Selling Income Annuities on Greed, Not Fear

By Kerry Pechter *Thu, Sep 26, 2013*

Iowa advisor Curtis Cloke claims that his 'Thrive" system,' which finances retirement with period certain, cash-refund deferred income annuities, offers safety without sacrificing upside. He's one of RIJ's 'RetiremEntrepreneurs.'

Burlington, Iowa is a small, fading river town where Mississippi steamboats and mighty railroad lines once traded freight. Adrift in an ocean of cornfields, it's an unlikely place to find what may be the future—perhaps even the salvation—of the income annuity business.

But that possibility is what drew me and a dozen other people to Burlington one morning last August. We had enrolled in Thrive University, the fancy name for the workshops where Curtis Cloke teaches his Thrive Income Distribution System for using deferred income annuities (DIAs) in retirement.

For a day-and-a-half, we sat classroom-style in a fluorescent-lit room and heard Cloke, a large, enthusiastic man of 50, talk through hundreds of slides about Thrive's recipe for creating mosaics of annuities, mutual funds and permanent life insurance and solving the major risks of retirement: longevity, volatility, inflation, tax, shortfall and legacy.

"Thrive believes in making the impossible possible," said Cloke. He delivers about a dozen of these workshops at different places around the country each year, charging up to $1,300 a seat for a taste of the Thrive secret sauce. "We buy income and invest the difference. We maximize the amount of money that's unfettered to income needs."

With a two-inch loose-leaf binder of material to cover and less than 18 hours to cover it, Cloke has to talk fast. Observations, anecdotes, calculations and data points come in torrents. The details can be dizzying. "I get a little deeper into the weeds than most people care to get," he said. "But you have to get your mind around the flexibility of these products."

Unexpectedly rapid sales of deferred income annuities since mid-2011 has gotten a lot of people interested in Cloke and Thrive Income. That's why, along with financial advisors, the Thrive University class in Burlington in August also attracted people from higher up the annuity food chain.

There was Jay Robinson of Financial Independence Group (FIG), an insurance marketing organization that uses Thrive principles in its "Booming Income" program for producers; Cliff Kitchen of Guardian Life, which intends to use Cloke's ideas to help its agents sell its deferred income annuities; and Gary Baker from Cannex, which provides income annuity pricing data to IMOs and broker-dealers. The Thrive Income method has even gotten the blessing of The American College, which includes it in the curriculum for its

Retirement Income Certified Professional designation.

Don't be an "asset hugger"

Cloke's Thrive Income method is a process, not a product. It follows the time-honored philosophy that retirees should use income annuities to cover any income need not covered by Social Security or pensions and to invest the rest of their money in risky assets—to maintain liquidity, protect against inflation, meet emergency needs or establish a legacy.

That's the same philosophy espoused by authorities as varied as the Retirement Income Industry Association, by Tom Hegna, the popular lecturer and author of "Paychecks and Playchecks," and by any number of marketers at companies that issue income annuities. It's a natural extension of the idea that people—and especially retirees—should gamble only with money they can afford to lose.

But Cloke takes this argument up a notch. He may be the first person to come up with data in support of the counter-intuitive idea that annuities provide more liquidity and more legacy potential than a retirement income program based on systematic withdrawals from a risky portfolio of stocks and bonds. In other words, annuities aren't just for fear-driven retirees. They're for greed-driven ones, too.

Instead of presenting annuities as pure defense, Cloke gets aggressive with them. He makes them un-boring. In his cosmology, it's retirees who *don't* annuitize that are timid. He calls them "asset huggers" who allow all of their money to become "hostage" to income production, and therefore not truly free for risk-taking, or emergencies or heirs.

How is this possible? It's possible if you use sequential or overlapping inflation-adjusted deferred income annuities with periods certain or cash refunds for retirement income and invest the rest of your money in growth-oriented mutual funds. The Thrive method generates customized, precisely documented retirement income plans using combinations of deferred income annuities (for income), life insurance (for legacies) and mutual funds, and to squeeze any efficiencies (tax advantages, mortality credits, higher yields) from them that he can.

Thrive clients don't have to worry that they might get "hit by a bus" in early retirement and lose a bunch of money. Since they have a safe income to live on, they can ignore market volatility. They can afford to let their equity investments compound until they die. They don't know how large their legacy will be, but they know there will be one.

