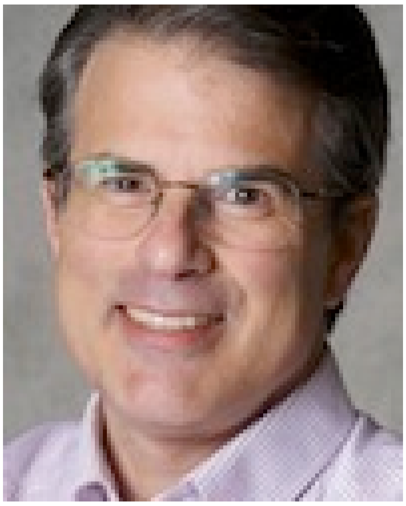
# Legal Limbo: Attorneys Await DOL Resolution

By Kerry Pechter *Thu, Nov 9, 2017*

*At the ALI-CLE's recent conference on securities and insurance law, Tim Pfeifer described new developments in the annuity world. Todd Solash and Merry Mosbacher spoke for and against FIAs, respectively.*



Merry L. Mosbacher runs the insurance and annuity business at Edward Jones, a financial services firm with 15,000 advisors. Todd Solash is president of Individual Retirement at AIG, the financial crisis survivor that sold some $7.4 billion worth of annuities in the first half of 2017.

These two influential annuity executives, a distributor and a manufacturer, respectively, probably agree on many issues. But they disagree on at least one: the value of fixed indexed annuities (FIAs) for investors. AIG sells a lot of FIAs, and Solash is bullish. Mosbacher remains unconvinced; there are no FIAs on Ed Jones' product shelf.

Last Thursday they faced off on the topic, in a friendly way, in front of some 300 securities and insurance attorneys during the American Law Institute–Continuing Legal Education's 35th annual conference last week at the Capital Hilton in Washingtonon, in a conversation moderated by consulting actuary Tim Pfeifer, president of Pfeifer Advisory.

The indexed annuity market is, of courrse, in regulatory limbo. The Trump administration has at least temporarily stopped the implementation of parts of the Obama Department of Labor's "fiduciary rule" that would make it harder to sell variable and indexed annuities to IRA clients for a commission. The rule, in its current form, would also create the potential for a wave of class action lawsuits against the financial industry.

But it's still unclear if that postponement will end in seven weeks, on January 1, 2018, or last until July 1, 2019, as the Trump DOL has proposed. A pending review of the proposal by the Office of Management and Budget will help determine that.

**'Manufacturered' return**

Over the past five years or so, indexed annuities have been, from a pure sales perspective, the brightest spot in the annuity firmament. Their commissions make advisors want to sell them and their value proposition—more upside than bonds with zero risk to principal—has found an audience. But they're likely to remain a niche product until they win over the Merry Mosbachers of the world.

"We don't offer any equity derivatives," Mosbacher said, referring to the options that drive FIA returns. "It's a manufactured return, and we have problems with that as a source of return for our type of customer. It's not aligned with what we think our clients need. With the indexed products, the sales message often goes: In a period low interest rates, you get the upside of the equity market but not the downside. That's what customers hear.

"We want our clients to understand the risks of what they buy. The indexed annuity is nothing more than a floating-rate fixed deferred annuity with a yield of up to four percent. Is it worth it to take that kind of risk? We haven't been able to get the math to work out where the answer is 'Yes.' And when we ask the carriers about it, no one has been able to prove that they'll get a higher return on an indexed annuity than they will on a fixed.

"We've been paying a lot of attention to the fee-based variable annuities. We're not offering them now, but we recognized that we're all going to a fee-based world. That trend was only accelerated by the DOL rule. We don't like today's fee-based products. It would be a cost increase for our clients to strip out the commission and put them in a fee-based product."

But AIG's Solash, a former AXA executive, claimed that indexed annuities meet certain needs that other financial products don't. "AIG is in all of these businesses—variable, indexed and fixed annuities—and we're unique in that respect. It lets us adapt to market changes and changing client needs. The indexed annuity's message—you get a floor of zero losses but also equity exposure—is a powerful one. That's a product that should have its time. It gives investors a different spot on the efficient frontier, a different outcome.

"We have a real demographic problem and a real public need [with regard to retirement financing], and we shouldn't make it hard to sell these products. That's why some of the regulation is detrimental. If annuities are too hard to sell, then products won't get talked about at all. We think that's a big problem for clients. They need protection.

"It's a interesting time. There's never been a time with so much convergence and confusion. It's very much mix-and-match. As manufacturers we actually provide very specific risk-appetite and risk/reward combinations, but it's hard on us. The world is built around fixed silos. Things are mixing in ways that are positive. But it's difficult for all of in the ecosystem."

**Lingering uncertainty**

Last week ended on a note of relief for the defined contribution industry, with House Majority Leader Paul Ryan announcing that the Republican tax proposal would not shrink tax deferral for retirement savings to offset the 10-year, $1.5 trillion tax cut he hopes to push through the Senate and onto the president's desk. But the lawyers who gathered for the ALI-CLE conference on securities and insurance law still had lots of shop to talk.

There were several items of general retirement-industry interest that came up during this admittedly specialized conference for a specialized segment of the legal community. Tim Pfeifer, a consulting actuary, offered a roundup of recent developments across the deferred and immediate annuity landscape.

**LTCI-annuity hybrids.** "There's a lot of pent-up interest in adding long-term care insurance features to annuities," he said, with declared rate fixed annuities the most likely vehicle. "That's been causing a bit of a stir, with several companies thinking about offering them."

**Fewer FIAs with living benefits.** "There's a reduced focus on adding guaranteed lifetime withdrawal benefits to indexed annuities. Although GLWBs were once a prime driver of FIA sales, that importance has declined in the last three years. About 50% of FIA sales involves a GLWB rider, but that figure used to be as high as 65% or 70%."

**Deferred income annuities.** "Companies are now looking at DIAs as possibly having an indexed feature. When income begins, it would have an indexed growth component," Pfeifer said. That could help perk up DIA sales, which slipped early in 2017 before flattening out. Companies see the index-linked DIA as a potential competition for variable annuities with GLWBs, SPIAs and conventional DIAs. Issuers—Nationwide may be one—are also looking for ways to add liquidity features to DIAs to ease contract owners' fears about irrevocability.

**FIA commissions.** "The average commission on an FIA used to be about 8%. That figure is now around 5%," he said. If that's true, then VAs now offer the highest commission, at about 7%. Pfeifer attributed the decline in FIA commissions to the DOL fiduciary rule as well as to the increase in sales of FIAs at brokerage firms, where they come under FINRA scrutiny.

**Impaired life annuities.** "We've seen one company using substandard annuities for long-term care needs." For people who are not in good enough health to qualify for long-term care insurance, "substandard" annuities (aka "medically underwritten" or "impaired" annuities) offer a way to maximize future income to cover medical costs. [Anecdotally, one insurer offered the SPIA pay rates for a 70-year-old to a 64-year-old policyholder in poor health.)

**ILVAs.** Pfeifer noted the growing success of indexed-linked variable annuities (ILVA), which are also known as structured variable annuities. Voya will introduce its Ascend ILVA in early 2018; it will join Allianz Life, AXA, Brighthouse (formerly MetLife), and Members & Investments (a unit of CUNA Mutual Group) in that space. ILVAs are classified as securities because, unlike FIAs, they can result in loss of principal.