
Mr. Indexed Annuity Goes To Washington

By Editor Test Sun, Jun 7, 2009

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On a sultry afternoon in Washington, D.C. in early May, the U.S. Capitol looked stark, lonely, and forbidding. The famous white dome, broad steps and balustered porticos glowed like the Taj Mahal but appeared deserted except for two or three black-clad sentries cradling automatic rifles.

Eighty-some members of the National Association for Fixed Annuities (NAFA) were undaunted and undeterred, however. In groups of four or five they had cabbied to the Hill from the gilded luxury of the Renaissance Mayflower Hotel and were bound for appointments with their legislators—or at least with their legislator's legislative aides.

The purpose of the meetings—a "March to the Hill" orchestrated for NAFA by the lobbying arm of the Washington law firm Blank Rome—was to educate senators and congressmen or their aides about indexed annuities and SEC Rule 151A, which made equity-indexed annuities subject to SEC regulation.

Most of all, the purpose was to urge legislators from both major parties to co-sponsor a bill that would reverse 151A, which reclassified index annuities as securities rather than insurance products. The rule was approved by the SEC last December but doesn't take effect until 2011.

The new bill, which apparently has not yet been submitted or given a number, would nullify 151A and "clarify" the Securities and Exchange Act of 1933 to ensure that EIAs are exempt from federal securities regulation. The original co-sponsors of the bill are Gregory W. Meeks (D-NY) and Tom Price (R-GA). There is no companion bill in the Senate yet.

Rep. Meeks' legislative director, Tre Riddle, explained the Queens, New York congressman's interest in the bill: "We have a number of constituents who hold annuities who have expressed concern about this issue, as have independent insurance agents who live or work in our district and insurance companies based in New York.

"As a member of the House Financial Services committee, we're acutely aware of the financial markets, globally, nationally, and in New York. We're also sponsoring the bill because we disagree with the SEC interjecting itself in a traditionally state-regulated matter."

The Meeks-Price bill is part of NAFA's "two-pronged assault" on 151A, which includes a lawsuit filed against the SEC by indexed annuity manufacturers and wholesalers, including American Equity Life, National Western Life, Midland National Life, OM Financial Life, BHC Marketing and others.

The lawsuit argues that indexed annuities are annuities, with guarantees that shift risk from the consumer

to the insurer, and therefore should be regulated as other insurance products are—by the states, not by the SEC. It rejected the SEC's claim that indexed annuities are risky assets because their upside is variable, even though they guarantee principal.

If successful, the lawsuit and the legislation would eliminate the ambiguity of EIAs' regulatory status forever. "Litigation locks the door and legislation throws away the key," said Danette Kennedy, NAFA's government affairs director.

Rule 151A has roiled the world of EIAs, which are a type of structured product in which most of the assets are invested in bonds and a small portion is used to buy options, typically on the performance of the S&P 500. The bonds offer principal protection (less costs) and the derivatives allow the contract owner to participate in S&P gains, if any.

Such products—especially those issued by Allianz Life—sold extremely well after the 2001 dot-com crash, when many investors felt paralyzed by a fear of buying stocks and the absence of attractive returns in fixed income investments. EIAs might be expected to shine in the current environment—a murky outlook for equities and low interest rates—but uncertainty about the outcome of the fight over 151A has caused far more EIA manufacturers to pull products off the market than introduce new ones.

Privately, many in the EIA industry claim that the SEC created Rule 151A to divert lucrative EIA transactions from insurance agents and IMOs to broker-dealers and their registered reps. Kim O'Brien, the executive director of NAFA, said that, while NAFA is fighting 151A on legal grounds, the stakes are ultimately economic. "Clearly, [the broker-dealers] are desperate for money," she told RIJ.

Others have said that then-SEC chairman Chris Cox, a Bush administration appointee, was moved to regulate indexed annuities after watching a Dateline NBC news episode in the spring of 2008 that depicted alleged mis-selling of EIAs to senior citizens for whom the products were inappropriate.

If 151A takes effect in January 2011, as scheduled, only those with securities licenses will be able to sell EIAs, and all EIA sales will have to be cleared through broker-dealers. To avoid seeing their EIA business diverted to broker-dealers, insurance agents will have to get securities licenses and IMOs must consider becoming broker-dealers—at no small cost.

That's what one large IMO, Financial Independence Group of Cornelius, NC, is doing, according to Brian K. Williams, its chief operating officer. "We want to be prepared for whatever comes along," he told RIJ at the NAFA annual meeting.

Before the NAFA members dispersed in taxis from the Renaissance Mayflower Hotel to their various meetings at the Capitol and the Dirksen, Hart, Longworth, Russell, Cannon and Rayburn office buildings, they received some inside tips on how to lobby Congress.

"Most folks in Congress want to do the right thing," Rep. Price said. "But when it comes to insurance, they don't know what the right thing is. You know much more than they do about fixed annuities, so you have to educate them. Above all, be passionate, or your representatives won't feel compelled to act. Show passion

for their constituents, not for your pocketbooks. And don't be discouraged if you don't get to meet your representative. The legislative aides are the key people here in Washington. They're the ones you need to impress."

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