Big Changes Ahead: Index Product Trends for 2015

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It isn't often that we see major changes in the index product landscape. Since fixed index annuities were introduced in the mid¬1990s, perhaps the only major change we have seen was the introduction of income riders – also known as guaranteed withdrawal benefit riders – in the mid-2000s. Index universal life insurance products have only incrementally changed since they were first introduced in the late 1990s.

But in 2015, we should see several major changes. They are:

- The culmination of a change in the fixed index index annuity marketplace brought on by completive forces.
- The continuation of an evolution in both markets brought on by changing customer needs.

Fixed Index Annuities Offer New Indices

Since the beginning of the fixed index annuity in the mid¬1990s, carriers have overwhelmingly based their interest crediting upon the S&P 500 Index. In the fourth quarter of 2012, more than 80 percent of fixed index annuity sales occurred in either the S&P 500 Index or a fixed non¬index account, according to Wink's Sales & Market Report. But now, that is changing.

The change started in 2012 when one company launched an annuity using a new index whose features were unusual at the time. After this annuity was successful, competitors took notice and soon followed with their own new indices. Now that the trend is firmly established, if your favorite annuity carrier hasn't already introduced a new index, it wouldn't be surprising if it is considering offering a proprietary index at some point in 2015.

These new indices have three unusual features:

1. They don't reference the S&P 500 Index, but instead reference multiple asset classes linked to lesser known indices, or indices that are designed or selected by the insurer.
2. They have different investment strategies. Some of these strategies include a volatility control feature that is designed to increase exposure to risk assets when volatility is low and decrease exposure to risk assets when volatility is high.
3. 3. They may offer the performance of the index without imposing an annual cap. However, they usually do impose participation rates, spreads or mandatory allocation

limits. So although the index strategy may be “uncapped,” it still limits the amount of performance that is credited as interest.

Use of these unusual new indices is not without its challenges. The index to which the strategy is linked may be less well known or may be created by the company. In these instances, it may be difficult to be able to validate their performance via publicly available materials. Indices that are created around specific strategies may not perform in the same manner as more commonly understood indices such as the S&P 500 Index, so your clients may have a harder time understanding how the interest credits are determined. Additionally, regulators have begun to publish warnings, specifically about advertising that is likely to contribute to inflated consumer expectations of an annuity product’s performance.

Regulators Focus on IUL Illustrations

Closer regulatory oversight on illustrations is another trend is expected to affect another index product, universal life.

Index universal life products are not explicitly referenced in the National Association of Insurance Commissioners (NAIC) Life Insurance Illustrations Model Regulation, so the American Council of Life Insurers (ACLI) had been working to achieve industry consensus and provide guidance to the NAIC as to how the model regulation should be updated so that index universal life illustrations are standardized across the industry.

There are two competing views, one that was recommended to the NAIC by the ACLI, and another that was submitted to the NAIC by a group consisting of several insurers that do not offer index universal life. The NAIC has said that it will consider both proposals and state regulators have started asking questions to insurers about their presentations of potential gains to prospective buyers in illustrations.

At this point, we don’t know which approach to standardizing these illustrations may be adopted. If the NAIC adopts the ACLI’s proposal, product designs will likely remain unchanged. If, on the other hand, the NAIC adopts the competing proposal, then it will likely become less important for carriers to offer high index caps and it will become more important for carriers to offer low cost of insurance charges.

It is possible that either development could result in a continued growth in popularity of index universal life as it could increase agent and consumer awareness of the product.

– Chris Conklin

Long¬Term Care Features Proliferate in Index Products

The future is bright for combining features across different product types. The need for long¬term care coverage has been growing as our population ages and, as a result, we have seen more and more carriers offering LTC¬related features in their life insurance and annuity products. It is now very common for income riders on fixed index annuities to provide an increased payment in the event of nursing home confinement. LIMRA estimates that there was $2.6 billion in life/LTC combination product sales in 2013, more than quadruple the sales volume of these products in 2008. There is every reason to believe that this increasing sales trend will continue because the consumer need is growing.

There are a variety of types of long¬term care¬related riders offered in index universal life products. Some carriers offer riders that have no explicit premium or cost of insurance charge, but if the benefit is exercised, the policy's death benefit is discounted. The advantage of such a rider is that it is provided at no cost unless the benefit is used, and the disadvantage is that the payment is only a portion of the death benefit that is accelerated.

Other carriers offer riders that have explicit charges associated with them and that pay the policy's full death benefit over time, and some carriers even provide an extension benefit such that amounts greater than the policy's death benefit is available for LTC¬related expenses over time. Some carriers offer chronic illness benefits, whereas others offer true tax¬qualified long term care insurance coverage. There are quite a few variations in the marketplace, all of which can be helpful – you just want to understand the differences, advantages and disadvantages of what you are selling versus other options that are available in the marketplace.

Next Steps for Agents

To recap our list of trends, key themes in the index product markets in 2015 will be new indices in fixed index annuities, regulatory debate over index universal life illustrations, and long¬term care¬related features. Also, we expect to see innovations in one type of index product influence changes in other index products. For example, I wouldn't be surprised if the fixed index annuity innovation mentioned above – new indices – migrates over to the index universal life market as well. After all, what works for one type of product can often work for another type, and there are many carriers looking to innovate to create an advantage in the marketplace.

Because there is so much innovation taking place in the marketplace, and because these innovations help to address consumers' key needs for reliable accumulation and income while providing a financial safety net in the event of chronic illnesses or death, advisors have an even stronger need than ever before to take advantage of educational opportunities available to them. Call your marketing organization and ask what’s new in the marketplace. Attend an industry meeting. Or attend a carrier’s on¬line educational event. You just may find a solution that helps you to better serve your clients and grow your business.

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