is for the guarantee for the income. We've worked hard to explain the product. When you look across Congress, it's been the Democrats who have educated themselves on this. The Democrats, including some that are in high-retiree districts, are pushing back harder than the Republicans. The UK went down a similar path with their RDR [Retail Distribution Review] changes. They admit that it created an advice gap and now they're trying to figure out how to undo the damage. The DOL seems to be going down same wrong path despite the evidence of unintended consequences.

RIJ: How exactly does Jackson National plan to respond to the final rule?

Stowe: We do more nonqualified business than qualified business. We can't comment on new products, but we are building a product that works under what we think the new rule will look like. We'll be able to take qualified money in a fair and compliant way, but it will just be more difficult to do so. The DOL rule doesn't really target insurers; it targets advisors. We're a big company, and we can figure out how to adapt, and so can our competitors. The problem is that middle class Americans are going to have a hard time getting advisors to talk to them. The layers of rules will be so onerous that the sale of the annuity won't be worth the risk that the advisor is potentially taking on. As important as these products are, the fact that is that the most important ingredient is the advice that the client gets on the front end. Advice is critical. Most people need help understanding these products.

RIJ: What lessons do you think the VA industry should take from the DOL's action?

Stowe: The industry has to make the products easier for people to understand. The mechanics of the product aren't complicated. But why do we call it a GMWB? How are people supposed to understand what a VA-with-a-GMWB-and-a-DB is? One of the most consumer-centric things we could do would be to make the product simpler to understand. It would help if we engaged regulators on how to improve financial literacy. You don't wait until somebody is 58 years old to introduce retirement concepts. You have to start telling them what they need to do when they're 30.

RIJ: Do you expect to see lower commissions in response to the rule? And, if VA commissions are lower, will intermediaries be as inclined to sell the product?

Stowe: Sales people are sales people. I would defend commissions to the death. In the long run, the commissions on a variable annuity are significantly less than fee-based compensation. It's less than half the cost over the life of the contract. All we are doing is financing the upfront provision of advice for middle-class Americans. The commissions are absolutely justified. What's tough to defend are the other kinds of sales incentives, like trips to Vegas for producers. We don't do that.

RIJ: As of the end of the third quarter of 2015, the market value of Jackson National's book of VA business was almost $135.4 billion, down from $142 billion at mid-year. How are you making sure that you don't take on too much risk?

Stowe: We think we have our pricing right. The academics are saying, oh-my-god, if you guarantee x and lots of your contracts have in-the-money guarantees, then no one will cancel and you'll have a big problem. That's possible, but only if assume that contract owners will behave rationally. In fact, there's never been a time when retail investors have acted rationally. If you do a quantitative study of investor behavior, you see that they buy high and sell low. And if you imagine an environment where [an issuer] would be in trouble—negative rates of return, an equity shock with no chance of recovery—I admit that it looks complicated on paper. But the same environment that would put pressure on us would put pressure on annuitants to get access to their money. If a guy is getting ready to lose his house, and the VA account is the only liquidity he's got, he's not going say, 'But our guarantee is in the money, so we won't touch it.' Sure, you can make a theoretical model that blows up the industry. You could also create a model where Lansing, Michigan, gets destroyed by a meteor. But it's never happened.

© 2016 RIJ Publishing LLC. All rights reserved.