"The process is not unique to him, but he does it in a way that's elegant. And he's created some complex tools to illustrate income," said Kitchen, who runs the Living Balance Sheet platform at Guardian Life, where agents learn how to structure annuity portfolios. He made the pilgrimage to Burlington in August. "Two of our leading reps went to Thrive University and told me, 'Cliff, you have to go out there. This guy has his finger on the pulse of this stuff.' He's the best at what he does."

Fun with Dick and Jane

During the workshop, Cloke offered up several hypothetical examples of a Thrive solution to a retirement income puzzle. One simplified case involved Dick and Jane, an imaginary couple ages 60 and 59 respectively. They wanted to retire in six years.

A mass-affluent couple, Dick and Jane had about $504,000 in non-qualified savings and each had about $95,000 in qualified savings. In addition, Dick expected to receive a monthly pension of $1,100. Both expected Social Security benefits.

The couple needed about $1,800 a month from their savings to reach their spending goal. They also wanted a 3% annual inflation adjustment. To achieve that for the first five years of retirement, Cloke used $121,000 of their non-qualified money to buy a five-year period-certain deferred income annuity with a 3% annual inflation adjustment that would start paying out in six years, when Jane reached age 65.

At the same time, he used $282,000 of their non-qualified money to buy a 20-year period certain DIA with a 3% annual inflation adjustment, starting in 11 years when Jane reached age 70. The two DIAs, in sequence, cost a combined $403,000 and produced the $2,000 a month inflation-adjusted income that Dick and Jane said they needed.

As for their remaining $291,000 in savings (including the assets in both IRAs and the rest of the non-qualified money), Cloke invested it in mutual funds for long-term compound growth at an expected rate of 5%. If Dick and Jane took no withdrawals from it for splurges or emergencies, it could be worth about $1 million in 25 years.

Is this strategy better than a traditional 4% systematic withdrawal strategy from a balanced portfolio? Cloke, who has done the cash flow comparisons, would argue that the inflation-adjusted DIAs yield more income with zero market risk. The instinctive answer is that it probably fares better in unfavorable markets, for highly risk-averse clients, and for advisors who like insurance products.

Let's make a crude, back-of-the-envelope analysis: If Dick and Jane used a 4%, inflation-adjusted withdrawal strategy, they could take 4% of $890,000 (the estimated value of their nest egg in six years, according to the Department of Labor's calculator). That's almost $3,000 a month to start.

Doesn't that beat Thrive's $1,800-a-month annuity payout? Yes and no. As Cloke likes to say, the entire nest egg is "hostage" to income. Dick and Jane can't dip into their savings without cannibalizing their income stream or their legacy fund. Moreover, their portfolio would likely require a higher bond component in order to match the safety of the annuity strategy.

A more apples-to-apples comparison might call for Dick and Jane to set aside $291,000 for long-term growth, as Thrive would have them do, and then take 4% from the rest of their assets (worth about $500,000 when they retired, according to the DoL) for an estimated income of $20,000 per year or $1,667 per month. At first glance, that strategy looks comparable to the DIA approach.

When you factor in the potential differences in fee drag (the annuity income is net of costs), the tax treatment of the income streams (a portion of the DIA income is excluded from income tax because it was purchased with non-qualified money), the transparency that comes from using period-certain annuities and the peace-of-mind that comes from the guarantees, the Thrive method looks even better, Cloke claims. His numbers are compelling enough, he says, to produce a 95% closing rate in six months with retirement income clients.

"We can compete with investments every day of the week because of the efficiencies of this system," he said. "I know that's not the view of the [investment] industry. But I'll annihilate them on the fees on the assets held hostage to income. An asset manager who can't have a conversation about insurance [products] can't compete with us."

The Dick and Jane scenario offers, as mentioned earlier, a simplified version of the Thrive process. Other hypothetical cases that were presented at the workshop in Burlington, using high-net-worth clients, suggested that the Thrive method can yield even greater efficiencies for people with challenging tax situations, cash flow needs, or legacy desires.

Thrive goes national

Cloke's personal story is of the jeans-to-Brooks Brothers variety. His grandfather was a family farmer in Iowa who had lost the farm. As a kid, Cloke would ride on the tractor seat beside him as he plowed other people's land, listening to the elder's advice about hard work, thrift and charity. "Save 10%, give 10% and live on 80%," he recalls.

