life annuity specialist

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Jackson, Lincoln, Transamerica Target RIAs With ETF-based VAs

By Warren S. Hersch November 1, 2017

Michael Kazanjian, VP of marketing at Lincoln Financial Group.

With the **Department of Labor**'s fiduciary rule set to fully take effect July 1, 2019, life-annuity carriers are scrambling to develop products that align with streamlined requirements for level-fee advisors. To that end, many among them — **Jackson National**, **Lincoln Financial**, **Transamerica** and others — have incorporated exchange-traded-funds into the subaccounts of fee-based variable annuities.

The reason: passively managed ETFs that follow a securities index, such as the S&P 500, can be bought at low cost to the consumer — a top priority for fee-based financial service professionals looking to keep VA fees to a minimum. Hence the industry's heightened focus on tailoring products to fee-based registered investments advisors, which carriers are counting on to help sustain annuity sales under post-DOL regime. And in the current market, ETF-based iShares from **BlackRock** are in especially high demand.

A Growing Distribution Channel

"For the last 5 to 6 years, the RIA space has represented the fastest-growing segment of the advisor population," says **Michael Kazanjian**, VP of marketing at Lincoln Financial Group. "To enter the RIA market in a significant way, we had to reduce fees and increase product transparency. ETF-based iShares from BlackRock were a perfect fit."

"The advantage of utilizing ETFs is that they are a cost-effective way of obtaining index exposure," adds **Brian Sward**, a senior VP of product and investment management at Jackson National. "The utilization of ETFs in the industry continues to increase, and Blackrock iShares offer the most diverse line-up, providing the most flexibility and broadest exposure."

According to **Morningstar**, 22 VA contracts were created in 2017 that carry iShares, up from 10 in 2016 and the highest number recorded since Morningstar began tracking the space in 2008. Carriers that offer VAs with iShares, Morningstar data shows, include, in addition to the aforementioned insurers, **Allianz Life**, **AIG**, **AXA**, **Forethought Life**, **Great-West**, **Nationwide**, **RiverSource Life** and **Symetra Financial**.

In most of the variable annuities, the iShares are a component of a larger investment portfolio offered by the carrier. That's true, for example, of three variable annuities that Transamerica launched in 2016: TA BlackRock Equity Smart Beta 100, TA BlackRock Smart Beta 75 and TA BlackRock Smart Beta 50. The products' three investment options carry different weightings of BlackRock's iShares Smart Beta ETFs.

iShares are a component, too, of the tactically managed ETF/index allocations portfolios available in Jackson National's variable annuities, including Elite Access Advisory and Perspective Advisory family of products. Funds flowing into these offerings are on the upswing: Since the launch of the ETF allocation portfolios in February 2012, assets under management have attained (as of Oct. 23) $624 million.

Brian Sward, a senior VP of product and investment management at Jackson.

Sward credits the increase in part to the strength of the partnership with BlackRock. "BlackRock continues to be one of Jackson's best partners and is able to provide a lot of distribution support to our advisors," he says.

Going all-in with iShares

That distribution support, combined with the advantages of the ETFs, were factors in Lincoln Financial's decision to develop a variable annuity based exclusively on iShares — reportedly an industry first. Unveiled in February 2017, the ETF-only product, Lincoln Core Income, boasts no surrender charge and AUM fees between 28 and 30 basis points. The product also provides a return of investment death benefit; and a guaranteed lifetime income equaling 4% of the initial deposit, the payout rising annually by 2% to keep pace with cost of living increases.

Eric Bass, an equity research analyst for life insurance at **Autonomous Research**, touts the ETF-only investment line-up and low fees as distinguishing features of Core Income, noting (in respect to the fee) that the average Morningstar VA subaccount fee rate is 76 basis points.

"There's a market for cheaper VAs that include only ETFs or index funds, given that one of the biggest historical objections to the product has been its high cost," says Bass. "[But] the jury is still out as to whether advisors will push fee-based annuities without the incentive of an upfront commission."

Also, setting the product apart, says Lincoln's Kazanjian, is its simplicity — another plus for discriminating RIAs. Except for the three iShare ETF options, clients need not decide among features and benefits; all are built into the annuity.

"As opposed to creating a product that has tons of different features and options, we opted to limit the number of choices to make the offering familiar but surprising," he says. "So, for example, we provided for the initial 4% payout and annual 2% annual enhancement to income — the familiar parts. The surprising part lay in a lost-cost VA chassis that offers tax-deferred growth and income for life."

With the release of Core Income, Lincoln is banking that it can capture a fast-burgeoning sector for passive investing through low-cost ETFs. According to the February 2017 report of Morningstar Direct, the retail market for passive ETFs rocketed to $2.53 trillion at the close of 2016, up from $228 billion in 2004. The company is gambling, too, that it can rope in a growing number of RIAs aiming to offer ETF-oriented clients guaranteed income and tax-advantaged investing in a variable annuity wrapper.

A new report from **Cerulli Associates**, U.S. RIA Marketplace 2017, reveals that assets managed by RIAs are increasing, most especially among the nearly 690 retail-focused advisory firms that have more than $1 billion in assets under management and that collectively garner 60% of asset market share. The report notes also that 53% of RIAs use ETFs for both “core and satellite holdings.”

The Hurdles Ahead

Kazanjian says that Core Income has “opened doors” for Lincoln in the RIA space. But he acknowledges the challenge of penetrating a market that historically shied away from annuities because of the products' perceived disadvantages, including still predominant comission-based compensation that doesn't lend itself to the RIA business model.

Conversely, many commission-based distributors, such as banks, broker-dealers and wirehouses, have yet to adopt fee-based platforms. As a result, sales of Core Income, though growing, remain small relative to Lincoln’s overall VA sales, says Kazanjian.

Deep Banerjee, a director at **S&P Global Insurance Ratings**, echoes the point, noting that the market for ETF-based variable annuities — from Lincoln, Jackson, Transamerica and other carriers angling for a share of the pie — is still in an emerging space.

“[The product] is part of a longer-term strategy for insurers that are selling it or are developing it today,” he says. “We wouldn’t expect this to be the leading VA product at this time. But if the DOL fiduciary rule remains unchanged and gets fully implemented, we would expect an increased interest in the product.”