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Let’s Put the Annuity Back in Annuity

By Robert W. MacDonald

Not too many years ago the annuity segment of the financial services industry was considered to be even more boring that an Al Gore speech. Because the annuity was simple, stable, safe and provided a steady stream of income that the recipient could not outlive, it was deemed appropriate only for “widows and orphans.”

As the more traditional insurance and banking products became less appealing to the consumer and more difficult to sell, annuities began to be seen as an alternative product. Factor in the professional tax avoiders and fast buck Freddies who soon discovered the product and suddenly the annuity world was turned upside down.

Almost overnight, a product intended to encourage the safe accumulation of capital on a tax-deferred basis for later payout as income became the cure-all for virtually any financial need.

Before long there were more forms of annuity products than promises in an election year. Offerings consisted of fixed, variable, indexed and split annuities. Annuities could be like life insurance or even long term care. Some annuities were even used as “wrappers.” (For wrapping what I don’t know!) What a magic product the annuity became!

As options increased for using the product to solve financial needs (real or perceived), so, too, did the complexity, confusion and misuse of the product. In direct proportion to the skyrocketing increase in sales, more players wanted a piece of the action. And to capture their fair share, market congestion soon forced players to attach more bells and whistles than on a motorcycle in a Shriner’s parade.

But it worked.

Annuities soon became the hottest and best selling product of the life insurance industry, which may not be saying much. But when the banks jumped into the fray, then you knew this was easy money lying on the table. Companies that once counted annuity sales (if they were counted at all) in the millions now sold billions. Bankers who neither had the inclination or talent to sell insurance products soon became the leading marketer of the product. (That should scare any reasonable person right there.)

All of this is good. Annuities — fixed and variable — are in concept, great products. They provide financial security, capital preservation, tax favored accumulation and myriads of options to receive benefits.

There is only one little problem.

In all the giddiness to jump in on this lucrative market, the companies and marketers have lost sight of the basic value and benefit of the annuity product, which is quite attractive. In an effort to go "one up" on the competition, the companies have gone "one down" on the consumer.

What the product does best has been smothered by complicated, confusing, expensive and (sometimes) unnecessary options. The product has been turned inside out in order to provide upside for sales. What was designed for the long term is marketed for the short term. With stability as a benefit, volatility is sold as a value. A product with simple low costs now has fees more complicated than the tax code, and once renowned for providing an income when it is needed most, for as long as it is needed, is now sold as quick gains and a quick rollover.

There is a twisting irony in this situation. A product once considered best for widows and orphans may now be considered unsuitable for them.

Things have reached the point that insurance companies and banks should be concerned that some fee-sniffing lawyer or publicity-hunting, governor's-mansion-seeking prosecutor, may just start asking questions about what has happened to this boring old product. But, all is not lost. Yet! As they sang in that old anti-war movie — "There's still time, brother…"

Annuities are great products. Not enough of them are sold. But, they should be designed, marketed and managed they way they were intended. The market is established. Now products need to establish themselves as fit for the market. The industry needs to stop trying to hype the annuity product into a sexy something it is not intended to be and start selling it for its value, which is pretty sexy.

The industry — not to mention the consumer — will be better off and better served if it goes back to the basics of the annuity product. That is a long term, secure financial product designed to encourage the accumulation of capital on a tax-deferred basis for later payout, as income then cannot be outlived.

One does not need games and gimmicks to make that type of product attractive to the consumer. The annuity market's potential has just been scratched. It could be the growth market of this century. But the race to suck out all the oxygen in the market for the short term may just snuff out its future.

The true rules for the annuity market are simple — sell value, be basic, be good, be successful.

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