SEC Ruling on Annuities – Right or Wrong?

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A recent (June 25, 08) announcement by the US Securities and Exchange Commission (SEC) suggests that additional regulations are needed to protect the public from abuses in sales of Equity Indexed Annuities and Life Insurance. The National Association of Insurance and Financial Advisors of Iowa (NAIFA – IA) strongly believes the SEC has it wrong. The SEC has reviewed these products before and had chosen not to impose additional regulations for the last 10 years. The primary reason for this delay is that these products are not equities (Securities); they are fixed guaranteed accounts that provide for interest rates calculated at the end of the year (or index period) rather than stating the interest rate at the beginning of the year (or rate period) as with traditional fixed rate annuities. They are Fixed Indexed Products.

The premise is that the public has trouble understanding that a fixed product can have a variable interest rate. Fixed Indexed Annuities have a guaranteed minimum interest rate, usually lower than a fixed rate annuity, but offers a higher rate when the index used to calculate the rate shows a gain. When the index does not show a gain, the Fixed Indexed Product retains its accumulated value. The appeal to investors is that they can realize some of the gains of the market with out incurring the losses of the market.

The Des Moines Register included articles relating to this issue recently. These articles seem to focus on questionable sales tactics, fees, and commissions. As a provider of Continuing Education for insurance agents in Iowa for the last 20 years for NAIFA IA (National Association of Insurance and Financial Advisors – Iowa), we have provided training on Indexed Products for Iowa agents. During 2007 all Iowa licensed agents that want to offer any indexed product must have completed four hours of indexed product training prior to making that offer to a prospective customer. That training was specifically designated by the Iowa Insurance department (Susan Voss Commissioner) to include valid explanations of how indexed products work and how to present them to the public in a manner that consumers can understand. Iowa has already and adequately addressed the indexed product sales tactics questions with the 2007 requirements. The amount of commissions and fees issue brings up many points to consider including the simple fact that additional regulations require additional expenses to conform to the regulations and to pay regulators for the required regulation.

The securities industry is regulated by the SEC and FINRA (Financial Industry Regulatory Authority). These agencies are charged with the regulation of securities offered to the public and the sales representatives that offer them. The claim that a Fixed Indexed Product has the same characteristics of a Security and understood by the public as a Security is a significant leap even for a Federal Agency. The success of these indexed products in the consumer market place and the advisors sales practices appear to be the driving force behind this recent development. Every security transaction includes a transaction fee paid for the regulation of those transactions. Additional regulation of Indexed Products will increase the expenses related to those products just as it has with securities.

Additional regulation generally translates into more disclosures to clients and more restrictions on agents. Fixed Indexed Products already have multiple disclosures about the technicalities of the account and the strategies available. Clients must sign these disclosures at the time of purchase. Insurance licensed agents (with Iowa's Indexed Product Training) currently can offer Indexed products to the public. Under the SEC proposed rule only securities licensed representatives would be allowed to offer these products. The benefits to the public are more than questionable in relationship to the restriction on product availability due to fewer agents allowed to offer them, additional costs for the product, and duplicated requirements for disclosures.

Consumers must be concerned about the value of any product that is being considered for investment. Annuities and life insurance are long term investments and should be considered with reference to the investment period (number of years of surrender charges). The success of indexed products with the public is an indication that these products offer a unique combination of security and returns that are not available with any other product in the market place. Any investment should be made after consultation with a professional insurance agent, securities representative, or investment advisor representative that is a member of NAIFA.