Out of high school, Cloke became an underground miner, working 600 feet below the surface of the earth in central Iowa's vast Jurassic-period deposits of gypsum, the chalky mineral that's used in wallboard, plaster and cement. A serious mine injury landed him on Social Security disability. By that time he had a house and a family but not much of a future.

Then, a mentor materialized, a local insurance agent who told him, "You could do what I do." In 1987, Cloke became a Prudential representative. He struggled. He landed a big contract. He began to prosper. In 1999, he discovered a product that Prudential didn't sell publicly—a five-year deferred income annuity—and started using it in retirement income plans. "That's how Thrive Income was born. I'd been laddering bonds and I realized that this was the perfect bond," he said.

In 2007, he received a phone call from a MetLife executive and actuary named Garth Bernard. Bernard, a gregarious income annuity enthusiast with a big Rolodex, thought Cloke was onto something huge. In April 2008, Bernard quit MetLife to go into business with Cloke. They took the Thrive Income Distribution System national.

The financial crisis interrupted their entrepreneurial plans. Bernard eventually left the business and moved abroad, but not before introducing Cloke to his network and bringing Thrive Income to the attention of the wider retirement income industry. In the wake of the crisis, with Boomers looking for financial safety and more than a dozen insurers marketing or developing DIAs, Cloke found himself to be in the right place at the right time.

The Thrive Income method is now a modest juggernaut. It reaches financial advisors and insurance agents either directly or indirectly through Cloke's advisory partnership, Two Rivers Financial Group, through Thrive University workshops, through proprietary software and training programs, and through a video that's part of the curriculum for the Retirement Income Certified Professional designation at The American College.

Its principles are also disseminated through the "Booming Income" platform that FIG maintains for its producers, through the Living Balance Sheet platform used by Guardian Life agents, and through a spinoff group called Precision Retirement by Design, which other advisors consult for income solutions.

Relationships with organizations like The American College have given Thrive Income a growing legitimacy, at least in circles that don't reject income annuities out of hand. "Our curriculum tries to include many voices, and Curtis is an important voice," said David Littell, an attorney, CFP and co-director of the New York Life Center for Retirement Income at The American College.

"A lot of the usual conversation about using income annuities for 'flooring' focuses on the safety of it. The academics tend to focus on the 'utility function.' But Curtis is saying that his method is actually a *cheaper* way to create retirement income," Littell added.

'Take this and run with it'

A few weeks after the Thrive University workshop, I called some of the people who attended to get their impressions of it. One was Denny Zahrbock, a Minneapolis-area financial advisor and an insurance celebrity of sorts. He is currently chairperson of the exclusive Top of the Table of the Million Dollar Round Table, an elite club of hyper-successful insurance agents and financial advisors.

"In some client situations that certainty of income would be appealing. But I wouldn't be as confident selling this as Curtis is. He's so confident that you buy right into it," Zahrbock told *RIJ*. "The biggest negative is that it's not mainstream yet. That's the problem for any pioneer."

Another Thrive University alumnus, Steve Goldstein of Dakota Wealth Solutions in Moorestown, N.J., said he likes Cloke's method because, once the annuities are purchased, the client's assets grow rather than shrink over time. "You're never running a negative cash flow," he said. Goldstein wrote the software for the simplified form of Thrive Income that FIG offers its agents.

"The right people will take this and run with it," he said, adding, however, that most investment-driven advisors and even most insurance-minded advisors will shy away from it, either because it's too strange or too labor-intensive. "A lot of investment professionals aren't open-minded in looking at what the insurance industry has to offer. And not every insurance agent will want to spend the time to concentrate on this. But the top-level agents will."

Kitchen of Guardian Life sees Thrive as effective, but a niche phenomenon. “What he does is revolutionary, but it’s not going to start a revolution because there are so many competing voices out there. And there’s a huge difference in compensation” [between income annuities and other, higher-commission products that intermediaries can sell], he said.

More bullish is Robinson of FIG, which is the first insurance marketing organization to promote the Thrive Income Distribution System to its producers. “There’s going to be a huge market for DIAs,” he said. “You’ll see the direction of the industry moving away from the variable annuity to the fixed indexed annuity with a living benefit and the DIA.” To help its agents sell those DIAs, FIG is counting on Curtis Cloke and Thrive.