How to Maximize Safety In Fixed Annuities

By Danny Fisher

HOW DO YOU MAXIMIZE THE safety of your client's money in fixed annuities? There are a number of ways. Here a few ideas:

To only offer highly rated companies is a quick and easy first response. However, the highest rated companies normally pay lower interest rates than can be found with companies rated B to A-.

Clients want and search for higher rates. And, in today's open information age, rates are posted on hundreds of thousands of Web sites, in bank lobbies, and newspaper advertising. That makes it easy to find out which companies pay the highest rates.

Therefore, agents are often faced with the dilemma, "If I don't sell the higher rate with a B++ company, my clients will find an agent who will sell it to them."

There is another problem, too. Just because the company was rated A+ when the annuity was sold, that doesn't mean the company will keep the high rating. Remember Executive Life, Fidelity Bankers Life, First Capital Life, and others who quickly fell from grace? What happened to those companies will continue to be discussed for years, but the end result was the same: The companies were placed in liquidation.

But, due to state guaranty laws, the vast majority of those policyowner funds were protected.

This means that there are ways to maximize safety under the guaranty laws. Basically stated, fixed annuity values are protected up to $100,000 per owner designation, per company. As I understand current laws, the amount is greater in 6 states and less in 4 states. Here is what I do in Texas: If a client has $300,000 and wants to make certain all the money is protected, including future interest earnings, while taking advantage of the highest rate possible, we set up 3 contracts in Company A for $80,000 each.

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In annuity 1, the husband is the Owner and Annuitant. In annuity 2, the wife is the Owner and Annuitant. In annuity 3, the husband and wife are Joint Owners with the husband as the Annuitant. Then, we'll put $60,000 in the next highest rate we can find in Company B, normally with the husband as Owner and Annuitant. That way, as the money grows, it will be protected under the guaranty laws because they are covered up to $100,000 per owner designation, per company.

"I didn't think we could tell clients about the guaranty laws," is a comment I often hear from agents. That's only a partially true statement. An agent cannot advertise or hold the guaranty laws out as an inducement to get someone to purchase a policy of insurance, but if a client asks you about the law, you have a fiduciary responsibility to explain the law to that person.

> Spread the money around in different companies and use different owner designations

In the example above, there was no mention of the guaranty law to the client. I just set the annuities up that way, explaining to the clients that the arrangement will maximize safety and flexibility. If they ask questions, I answer them directly.

What happens if a client comes back later and says, "I have more money and want to put it in annuities." Then, I recommend we put more in Company B and some in Companies C, D, E, etc. Again, the purpose for spreading the money around is to increase flexibility, ladder interest rates, and maximize safety.

If a client already has more than $100,000 in an annuity, most companies will allow the annuity to be split up and reissued as 2 or 3 separate contracts. Once the split is complete, ownership of the contracts can be transferred to a spouse or a spouse can be added as a joint owner without tax consequences.

If the policyowner is not married, it becomes a little more complicated, but steps can be taken to maximize safety.

Occasionally, a client will max out the guaranty law in Company A and still want to put more money in Company A. Then I try to make certain the person understands the limits of their protection under the law. I further explain that historically all funds over the limit don't just vanish into thin air. If the company is placed in liquidation, it can be reasonably expected that there will be some amount paid over the limit.

For example, in the recent liquidation of London Pacific Life, policyowners in Texas received about 91% of the adjusted value over $100,000.

The two main reasons why people want to exceed the guaranty law coverage with a particular company are: 1) the company offers a higher rate than can be found elsewhere, and 2) the client has experienced vastly superior and friendlier service with that company. A frequent comment I hear is, "A live person actually answered the phone!"

While writing this article, a client called and said, "Last night, the boys at the VFW were talking and they all said annuities weren't safe. What do you have to say about that?"

I explained the guaranty law to him in what I thought was an eloquent, professional manner. His comment was, "Well, if there is such a law, why haven't we heard about it before?" I continued to explain, in Texas, a copy of the law is included in every policy delivered and the Texas Department of Insurance, along with the Texas Legislature believes that is enough notification.

That conversation brings up some things that have frustrated me for a long time. I believe that financial advisors should be able to tell clients about how their money is protected. I believe the guaranty laws should be the same in all states. Also, since $100,000 just isn't as much as it used to be, I believe the amount of protection needs to be increased.

Until those things happen, about the same time as hell freezes over, spread the money around in different companies and use different owner designations to maximize the safety of your client's money in fixed annuities. NU