



ABS Annuity Alert Imperialism, the NASD, and Fixed Indexed Annuities

NAFA (National association of Fixed Annuities), of which American Brokerage Services Inc. is a member, is doing a terrific job of providing clear, distinct information regarding the clash of the NASD (National Association of Security Dealers), and the insurance industry, over fixed indexed annuities.

ABS believes in putting information in writing, and has been doing so for the past 10 years, functioning as both a consulting firm and as a national distributor of annuities. We pride ourselves on providing you clear, distinct information on products and marketing material. .

I have stated in past articles of “The ABS Annuity Alert”, that FIAs are simply an evolutionary financial product. Anyone who is honest with themselves can see that FIAs fall uniquely towards the center of the ‘Spectrum of Risk and Return”.

If an advisor/agent is to help in securing a retirement plan, how can they not discuss fixed-indexed annuities as a possible product within the portfolio? The client certainly does not have to reposition assets into a fixed-indexed annuity, but the product should, at least, be brought up as a possible solution. If fixed-indexed annuities are not included in the planning discussion, one could conclude that such omission could cause a client to choose a product which may not be suitable, with regard to their risk tolerance and time horizon.

Let’s say you are a securities licensed advisor, and in 1999 you suggested, and the client agreed, that 100% of their investment portfolio be well diversified in the stock of companies that make up the NASDAQ, Dow Jones, S&P 500, Mid Cap 400, small caps etc... Your client by the way, was 65 years old, and for the sake of discussion, you did not include FIAs in your repertoire of financial offerings. You did not include FIAs in your client meeting either because you did not know about FIA’s or your broker dealer forbid you from marketing such products to your clients. In 2000, we all know what happened to the value of even well diversified stock portfolios.

In October 2001, ABS wrote in “Annuities Coast to Coast”, ‘The S&P 500 is sitting at approximately 1000. Don’t wait!!! There may never be a better time to show your clients the brilliance of Equity-indexed Annuities!’”

“The performance of the equity markets over the last few years clearly points to the growing need for the equity-indexed annuities. Looking back, who would not like to have locked-in their gains when the S&P 500 hit its high of 1527? Only equity-indexed annuities could have done this for your clients! If you are not comfortable with equity-indexed annuities – you should get acclimated with these products as soon as possible!”

“As your clients approach retirement, less and less of their assets belong in market sensitive investments such as mutual funds, variable annuities, variable life, and individual stocks. More and more of their assets should be in fixed products that provide moderate growth and safety of principle. A diverse portfolio of stocks and mutual funds was not enough to protect the majority of seniors over the last few years. Guess what would have not only protected them from losses and locked-in their gains, but would have also put them in a position to take advantage of the market’s downturn? Equity-indexed annuities! We can show you how to capture your client’s attention, get them excited, and motivate them to place their money and their trust with you. We do this with a very simple presentation that we would be glad to share with you. Equity-indexed annuities will allow both you and your client to sleep peacefully, participating in market gains but not in market losses.”

“Further, broker dealers and agents who refuse to acknowledge the merits of these products, and refuse to present equity-indexed annuities to clients, and continue to present only variable annuities, stocks and mutual funds, bear not only responsibility but perhaps liability. The question of suitability is one being raised by clients and attorneys everywhere. Agents are often forbidden by their career companies, or their broker dealers, from marketing equity-indexed annuities. This practice is wrong. We would all agree that the client’s welfare is more important than keeping all of your business with your career company or with your broker dealer. Remember that you do not need a securities license to write equity-indexed annuities, thus you do not need to place this business through your broker dealer. If you would like to begin presenting equity-indexed annuities to your clients, please call us today at 1-888-227-3131, x-500.”

The excerpt you just read was from October 2001. Here we are in May 2006, and the NASD has zero jurisdiction over the sale of FIAs, by its own admission, as stated in a hearing held March 29th, on the subject of investment fraud targeting the elderly. The NASD is a self regulatory body, normally concerned with taking action against broker dealers, who, in the opinion of the NASD, sell unsuitable variable annuities. Now, under the guise of protecting seniors, the NASD is conducting a series of “sweep exams”, to investigate brokers who recommend that clients exchange their variable annuities, mutual funds, or stock portfolios, for FIAs. This is clearly a new vein of thought for the NASD. “This is an evolution in our position”, according to James S. Shores, executive vice president for enforcement. Think about it. The NASD is normally concerned with unsuitable recommendations to buy securities, but now the NASD is concerned with unsuitable recommendations to exchange market sensitive, risk oriented products, into more risk adverse products, -FIAs, to seniors! Do they possess a crystal ball? Can the NASD see for certain, that millions of seniors will not fall prey to market fluctuation, gyrations, or upcoming bear markets? Can they all of a sudden guarantee that seniors will not potentially lose their retirement savings?

