FEATURE

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Consumers' Ability to Secure Guaranteed Lifetime Income Impacted by DOL Rule

The Department of Labor (DOL) fiduciary rule has the potential to impact retirees' and pre-retirees' ability to obtain guaranteed lifetime income from annuities. This consequence is unfortunate because it comes at a time when increasingly more retirees must find ways to create their own sources of guaranteed lifetime income in retirement. Under the current form of the DOL fiduciary rule, which goes into effect July 1, 2019, there are additional requirements needed for advisors and their firms to service retirement accounts that include rollovers and IRAs. Since these new standards may be prohibitively arduous, they will likely result in a significant decline in the sales of annuity products that provide owners with much needed guaranteed lifetime income.

How Much Is at Stake?

LIMRA Secure Retirement Institute estimates $91 billion of annual variable and indexed annuity sales will be subjected to Best Interest Contract Exception (BICE) constraints under the new DOL fiduciary rule (Figure 1).

More than half of the variable annuity (VA) sales and nearly two thirds of fixed indexed annuity (FIA) sales in 2016 were funded through IRAs or rollovers from retirement accounts. Advisors will be required to use the BICE process to exempt these sales from the status of "prohibited transactions." The difficult compliance process, along with increased litigation risks with the BICE provisions, will provoke some advisors and their firms to avoid VAs and FIAs, possibly even with clients' nonqualified assets. Three in 10 banks and credit unions

Figure 1

U.S. Individual Annuity Sales in 2016 by Market Type (in billions)

Source: LIMRA Secure Retirement Institute, 2017. Structured settlement sales are not included.

say they will drop some guaranteed income products, like VA with guaranteed riders, in response to the DOL fiduciary rule.

Who Will Lose? Pre-Retirees and Retirees

Another consequence of the new DOL fiduciary rule could result in depriving retirees and pre-retirees of guaranteed lifetime income sources from these VAs and FIAs.

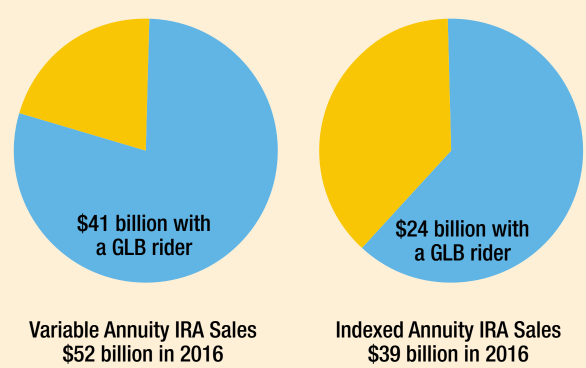
$65 billion of the $91 billion at risk due to the BICE restrictions comes from VAs and FIAs with a guaranteed lifetime withdrawal or income benefit (GLB) riders (Figure 2). These GLB riders enable consumers at or near retirement to create a guaranteed income stream when they need it while retaining the flexibility to manage their investments. Given the growing need for individuals to generate some of their own retirement income, many use some of their retirement plan and IRA savings to buy annuities with guaranteed living benefit riders so they can generate guaranteed income.

These VA and FIA buyers are predominantly pre-retirees and retirees, at or near the cusp of retirement. Research from Secure Retirement Institute *Annuity Buyer Metrics* shows the average age of a buyer of a VA or FIA with a guaranteed living benefit elected is 62, and 6 out of 10 buyers are between ages 50 and 65. Many of these buyers are from mass-affluent and affluent wealth segments (between $100k to less than $1 million in investable assets) and are putting on average $148,000 into VA contracts with a living benefit and $116,000 into FIA contracts with a living benefit.

Figure 2

Variable and Indexed Annuity Sales in IRAs/Rollovers in 2016 With a GLB Rider

$65 billion with a GLB rider out of $91 billion



Source: LIMRA Secure Retirement Institute, 2017.

These consumers buy annuities to create a guaranteed income stream that will supplement their income from Social Security benefits in their retirement years.

Disruption of access or fewer choices under the BICE restraints, particularly in variable or indexed annuity sales with a guaranteed income or withdrawal riders, will certainly mean shrinking ability for generating guaranteed income for many mass-affluent retirees and pre-retirees. Should these annuity sales falter under the effects of the new rule, the purported objective of the DOL rule to foster retirement security for Americans could be seriously impeded.

