# The Year of Living Less Dangerously

By Editor Test *Wed, Jun 16, 2010*

*A year or more after the financial crisis, major VA annuity issuers are trying to do more with less—less risk, that is. Here are nine of the latest efforts.*

Over the past year, major variable annuity issuers have been busy making their contracts and contract riders less vulnerable to the kind of shocks they suffered from falling share prices and rising hedging costs.

Here's a look at nine of the past year's noteworthy product developments from top-15 issuers, many of whom tried to make a virtue of necessity by incorporating designs that reduce the product's risks while also responding to the demands of various types of clients and intermediaries. They include:

- Allianz Life Retirement Pro
- AXA Equitable Protected Capital Strategies
- ING Select Opportunities
- Nationwide Destination DV
- Jackson National LifeGuard Freedom Net 6
- MetLife Growth and Guaranteed Income
- Hartford Life Personal Retirement Manager
- AXA Equitable Retirement Cornerstone Series
- John Hancock AnnuityNote

Not all of these nine contracts or contract revisions have been approved or come to market yet. The first four are new this spring. The rest were reported in *Retirement Income Journal* at various times in the past year.

**Allianz Life Retirement Pro**

The soon-to-be-released Retirement Pro from Allianz Life has two investment sleeves, which places it in the same innovative category as the Axa Cornerstone and The Hartford Personal Retirement Manager two-tier contracts, both recently introduced.

In the Allianz Life product, the client's riskiest assets go into one sleeve, called the Base Account, which has a wide range of investment options. Its value is not guaranteed. Less risky assets go into the Income Advantage Account. It offers limited investment options, but the client can apply a guaranteed lifetime withdrawal benefit and a death benefit to it.

Retirement Pro is aimed at clients of fee-based investment advisors who hold security and insurance licenses. It has no distribution charge. Clients can apparently move money back and forth between the accumulation account and the guaranteed account before taking income.

There’s a 30-basis point charge on investments in the Base Account. The maximum annual expense ratio on the Income Advantage Account will be 1.75%, but the current charge has not been established yet.

The contract has an unusual, inflation-sensitive payout formula. Instead of corresponding to the age of the annuitant at the time of the first income payment, payout rates depend on the 10-year Treasury yield. The payout rates are currently 4%, 5%, 6% or 7%, depending on whether prevailing 10-year Treasury yield is 3.49% or less, 3.5% to 4.99%, 5% to 6.49%, or 6.5% and above.

Investment options include funds managed by AIM, Allianz Fund of Funds, BlackRock, Columbia, Davis, Dreyfus, Eaton Vance, Franklin Templeton, Gateway, Invesco, JPMorgan, MFS, Oppenheimer Capital, PIMCO, Schroeder, Turner and Van Kampen. Not all investments are available in the Income Advantage Account.

**Axa Equitable Protected Capital Strategies**

This contract from Axa Equitable, which has not come to market yet, gives its contract owners exposure to the performance of securities and commodities indices. The owners do not invest in index mutual funds, however.

Instead, contract owners invest in “Segments” with durations of one, three and five years. Each segment is invested in either the S&P 500 Price Return Index, the Russell 2000 Price Return Index, the MSCI EAFE Price Return Index, and, for IRA contracts only, the London Gold Market Fixing Ltd PM Fix Price /USD and NYMEX West Texas Intermediate Crude Oil Generic Front-Month Futures.  The equity indices do not include any dividends paid by the companies in the index.

Each Segment has a target cumulative return that Axa expects it to reach at the end of its duration. The investor’s return is capped at the target; the issuer keeps any outperformance. At the same time, each Segment offers one or more “buffers” of either -10%, -20% or -30%. The investor can only lose the amount by which the segment’s losses exceed the buffer amount by the end of its duration. Investors don’t know until they choose a segment what the cap on the cumulative return will be.

The durations of the MSCI EAFE Price Return Index, the oil index, and the gold index segments are only one year and a buffer of only -10%.  The contract also offers three variable investment options, a bond index fund, a S&P 500 index fund and a money market fund, which are not treated like the segments.

There’s a B-share version of the contract that charges an annual M&E fee of 1.25% and has a five-year surrender period with an initial charge of 5%. There’s also an ADV version for fee-based advisors that charges 80 basis points per year and has no surrender period. The contract has a $25,000 minimum. The investment management fees are incorporated in the unit value of the segments.  not specified in the available version of the prospectus filing.

