New York Life Remixes the Variable Annuity

By Kerry Pechter *Tue, Jul 17, 2012*

You've heard of New York Life's Guaranteed Future Income, where clients pay today for lifetime income several years from now. A new NYL product, Income Plus, also locks in future income, but lets policyholders put some money at risk during the waiting period, a recent prospectus shows.

At a time when most variable annuity issuers are draining the risk out of their products, New York Life has filed a prospectus for a variable annuity that takes the company's fast-selling deferred income annuity (DIA) and mixes some upside potential into the deferral period.

The new single-premium variable annuity will be called New York Life Income Plus. The prospectus was filed for SEC approval on July 10. The product, not yet announced, is a variation on New York Life's Guaranteed Future Income DIA, which was launched a year ago and has attracted over $1 billion in premiums.

People who purchase the existing Guaranteed Future Income DIA product purchase a delayed income annuity, and get a discounted price by buying early. Between the purchase date and the income date, the money grows in the insurer's general account. The future payout is fixed at the time of purchase.

The new Income Plus product, not yet announced by the issuer, also involves purchasing a delayed income annuity with a predetermined payout. But between the purchase date and the income date, the premium starts out in mutual funds, and is incrementally transferred into the general account (through an "Automatic Income Benefit Purchase Formula") where it funds the future income annuity. Policyholders can also accelerate the transfer of money to the income annuity.

The guaranteed income from the Income Plus is smaller than the guaranteed payout from the straight DIA. In return, if interest rates or equity prices rise during the deferral period, clients have the chance that their accounts will grow fast enough to fund the income stream and then some. They can buy additional guaranteed income with the excess, if any, or leave it in the separate account or spend it as they wish.

The product is a bit like the Hartford Personal Retirement Manager, which allows the contract owner to gradually move money from a variable account to a fixed account. It appears to differ from a conventional GMIB (guaranteed minimum income benefit) variable annuity rider in that the policyholder is pre-committed to purchasing the income annuity after the waiting period.

With Income Plus, New York Life takes the risk that the market value of the underlying mutual fund investments will fall or fail to appreciate and that the assets will not be sufficient to fund the deferred income annuity. To compensate for that risk (besides promising as much income up front as it does in the DIA product) the company charges a 1% fee on the "unfunded income benefit base"—the amount that at any given time remains to be paid to purchase the income annuity. That balance declines as money moves from the separate account to the general account.

The permitted investments under Income Plus include New York Life's proprietary MainStay mutual funds, as well as funds from BlackRock, Columbia, Dreyfus, Fidelity, Janus, MFS, Neuberger Berman, The Royce Capital Fund, and Victory Variable Insurance Funds. Fund fees range from 47 basis points to 162 basis points. There is a 2% charge for cancelling the rider, as well as a seven-year contingent deferred acquisition cost period that starts with a first-year surrender charge of 8%. The current and guaranteed mortality & expense risk is 1.35%.

"While this rider allows for investment in variable subaccounts during the accumulation phase followed by a guaranteed fixed payout in the distribution phase—which bears similarity to a GMIB—it is distinguishable from a GMIB," said a consulting actuary and living benefit designer who had a chance to read the Income Plus prospectus.

"The GFIB rider [Guaranteed Future Income Benefit, the deferred income annuity rider in Income Plus] appears to call for investment of only a single premium (no further premium payments allowed into the VA). Each quarter, a portion of the accumulation value is removed and the accumulation value is commensurately decreased. The portion removed is used to buy a fixed immediate annuity with deferred first payment.

"This rider appears less risky for an insurer to issue than a GMIB, even though both provide guaranteed future fixed immediate annuity benefits. With a traditional GMIB, the insurer has in essence sold a complex put option where the insurer's risk depends on both variable performance during the accumulation period and the level of interest rates at the point GMIB annuitization is triggered. The full accumulation value can remain invested by the consumer in variable subaccounts for the full accumulation period.

"In contrast, with the GFIB rider the insurer appears to regularly sell off accumulation units, raise cash, and apply the cash to a fixed immediate annuity with deferred first payment. There would appear to be somewhat less investment risk to the insurer as (i) the insurer can sell off higher and lower numbers of accumulation units based on variable performance to raise whatever amount of cash is needed each quarter to fund the future benefit payments and (ii) the interest rate environment can be taken into account to perform better asset-liability management during the accumulation period for the eventual fixed payouts than is achievable with a traditional GMIB.

"That's not to say it's a riskless proposition for the insurer, as a long period of investment underperformance and/or a long period of low interest rates makes it tougher to achieve the eventual fixed payout guaranteed. And the eventual fixed payout is guaranteed, regardless of whether there was sufficient value in the accumulation account along the way to fully fund it."