A Sense that the Worst Is Over

By Kerry Pechter *Thu, Oct 2, 2014*

At the IRI annual conference in this quaint colonial village, the annuity industry shared a sense that, after several hellish years, the worst may be over.

Back in 2008, before the Crisis broke, the National Association of Variable Annuities realized it had to represent the interests of distributors as well as manufacturers—i.e., broker-dealers and advisors as well as life insurers–in order to reach its goals.

Those goals were political as well as commercial. The trade group wanted to become an advocacy—lobbying—group for the retirement industry. And to wield influence in Washington, it needed to grow in size and breadth, like a boxer eager to fight in a higher weight class.

And that is what has happened in the six years since NAVA changed its name to the Insured Retirement Institute. Under the leadership of former Kansas insurance regulator Cathy Weatherford, her staff says, IRI's biggest accomplishment has been to bring more advisors and distributors into the fold.

At the IRI's well-attended and relaxed annual conference in quaint and relatively deserted colonial Williamsburg, Va., earlier this week, evidence of the organization's ongoing makeover was subtle, with only a few obvious changes to distinguish it from NAVA meetings.

NAVA meetings typically featured carnival-like exhibit halls; partly for lack of space, IRI had no booths at all this year. NAVA had lots of lively internal bickering; IRI presents a unified front. IRI has a political action committee and 11 standing committees; NAVA had no PAC and two committees. But many of the same companies are still in attendance, and even some of the same faces.

Eight years ago, NAVA listed 85 distributor members, or 17% of the total. Of the nearly 1,000 members currently listed on IRI's website, some 700 are listed as "distributors and bankers." (According to IRI, the membership includes only 48 "parent" broker-dealers, distributors and banks; the rest are affiliates.) Many of those appear to be small wealth management firms. Through all of its distributor members, IRI boasts that it now reaches some 150,000 advisors.

Glass three-quarters full

A mild vibe went through this meeting that, after several years of hell, the worst may be over for the annuity industry. Dennis Glass, CEO of Lincoln Financial Group, started off the conference with a sort of rambling no-prompter keynote address about the economy and his company. As someone in his position should be, he was circumspect but confident about the immediate future.

"A recent article by Goldman Sachs said the 10-year Treasury rate will go to 4% in the near future. But with the German government note paying only one percent, and with the free flow of capital around the world, it's hard to imagine the U.S. being much different from that. [Lincoln] is planning for an increase in the 10-year rate of 25 basis points a year going forward, and rising equities markets—though not as big a rise as in 2013. I don't buy into the idea, 'This is the longest bull market in history so the market can't keep going up.' Stocks are tethered to profits and economic growth, and the economics are positive."

The annuities industry had a lot of bad news for consumers after the financial crisis, with discontinued products, higher costs, weaker benefits and so forth, Glass suggested, but the situation has bottomed out and there's nowhere to go but up.

"We re-priced our products when rates were at their lowest, so the major shift toward sharing of risk with the consumer is now behind us," he said. "There are no more significant price increases on the horizon. As rates rise, the next move will be to reduce prices so more people can take advantage of our products. But if we're not careful about our next steps, we'll lose market share to disruptive companies. The life industry has been terrible at demonstrating value to consumers. Five years ago, nobody was asking consumers what they wanted. Actuaries were developing products they thought the consumers would be interested in. As we move forward, pure research and conversations with consumers will be hugely important."

Glass mentioned several ongoing irritants for life insurers: the government's failure to recognize fundamental differences between banks and insurance companies in their push to classify MetLife and Prudential as systemically important financial institutions (SIFIs). He railed against details of Congressman David Camp's early-2014 tax reform proposal that would reduce life insurer profits. On the other hand, he welcomed the arrival of new capital in the U.S. life insurance business from Japan and from private equity companies. He also celebrated his own company's reinsurance deal last fall, in which Union Hamilton Re agreed to provide 50% coinsurance on up to $8 billion of new living benefit guarantee sales on

Lincoln variable annuities.

Traction on the Hill

As a lobbying force, the IRI has been a source of information and donations for key legislators, a partner with other groups on protecting existing benefits for retirement products (like tax deferral) and creating new ones (like the Qualified Longevity Annuity Contract, or QLACs), and an overall cheerleader (leading the National Retirement Planning Coalition, which created National Retirement Planning Week). It has also worked on issues like NARAB II, which involves simplification of agent licensing in the balkanized regulation of insurance product sales and sellers at the state level.

It’s hard to tell exactly how big a difference IRI has made in Washington over the past six years. The wheels of government turn slowly, especially today. The fact that the IRI, an inherently conservative group, has been fated to deal with the liberal Obama administration since its inception, has not been helpful. But that’s probably less a factor than the overall red/blue gridlock that has frozen Washington—a gridlock that history may show to be a symptom of the conflicts baked into our Constitution.

Regarding the regulatory change that enabled above-mentioned QLACs, it is not easy to tell how much influence the IRI had in bringing it about. An IRI lobbyist this week seemed to downplay the IRI’s role in the change, which allows Americans to delay required minimum distributions on up to $125,000 (or 25%, if less) of their pre-tax savings until as late as age 85 by buying a deferred income annuity. But Mark Iwry, the deputy assistant Treasury secretary who steered the new regulation to reality, honored the IRI by announcing the accomplishment at IRI’s regulatory conference in July.

As for protecting the favorable tax treatment of retirement products, the threat has probably been that great. Although President Obama himself had proposed capping the benefits of tax deferral for higher-income taxpayers, and capping the size of rollover IRAs, the administration never showed much appetite for shrinking the $110 billion-a-year annual retirement savings tax expenditure. There was talk, but little or no chance that it would happen.

Political contributions

Unlike NAVA, IRI has a PAC, which has been funded by individual contributions from senior executives of member companies and the PACs of member companies. Between January 1, 2013 and August 31, 2014, the IRI PAC took in $59,200 in individual contributions and

$66,750 from PACs of life insurance companies, according to the Federal Election Commission. The IRI PAC disbursed $109,800 to the campaign committees of candidates, donating about $60,000 to Republican and $40,000 to Democratic candidates.

In this election cycle, IRI has donated $7,500 to the U.S. Senate campaign of Shelley Moore Capito, Republican congresswoman of West Virginia and chair of the House Financial Services Subcommittee on Financial Institutions and Consumer Credit, according www.fec.gov. The daughter of former West Virginia governor Arch Moore, she's running for the seat vacated by Democrat Jay Rockefeller, who is retiring. The Federal Election Commission lists 68 other recipients of IRI PAC donations in 2013-2014.

Even though IRI describes the assembly of manufacturers and distributors under one roof as a means toward the goal of wielding greater political heft, that union of inter-dependent insurers and advisers has significance of its own. Since the 1990s, annuity issuers have become increasingly reliant on third-party distributors. Annuity issuers regard distributors, not investors, as their primary audience. The insurance company wholesalers compete for broker-dealer shelf space and advisor mind-share. Their products are arguably tailored as much to broker-dealer needs as to the consumer/investors'.

With the coming of the Boomer retirement wave and the explosion in variable annuity sales in the mid-2000s, the relationship became just as important for the broker-dealers. Anecdotally, a significant portion of the revenues of some broker-dealers came from VA sales. VA commissions are said to be particularly important in the compensation of younger advisers who don't yet have a large enough book of business to generate sufficient asset-based fee revenue. Even if the IRI's political accomplishments turn out to be modest or hard to quantify, the long-term benefits of cementing insurer-distributor relationships and understanding may alone turn out to have made the whole transition from NAVA worthwhile.