
Nationwide Ties New VA Income Rider to Managed-Vol Funds

By Kerry Pechter Thu, Dec 12, 2013

For its deferral bonus, the "Income Capture" GLWB offers a simple interest rate credit of 3% plus the nominal rate of the monthly 10-year Treasury constant maturity (currently 2.86%).

Pending SEC approval, Nationwide Life Insurance Company is expected to announce a new living benefit rider on its Destination 2.0 variable annuity contract. Selection of the rider, called Lifetime Income Capture, requires investment in one or more of five "managed volatility" portfolios. Its annual deferral bonus is linked to the 10-year Treasury rate.

The deferral bonus or roll-up is the sum of 3% simple interest plus the nominal rate of the monthly 10-year Treasury constant maturity (currently 2.86%). The crediting period lasts until the first lifetime income payment or up to 15 years. The roll-up can't be less than 4% or more than 10%, according to the prospectus.

The expense ratio of the Income Capture rider is 1.20% (1.50% maximum) for a single person, and an additional 0.30% for a joint contract. The mortality and expense risk charge is 1.10% on the B-share, which has a seven-year, 7% surrender schedule. The administrative charge is 0.20%. Death benefit options are extra. The annual payout rates and age bands that apply to Income Capture are not included in the current filing, which is dated effective December 16, 2013.

In addition to the lifetime withdrawal benefit, other payout options include: systematic withdrawals, annuitization or a lump sum payment equal to the current lifetime withdrawal amount multiplied by an age-related factor.

Contract owners who choose Income Capture have five investment options:

- American Funds Insurance Series – Managed Risk Asset Allocation Fund (Class P2)
- Nationwide Variable Insurance Trust – NVIT Cardinal Managed Growth & Income Fund (Class II)
- Nationwide Variable Insurance Trust – NVIT Cardinal Managed Growth Fund (Class II)
- Nationwide Variable Insurance Trust – NVIT Investor Destinations Managed Growth & Income Fund (Class II)
- Nationwide Variable Insurance Trust – NVIT Investor Destinations Managed Growth Fund (Class II)

The expense ratios of these funds do not appear readily accessible in the prospectus. The NVIT Cardinal Managed Growth & Income Fund has an expense ratio of 1.02% (1.31% without the temporary waiver), according to Nationwide's website.

Regarding the impact of required minimum distributions at age 70½, the prospectus states:

"Contract Owners subject to minimum required distribution rules may not be able to take advantage of the Lifetime Withdrawal Percentages available at higher age bands if distributions are taken from the

contract to meet these Internal Revenue Code requirements. Contract Owners who elect not to take minimum required distributions from this contract, *i.e.*, they take minimum required distributions from other sources, may be able to take advantage of Lifetime Withdrawal Percentages at the higher age bands.”

The NVIT Cardinal Managed Growth & Income Fund’s Volatility Overlay, which BlackRock manages, is described on Nationwide’s website as follows:

The Volatility Overlay is designed to manage the volatility of the Fund’s portfolio by using stock index futures to hedge against stock market risks and/or to increase or decrease the Fund’s overall exposure to equity markets.

The Volatility Overlay also invests in short-term fixed-income securities (or Underlying Funds that themselves invest in such securities) that may be used to meet margin requirements and other obligations of the Fund’s futures positions and/or to reduce the Fund’s overall equity exposure.

When volatility is high, the Volatility Overlay will typically seek to decrease the Fund’s equity exposure by holding fewer stock index futures or by taking short positions in stock index futures. A short sale strategy involves the sale by the Fund of securities it does not own with the expectation of purchasing the same securities at a later date at a lower price. When volatility is low or stock market values are rising, the Volatility Overlay may use stock index futures with the intention of maximizing stock market gains.

These strategies may expose the Fund to leverage. Therefore, even though the Core Sleeve allocates approximately 50% of its assets to equity investments, the Volatility Overlay will be used to increase or decrease the Fund’s overall equity exposure within a general range of 0% to 65%, depending on market conditions.

Nationwide Fund Advisors (“NFA”) is the investment adviser to the Fund and is also responsible for managing the Core Sleeve’s investment in the Underlying Funds. BlackRock Investment Management, LLC, the Fund’s sub-adviser, is responsible for managing the Volatility Overlay, including the fixed-income securities it holds.

The American Funds’ Managed Risk Asset Allocation Fund that’s available to Income Capture clients is sub-advised by Milliman. The Milliman Volatility Overlay is described as follows on the American Funds website:

The fund employs a risk-management overlay referred to in this prospectus as the protection strategy. The protection strategy consists of using hedge instruments—primarily short positions in exchange-traded futures contracts—to attempt to stabilize the volatility of the fund around a target volatility level and reduce the downside exposure of the fund during periods of significant market declines.

The fund employs a sub-adviser to select individual futures contracts on equity indexes of U.S. markets and markets outside the United States that the sub-adviser believes are correlated to the underlying fund’s equity exposure. These instruments are selected based on the sub-adviser’s analysis of the

relation of various equity indexes to the underlying fund's portfolio. In addition, the sub-adviser will monitor liquidity levels of relevant futures contracts and transparency provided by exchanges as the counterparties in hedging transactions...

The sub-adviser will regularly adjust the level of exchange-traded futures contracts to seek to manage the overall net risk level of the fund. Even in periods of low volatility in the equity markets, the sub-adviser will continue to use the hedging techniques to seek to preserve gains after favorable market conditions and reduce losses in adverse market conditions.

In situations of extreme market volatility, the exchange-traded equity index futures could significantly reduce the fund's net economic exposure to equity securities. The fund's investment in exchange-traded futures and their accompanying costs could limit the fund's gains in rising markets relative to those of the underlying fund, or to those of unhedged funds in general.

To get a wider range of investment options, contract owners can take the Nationwide Lifetime Income Track rider. Though it has no roll-up, investors who wait at least five years before starting income get an extra half-percent annual payout. This rider currently costs 0.80% of the benefit base per year.

The Nationwide Lifetime Income Track option has two sets of payout bands. One band is for single people who take income within five years of purchase. It pays 4% a year to those ages 59½ to 64, 4.5% to those ages 65 to 74, 5% to those ages 75 to 80, and 5.5% to those ages 81 or older. Another band, for single people who wait at least five years before taking income, pays, as mentioned, a half-percent more in each age band.

For joint contracts, the payout rate is 0.25% less than the rate for single lives in each age band mentioned above. For instance, the payout for a 65-year-old couple, after a five-year waiting period, would be 4.75% per year. The current additional charge for the joint option on the Income Track rider is 0.15%.