The contract assets, or at least the assets in the segments, is intended to be converted to a fixed or variable annuity contract that provides income for life or life with a period certain. The unusual nature of this contract makes it difficult to determine exactly how it works, at least until it is approved and Axa can discuss it.

**ING Select Opportunities**

The payout formula in the guaranteed lifetime withdrawal benefit of ING's low-cost, limited-investment option Select Opportunities contract, introduced in March, seems to reward contract owners for buying their annuities early. The contract encourages income deferral without offering a roll-up.

For instance, three owners might all convert their assets to lifetime income at age 71. But one might receive a payout rate of 3.5%, another of 4.5% and the third of 5.5%. Owners who bought their contracts less than five years before taking income get the low rate, those who bought five to 10 years before get the middle rate, and those who bought their contracts at least 10 years before taking income got the higher rate.

A few years ago, an investor could have gotten a 5.5% payout at age 71 without any wait. So where's the upside? Liquidity (a four-year, 6% surrender period) and low costs. The current mortality & expense risk ratio is only 75 basis points, there's a Minimum Guaranteed Withdrawal Benefit fee of 100 basis points, and investment fees are just 51 to 83 basis points. (The M&E fee and the rider fee are subject to future increases.)

Advisors who fancy the idea of gaming the income guarantee with a high-growth strategy aren't likely to favor Select Opportunities. Contract owners must put at least 40% (30% temporarily) into a bond index fund or money market fund, and no more than 10% into international equities (Dow Jones Euro STOXX 50 Index or an international index fund). For the balance of their assets, there are just four Russell stock index funds and an ING stock index fund.

**Nationwide Destination DV**

This extension of Nationwide's Destination contract series offers a 10% simple roll-up during a 10-year deferral period (5% in New York) so that a contract owner could at least double his or her income base after waiting ten years for the first withdrawal. At the stipulated 5% payout rate, a 60-year-old who invested $100,000 would receive at least $10,000 a year for life starting at age 70.

The contract offers a wide range of funds from the following providers: Alliance Bernstein, American Century, BlackRock, Dreyfus, Fidelity, Franklin Templeton, Invesco, Ivy, Janus Aspen, MFS, Nationwide, Neuberger Berman, Oppenheimer, PIMCO, T. Rowe Price, Van Eyck, Wells Fargo. The lifetime income benefit option brings certain investment restrictions, however.

It's an expensive, B-share contract. There's a seven-year surrender charge period starting at 8%. The M&E fee is 1.60% and the administration charge is 0.20%. When you add a death benefit option, the living benefit (1.00% single, 1.20% joint) and fund fees of 45 to 194 basis points, fees could easily reduce the account value each year by more than 3.50%.

This contract pays out 5% of the benefit base starting at age 65, and doesn't offer 6% until age 81. The payout rate for those who begin taking income between ages 45 and 59½ is 3%. For those ages 59½ through 64, the rate is 4%.

**Jackson National LifeGuard Freedom 6 Net**

In May, Jackson National Life introduced a guaranteed lifetime income benefit rider for advisors and clients who expect tax rates and equity markets to rise. Called LifeGuard Freedom 6 Net, it allows owners of a Jackson National Perspective II variable annuity to potentially take a two-tiered withdrawal from their contract each year during the product's income phase.

The first tier of the withdrawal is the one usually associated with GMWB—a percentage of the guaranteed income base that Jackson National calls the GAWA or guaranteed annual withdrawal amount. Depending on the client's age when income begins, that would mean a withdrawal of 4% to 7% of the premium, adjusted up (for to lock in market gains) or down (for excess withdrawals).

The second tier of the withdrawal is called the Earnings-Sensitive Adjustment. It equals 40% of the net gains in the account each year, if any, but not more than two-thirds of something called the Maximum Eligible Withdrawal Amount Remaining (MEWAR), which starts out as the same as the GAWA but may change over time.

"Let's say that your contract value increases to $120,000 in the first year," she explained. "With most available withdrawal benefits a person in the highest income tax bracket would take out five percent, or $6,000, and net about $3,600 after taxes. With Freedom Net 6, you take out $10,000″—$6,000 plus the MEWAR of two-thirds of $6,000—"and net $6,000 after taxes," said Alison Reed, Jackson National's vice president, product management, variable annuities.