Is the answer from the NASD products with guaranteed withdrawal benefits, or living benefit guarantees? I hope not, because such riders may be acceptable for some folks, but in my opinion, such riders are costly, and still full of risk, with poor internal rates of return, which you are forced to take over time. In my experience, many security advisors have failed to truly examine these riders. Such riders provide a real rate of return to be approximately 3.69% for a living benefit guarantee over a 25 year period, assuming a hypothetical 7% constant market return, 10 years of accumulation, with a 15 year period certain payout, as a minimum 10 year payout is required. In another example, with the same 7% constant market return, I site a guarantee withdrawal benefit of 5%, producing a rate of return, of approximately 2.14% over a total of 30 years. In this hypothetical scenario, a male age 59 takes 20 years of a 5% withdrawal, and then annuitizes at age 79 over life with 10 years period certain, with an assumption the gentleman passes away at age 89.

Wow! That was a lot of information. An agent recommends a flight to safety due to obvious risk tolerance and time constraints, via the transfer of retirement savings out of the share markets where the value of such savings is subject to the ups and downs of the stock market, into an evolutionary financial product, providing the protection element seniors are gravitating towards. This evolutionary financial product, the FIA, provides the client with safety of principal, with interest gains that are locked-in annually and guaranteed never to go down, a guaranteed income stream which the client cannot outlive, -providing protection with upside potential!

Isn’t this idea ridiculous? Again, the NASD is normally concerned with unsuitable recommendations to buy securities, but now the NASD is concerned with unsuitable recommendations to exchange market sensitive, risk oriented products, into more risk adverse products, -FIAs, to seniors! Perhaps ridiculous is not the right word, never the less, transferring savings, exchanging financial products, to avoid risk, was a decision the client made. How can such a recommendation be unsuitable, if given the choices at 65 years of age, with current risk tolerance and time constraints, (regardless of past risk tolerance), be unsuitable! Who is this unsuitable for? The coffers of the Broker Dealer who have no jurisdiction over such products? Agents/advisors meet with prospects and clients, discuss individual needs, preferences, and circumstances, financial products and choices are discussed, recommendations are made, disclosures are made, and the client makes a decision. It’s not complicated. It’s about losing commission dollars. It’s about Imperialism on the part of the NASD, and particular broker dealers!

What appears complicated are the challenging jurisdictional constraints facing the NASD, in attempting to supervise or govern the sale of FIAs, when the NASD has no authority to do so. The SEC has twice been asked by the NASD to consider making the FIA a security and has not done so. The NASD has recently asked the SEC again, for the third time in less than 10 years, to label FIAs as a security product. Based on information made available to me, they have again said the FIA is not a security.

Times change, my advice to the NASD is to accept the fact that consumers like apples, oranges, bananas, pears, pineapples, cherries and so on. It used to be that stocks and bonds were all we had to choose from. Today we have mutual funds, variable annuities, hedge funds, and exchange traded funds, and ...Fixed Indexed Annuities. Consumers buy Fixed Indexed-Annuities when they are given the opportunity, when they are given the choice. Consumers choose FIAs when agents/advisors include these products in their "portfolio of retirement savings products".

The NASD must simply come to terms with the fact that you cannot stop evolution. People buy products, and they invest, based upon how they feel about the economy, and the information and knowledge they possess. In 1998, 1999, 2000, consumers felt great about the economy, the market. They did not know about fixed-indexed annuities at that time, but even if they did, they were so giddy about the market, they would have chosen market sensitive products! Seniors bought lots of product directly linked to the stock market, because they felt good about the market and the economy. Times have changed. People don't feel the same way about the stock market today as they did in 2000. They feel contrived; they just don't know what the market holds for them, and they have time constraints, and they don't want to lose their money. Today they have an advantage, they know about a product with both safety and potential, and they choose this product over market sensitive products everyday. We all learn from our past mistakes. Thanks to agents/advisors, more consumers are introduced to fixed-indexed annuities everyday.

The NASD is, of course, free to pursue supervision of FIAs. But the solid agents/advisors and the insurance industry are not going to just stand there and give up a product which is so revolutionary. The insurance industry is proactive, and is not going to allow the NASD to govern FIAs, an insurance product.

The truth is, the NASD and the insurance industry have different perspectives. In my opinion, what the NASD should realize, is that as we grow closer to retirement, there is a natural bias towards savings products; where the client has safety of principal, where interest gains are locked-in annually and account values are guaranteed never to go down, plus a guaranteed income stream which the client cannot outlive, - providing protection with upside potential! The worst case scenario for the consumer is a 0% return, when the market experiences a down year. (The 3rd time in this article I have said this.) The upside potential is that each year the fixed-indexed annuity resets, and in a down year it resets at the new, lower index value, whereby the clients has the opportunity to ride the market back up in its recovery, and lock-in the gain annually. It almost sounds too good to be true, but it's not, it's a fixed-indexed annuity, and that's how it works!

Back when we had only horses, we rode horses, or walked. When we had horses, or cars, we could ride horses, drive cars, or walk. Some people rode horses, some people drove cars, some people still choose to walk. Now we have stocks, bonds, mutual funds, variable annuities, exchange traded funds, hedge funds and more, and FIAs. Some people choose mutual funds, some people choose FIAs. There has always been enough room for both the securities industry and the insurance industry, they are different, and their products are different. The fixed-indexed annuity is simply evolutionary. Unfortunately for some, it is an insurance product. That's the way I see it. The NASD and its members can still do a lot of good for the consumer, and everyone can continue to make a well deserved, fine living.

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