Retirement Income
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# Great Hopes Ride on Great-West's New Annuity

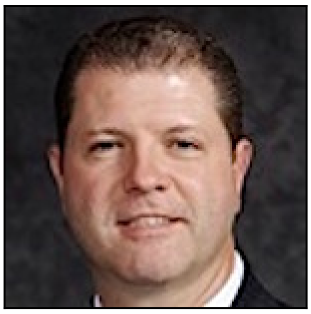
By Kerry Pechter *Fri, Jul 8, 2016*

*Great-West Financial's new Smart Track II variable annuity contract has four different income riders. Will it help Bob Reynolds achieve his goal of making Great-West a top-five retirement company in three to five years?*

Although Empower Retirement is a powerhouse in the retirement plan industry, its corporate sibling, Great-West Financial, has never issued a lot of individual annuities. Ranked 26th in VA sales ($71 million) and 31st in VA assets ($2.55 billion) in the first quarter of 2016 by Morningstar, the firm has no more than a toe in the market.

But Robert Reynolds (below left), the former Fidelity COO who became Great-West's CEO in 2014, has given his minions the big hairy aggressive goal of becoming a top-five retirement income company within the next three to five years. Selling a lot more variable annuities is on the agenda.

To that end, Great-West has headhunted a new team of annuity sales managers from top issuers. Michael McCarthy (at right) arrived from AXA in April as senior vice president of national sales. He has hired annuity executives from AIG, MetLife and Transamerica. He also doubled the number of life/annuity wholesalers, to 32; 27 are assigned full-time to annuities.



The company is also launching new products. Last week, Great-West announced **Smart Track II – 5 Year Variable Annuity**, a B-share contract with a surrender period of only five years instead of the usual six to eight. The surrender penalty in the first two years is 7%, then 6%, 5% and 4% in the remaining three years.

The product is aimed at commission-earning investment advisors, especially in the bank channel (where Great-West is a top seller of life insurance) and at Wells Fargo, one of four remaining full-service brokerages. Great-West may also try to market the product through the Allstate and State Farm sales networks, McCarthy told *RIJ* this week.

Smart Track II is a two-sleeve variable annuity. As seen in similar products from AXA and Hartford in the past, the first sleeve is built for accumulation. Contract owners can invest in dozens of funds from well-known families, with annual expense ratios starting at 0.46%. The mortality & expense risk fee is 1.20%.

The second sleeve is earmarked for lifetime income. Contract owners can transfer money from the first sleeve to this sleeve (and back again, with constraints) to gradually build up an income base. Any of four guaranteed lifetime withdrawal benefit (GLWB) riders can be applied to the second-sleeve assets, at an annual cost of 0.65% to 1.30% of the second-sleeve account value. Second-sleeve assets must be invested in asset allocation funds (with equity exposure ranging from 35% to 65%) at an annual cost of 0.88% to 1.10% of the account value.

## A chance for age-related gains

The catchiest aspect of this product is the potential, under all four GLWB riders, for contract owners to get higher payout rates as they reach new age thresholds. If the account value is high enough (see explanation below), there's a step-up in withdrawal rates from 4% (for single life starting at age 59½) to 5% at 65, to 6% at age 70 and to 7% at age 80. (The withdrawal rates for joint contracts are based on the age of the younger spouse and are 50 basis points lower at each threshold than rates for single life policies.)

The riders are:

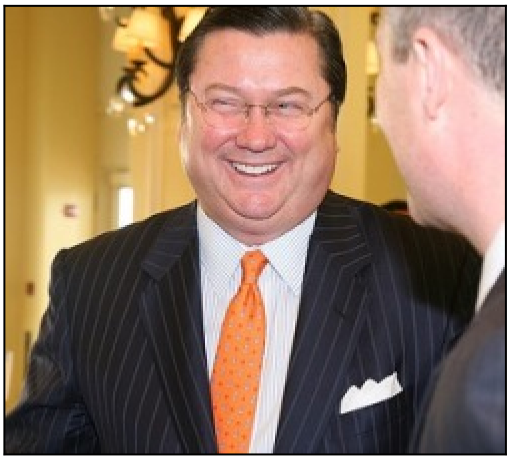
- **Secure Income Foundation** (0.90% of benefit base). This rider provides potential increases in income as the contract owner crosses the age thresholds of age 65, age 70 and age 80. If a client invests $100,000 at age 65 and begins taking $5,000 a year in income, his or her income at age 70 would be the greater of 6% of the account value or 5% of the benefit base ($5,000).
- **Secure Income Plus** (1.30%). This rider is similar to Foundation but provides a 5% simple interest annual "roll-up" to the benefit base for the first ten years of the contract. If a contract owner invested $100,000 at age 60, the benefit base would be at least $150,000 after ten years, assuming no transfers from the second sleeve back to the first sleeve.
- **Secure Income Max** (1.20%). This rider raises the withdrawal rate by an additional 1% for any contributions older than five years. If a 60-year-old invested $100,000 and took no excess withdrawals for five years, he or she could withdraw at least $6,000 a year at age 65, $7,000 at age 70 and $8,000 at age 80. (Or $5,500, $6,500 and $7,500

