Solving the SPIA compensation puzzle

By Editor Test *Tue, May 3, 2011*

By re-valuing each client's annuity contract each day, New York Life enables advisors to charge a fee based on the (shrinking) cost of replacing the income stream.

Many of New York Life's 11,000 agents were wary about selling income annuities. Agents feared that clients would resist any kind of annuities because of concerns about the high fees that are sometimes charged by variable annuities. But Christ Blunt says that agents were soon startled by the warm reaction that they got from many clients. "If you tell 65-year-old people that you can give them a paycheck for life, they love it," he says.

Agents start by talking to clients about their desire for guaranteed income. A typical client might say that he has $2,500 a month in Social Security benefits and would like to have another $1,000 in guaranteed income. The agent explains how an income annuity can fill the gap.

While most annuity sales have come from agents, banks have started to play a growing role. When savers grumble about the low yields on certificates of deposits, bank tellers refer them to advisors who can sell annuities.

In the past year, New York Life has been gaining a foothold among broker-dealers, signing agreements with Edward Jones and major wire houses. Brokers had been reluctant to sell the annuities because it was not clear how to compensate advisors. Many advisors typically charge a fixed annual fee, such as 1% of assets. If a client pulls $100,000 out of a portfolio and uses the cash to buy an annuity, the advisor's income could fall by $1,000 a year. To get around the problem, New York Life now calculates the daily value of each client's annuity contract. Advisors charge annual fees based on the (shrinking) present value of the annuity.

"If I am in a fee-based account, how do you charge a fee on an income stream?" Blunt said. "Every day we price an income annuity and we can tell you what it would cost you today. Say that you bought an annuity a month ago. We could tell you on any given day how much premium you would have to give us to replace the income stream that you already have. You are showing the present value of the remaining payments. It is the declining amount."