To Insurers' Relief, VA Owners Acted Inefficiently

By Editor Test *Wed, Feb 3, 2010*

Ruark Consulting's study showed that one in five owners of contracts with a guaranteed lifetime withdrawal benefit (GLWB) or guaranteed minimum income benefit (GMIB) took withdrawals between 2005 and 2009.

Issuers of variable annuity living benefit riders did not come through the financial crisis unscathed. But the pain would have been worse if hordes of contract owners had decided to begin drawing guaranteed income while their account values were depressed.

But they didn't. According to Ruark Consulting's Variable Annuity Benefit Utilization Study, only one in five owners of contracts with guaranteed lifetime withdrawal benefit (GLWB) or guaranteed minimum income benefit (GMIB) riders took withdrawals. Of those, only one in three withdrew the maximum annual amount.

Seven insurance companies furnished data to Ruark for the study, including MetLife, AXA Equitable and Pacific Life. The study was based on three million contract years of data from January 2005 to June 2009, and the study encompassed about 25% of the variable annuity living benefit market.

To the extent that these results are incorporated into insurer's assumptions about policyholder behavior and enable them to reduce estimates of risk exposure, the new data could mean that issuers can reduce their reserves for variable annuity income riders.

"If utilization went the other way, they would have to reserve more," said Peter Gourley, an actuary and vice-president of Ruark Consulting LLC in Simsbury, CT. Surrender rates for the contracts went down as the contracts became in-the-money, meaning that owners were not letting insurers off the hook for the guarantees.

As at least one observer pointed out last year, savvy VA owners and their advisors could have made the most efficient use of their living benefits by starting their income benefits while the account values were down, and perhaps even using the income to buy equities at depressed prices. Few apparently did.

The study covered partial withdrawals under variable annuity contracts containing Guaranteed Living Withdrawal Benefits (GLWB), Guaranteed Minimum Withdrawal Benefits (GMWB) and Guaranteed Minimum Income Benefits (GMIB).

Withdrawal rates for owners of guaranteed minimum withdrawal benefits (GMWBs) were somewhat higher, with one in three owners taking withdrawals. The higher rate was attributed to the fact that most GMWB contracts lack the "roll-ups" or annual bonuses, common in GLWBs, which incentivize owners not to make withdrawals for as many as 12 years.

The Ruark study also showed that, as common sense would predict, utilization rates went up with the age of the contract owner. Tax qualified policies had higher usage than non-tax qualified policies.

The U.S. insurance industry established a new standard in 2009 for establishing statutory reserves on variable annuity business. Often referred to as VA CARVM, it is a principle-based reserve calculation, requiring companies to perform financial projections that utilize assumptions believed to be appropriate.

Insurance companies also establish allocations of their capital, above and beyond reserves, to support their variable annuity business. These allocations, known as Risk Based Capital, have been on a principle-based method since 2005.

This was Ruark Consulting, LLC's first Variable Annuity Benefit Utilization Study. In combination with its Variable Annuity Mortality Study in 2007 and Surrender Study in 2008, the actuarial firm claims to have provided the first insights into variable annuity policyholder behavior.