for couples, respectively.)

Some explanation is called for here. The payout rate doesn't always rise at the threshold ages of 65, 70 and 80. The increase is conditional on the size of the account value. If the current account value, multiplied by the new rate, is not greater than the current payout (the existing rate times the existing benefit base), the new rate doesn't apply. The payout rate and benefit base stay where they are.

For example, consider a single contract owner who reaches age 70 and has a benefit base of $100,000. If the account value has declined (because of withdrawals, fees and/or poor market returns) to, in this particular example, less than $83,333, then that new 6% rate doesn't kick in. That's because 6% of $83,333 is $4,998.98, which is less than the current annual payout of $5,000. The benefit base stays at $100,000 and the payout rate remains 5%.

What triggers the rate increase? If the account value at age 70 was, say, $90,000 and the new payout is $5,400 (6% of $90,000, and higher than $5,000), then the client's payout rate jumps to 6%. The client's payout rate going forward will be 6% and the minimum payment will be $5,400. But, in that case, the benefit base would drop—this is unusual for a GLWB—back to $90,000. As a consolation to the policyholder, the rider fee would also fall, because it is a multiple of the benefit base.



In short, there's a trade-off. Unless market appreciation (or new premia) overcome the natural decline in the account value (as a result of income payments and annual fees), the age-related hikes in payout rates may not apply. The same calculation is repeated each year, so the contract owner can get a second chance at a higher rate.

Smart Track II offers an additional income rider, called the T-Note Tracker (0.65%), where the withdrawal rates increase with a rising 10-year Treasury rate. But that product has gotten little traction because rates are still infinitesimal and don't appear ready to rise significantly in the near future.

"Most variable annuities will allow the contract owner only one way to get a raise. That's through a step-up in the benefit base, and the only way to get that is through market performance. But the odds of getting a pay raise during the income stage are almost nil if you get a down market and you're still withdrawing five percent," McCarthy told *RIJ*. "We offer several ways to get a pay raise."

The Secure Income Max is expected to appeal to couples, McCarthy said. Industry-wide, couples often buy single-life annuity contracts because the payout rate is higher. Secure Income Max, which provides an additional one-percentage-point hike in the withdrawal rate for premia that's left untouched for at least five years, gives couples who don't need income right away the opportunity to buy joint contracts without suffering a "marriage penalty."

To build an annuity sales team, McCarthy has recruited Lance Carlson, a former head of distribution at MetLife; Brett Ford, a former divisional sales manager at Transamerica; Barbara Dare, a former vice president of third-party distribution at MetLife; and Greg Alberti, a former head of strategic accounts at AIG. They report to McCarthy, who reports to Bob Shaw, president of individual markets for Great-West Financial, which is based in Greenwood Village, Colorado.

Great-West currently markets the low-cost, investment-only, no-surrender-fee Smart Track variable annuity through TD Ameritrade and Charles Schwab. Last month, that product was named one of the top 50 annuities of 2016 by *Barron's* magazine.

Great-West recently filed a **prospectus** with the Securities & Exchange Commission for a no-commission version of Smart Track II that is tailored to the needs of fee-based independent financial advisors affiliated with broker-dealers who will be operating under the terms of the Department of Labor's fiduciary rule starting next April.

Under the new rules, advisors who sell B-share contracts and accept commissions must sign (or rather, their broker-dealers must sign) a contract (the so-called Best Interest Contract or BIC) promising that the sale is not merely suitable for a client but also in the client's "best interest." Many advisors are expected to avoid the BIC by switching to fee-based compensation, which means they'll need to sell no-commission versions of their favorite variable annuity contracts. The new version of Smart Track II would fill such a need.

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