Implementation — A Lot of Stress on Specific Distribution Channels

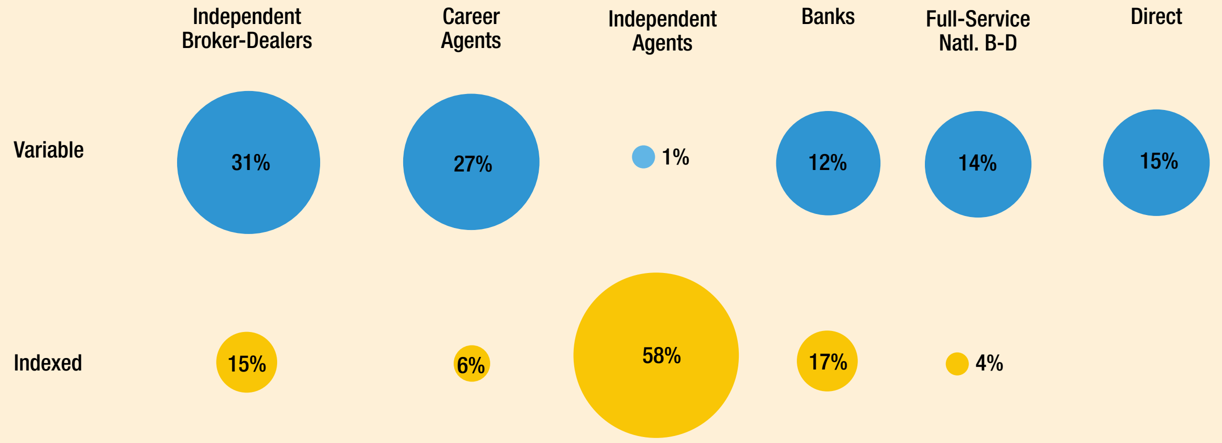
Historically, VA and FIA sales have skewed towards a few specific distribution channels (Figure 3). For example, almost 60 percent of VA sales in 2016 were primarily distributed by third-party channels like independent broker-dealers, full service national broker-dealers, and banks. On the other hand, around 60 percent of FIA sales were sold through the independent agent channel, which typically caters to mass-affluent clients.

In the event these key channels experience a decline in sales, it could negatively impact the availability of these products to the pre-retirees and retirees they serve. Also, many annuity manufacturers tend to have most of their successes within one or two particular annuity product types. The implementation of new policies and procedures needed to comply with the DOL fiduciary rule will put a lot of stress on a few specific distribution channels and/or manufacturers, which may limit the availability of these guaranteed income riders.

Since the new administration entered Washington in January 2017, uncertainty has surrounded the DOL fiduciary rule. While the industry entered the initial phase of implementation on June 9, the target date for full implementation — initially slated for January 1, 2018 — has been pushed back to July 1, 2019, creating even more uncertainty. The industry is still guessing as to what the final implementation will look like. This uncertainty has made it difficult for annuity manufacturers and distributors to focus on guaranteed lifetime income solutions for the future.

Figure 3

Variable and Indexed Annuity Sales in 2016 by Share of Distribution Channels



Source: LIMRA Secure Retirement Institute, 2017.

Annuity Sales — Already Feeling the Impact

The costs to comply with the DOL fiduciary rule will be substantial, and they may likely result in advisors/firms discontinuing the use of annuity GLB riders to generate guaranteed income in a post-DOL fiduciary rule world. In fact, the industry is already seeing an impact on annuity sales. For example, variable annuity sales dropped over 20 percent in 2016. LIMRA estimates it could drop another 10 percent in 2017. In addition, FIA sales are likely to decline slightly in 2017, reversing their upward trend over the last nine years.

Even if the DOL fiduciary rule sees a significant revision or a delay in implementation, many of the new policies and processes will remain; and the anticipated delay of this regulation through July 2019 will extend the period of uncertainty. Despite it delaying the fiduciary rule will positively impact sales for both variable and indexed annuities for the time being.

Looking Ahead

The DOL fiduciary rule will change the retirement market. It will have a profound impact on stakeholders in the annuity market — including annuity manufacturers, distributors, advisors, and even consumers — in terms of how and when they receive retirement information. This impact could result in less access and fewer choices for retirees and pre-retirees and set back their retirement security. The annuity manufacturers and distribution firms will need to work together closely to make sure retirement planning solutions for pre-retirees and retirees continue to include annuities and, further, that BICE constraints do not constrict the value of annuities in retirement. Equally important, there will be an increasing need for tools and services to support the annuity sales process and to help financial professionals assess the suitability of retirement solutions like annuities in their clients' retirement income planning.

Todd Giesing joined LIMRA in 2013 with an extensive background in individual annuity products. As Director of LIMRA's Secure Retirement Institute annuity research, Giesing is responsible for annuity and retirement income-related projects such as the U.S. Individual Annuity Yearbook, Annuity Buyer Metrics, and oversees LIMRA's annuity benchmarking reports.

Prior to joining LIMRA's Secure Retirement Institute, Giesing was an annuity wholesaler at MetLife, and a licensed personal banker at Wachovia Bank. Giesing earned a bachelor's degree in Accounting from Eastern Connecticut State University. He can be reached at 860-285-7899 or tgiesing@limra.com.

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