Under the same contract, the owner can receive a 6% roll-up in the income base for each year he delays withdrawals. If he delays 10 years, the income base is automatically at least double the original premium.

**MetLife Growth and Guaranteed Income**

Last November, Fidelity Investments has replaced its successful Fidelity Growth and Guaranteed Income variable annuity with a new contract that's similar in name, less risky to the company, a bit more expensive for investors and has a different underwriter: MetLife.

Now called MetLife Growth and Guaranteed Income, the product will be sold exclusively through Fidelity, which markets no-load mutual funds and other financial products and services directly to investors. Fidelity also sells MetLife fixed annuities and single-premium immediate annuities.

FGGI was "one of the most successful product launches Fidelity has ever had," said Joan Bloom, senior vice president at Fidelity Investments. But after the financial crisis its living benefit guarantees became too expensive for FILI, Fidelity's relatively small captive life insurer, to keep underwriting.

So far, the product has done well. Of the top 50 best-selling variable annuity contracts in the first quarter of 2010, it ranked 37th, with $197 million in sales. It was also among the top five contracts in the regional broker-dealer channel, ranking fourth.

**Hartford Life Personal Retirement Manager**

Last fall, Hartford Life launched its Personal Retirement Manager, which the Simsbury, CT insurer calls "a way to combine long-term investment growth and guaranteed lifetime income potential in a single, user-friendly, tax-deferred retirement planning vehicle."

The Personal Retirement Manager is like Neapolitan ice cream: it's three flavors in one. Contract owners can allocate their assets bucket-style among mutual funds in a variable account, a fixed return account, and a "Personal Pension Account" or PPA that's actually a deferred income annuity.

There's also a process baked into the product. It lets retirees gradually transfer money ($10,000 initial minimum) whenever appropriate from their variable and fixed accounts into the PPA—perhaps between ages 60 and 70—before turning on lifetime income.

"For years, everybody knew that if you wanted income, the SPIA was the most efficient way to deliver it," said John Diehl, CFP, senior vice president with The Hartford's Investment & Retirement Division.

"So we looked at the basic concept of the SPIA, and we looked at the reasons those products don't sell, including the fact that the advisor loses track of the assets. We thought that if we offset that, we could get a more successful product than a SPIA and a cheaper, more effective product than a GLWB."

**AXA Equitable Retirement Cornerstone Series**

Introduced last January, the Cornerstone Series is designed to give investors a way to benefit from the interest rate increases that, to many financial prognosticators, seem inevitable. And if rates do go up, it could give them a higher roll-up and higher payout rate than the five percent currently offered by competitors.

"In times of historically low interest rates, we're giving clients an opportunity to benefit from rising rates. They can let their benefit base grow by 10-year Treasury rates plus one percent or withdraw at 10-year Treasury plus one percent," said Steve Mabry, senior vice president of annuity product development. The current rate for the product, which has been rolled out through AXA Equitable career agents but not third-party distributors, is rounded to 5%, based on a 3.8% 10-year Treasury rate.

The contract contains two buckets or "sleeves." The first sleeve is a traditional variable annuity separate account with some 90 investment options, ranging from cheap index funds to aggressive actively managed growth funds.

The second sleeve is also a separate account, but its value is protected by a living benefit rider that provides a roll-up and a guaranteed lifetime income benefit. Both the roll-up and payout rates are linked to the 10-year Treasury rate. The client pays a rider fee only on the assets (or rather, on the benefit base achieved by the assets) in the second sleeve.

On each contract anniversary during the accumulation period, the guaranteed benefit base—the sum of contributions to the second sleeve minus withdrawals—automatically compounds at a rate equal to about one percent over the prevailing 10-year Treasury rate, but no less than four percent and no more than eight percent. Every three years, the value of the benefit base is also ratcheted up to the market value of the assets in the sleeve, if it's higher.

**John Hancock AnnuityNote**

In the post-crisis summer of 2009, John Hancock, the U.S. unit of Canada's Manulife Financial, launched an A-share variable annuity with a simplified lifetime income guarantee. The company hoped it would appeal to a broad swath of retirement-bound Boomers ages 55 to 75. But so far it has not gotten much traction in the marketplace. This spring, John Hancock filed a prospectus for a C-share version of AnnuityNote. The A-share AnnuityNote charges as one-time 3% front-end load. C-share contracts typically have no front-end load or surrender period but have higher ongoing M&E fees than A or B shares.