FINANCIAL ADVISOR

What's It Worth?
By Mary Rowland

A consultant shines a light into the dark hole of equity-indexed annuities.

Most financial advisors know that equity-indexed annuities are a seriously flawed product, appropriate for almost no one. Yet, according to an April 2 report in the National Underwriter, sales topped $25 billion last year. Someone is buying them. So what to do when a new client comes in with such an annuity already in his portfolio? Dump it? Wait until the hefty surrender charge disappears? Take penalty-free withdrawals? Maybe.

My Response: Mary Rowland is a financial columnist who is not without her redeeming qualities, but this particular article is pure drivel. I should also add that I've read her book The New Commonsense Guide to Mutual Funds and my impression is that she has a strong bias for stock mutual funds and clearly doesn't think much of bonds or bond mutual funds. In other words, she makes her living by being what I like to call a "Wall Street Cheerleader".

She also seems to think active fund management and load stock mutual funds are fine … as long as you limit your purchases to up-front "A" shares. This is understandable in that she writes extensively for publications like Financial Advisor, which I generally find quite informative. All of these financial publications, of course, are dependent on advertising from these expensive load mutual fund families for their survival. Is she biased? She obviously has her own agenda, in my humble opinion. But YOU be the judge!

She continues …

Introduced in 1995, equity-indexed annuities were touted as a way to get hold of a stock market return on the upside while receiving a guaranteed return on the downside. What could be better for a conservative investor who had become frustrated in the mid-'90s because he was losing out on the biggest stock market boom in history? No risk, great return. But of course, the pitch turned out to be an empty promise. Both fee advisors and financial journalists slammed the product right from the start, arguing that it was riddled with hidden costs and unsuitable for retail investors. But sales took off anyhow.

My Response: To say both fee advisors and financial journalists slammed the product "right from the start" is highly inaccurate. The fact is, most of the financial press that caters to the securities industry didn't give two hoots about Index Annuities back in the mid-to-late 1990s because they were too busy singing the praises of the "New Economy" and the tech stock revolution. Further, the sale of Index Annuities didn't really take off until the stock market came crashing back to earth in 2000. And the financial press didn't really jump on the band wagon and start knocking these Index Annuity insurance products until a couple of years ago when the NASD made its (still unresolved) move to get this product under its regulatory control. Further, if you are a true 100% fee-only advisor you don't even carry an insurance license. So why in the world would you give an insurance product that is capturing billions in assets (that you might otherwise be managing) a thumbs-up, no matter how good it might actually be? By definition, you're going to "tout" your own limited approach to money management and let the client go elsewhere for their insurance planning needs. Why? Because fee-only asset management is all you have to offer!

I have 42+ years in the financial services industry and started my career as an insurance agent, so I like to think I have a better grasp on this side of the planning process than most. I have also been a Certified Financial Planner Practitioner (CFP) since 1985. And when I made the decision to give up my securities license and set up my own RIA, I was a Registered Principal with a national broker/dealer. In short, I think I have a pretty good understanding of what it means to be a good financial planner. And that goes far beyond touting stock mutual funds for a living, as Rowland is so quick to do ... with no regulatory body overseeing <u>even</u> <u>one</u> <u>word</u> of her "opinions", I might add!

Specifically, I've been recommending Index Annuities (where appropriate) since they were first introduced in 1995. And I can assure you that I DID NOT "tout them as a way to get hold of a stock market return on the upside while receiving a guaranteed return on the downside". The first product introduced was, in my opinion, actually a perfect alternative at the time to bonds … not stocks. Rowland is correct that the stock market was on a tear from 1995 -2000. But who invests 100% of their money in stocks as Rowland generally recommends; particularly during a run-away bull market? A balanced portfolio usually has <u>at</u> <u>least</u> 30% of the money in bonds and most clients (with some honest help from their advisors) will admit that their risk tolerance is moderate at best.

When the first Indexed Annuity came out, the interest crediting was linked to the S&P500 only and it paid a full 84% participation on the index's return (without dividends). It was a 5 year high-watermark design and locked in the highest point on the index over the five year period. Given the stock market's "exuberance" at that time this presented a great opportunity to make some potentially excellent returns for our clients on the money we had allocated to bonds in their portfolios … with a 3% guaranteed floor over the five year period of the plan. And we could still keep the money that was allocated to stocks invested in the market. In short, all you had to do was think a little outside of the box and take action. The bottom line was we made an average annual 12% -14% return for our clients during this period on the "bond side" of the portfolio with no downside market risk <u>and</u> minimum guarantees of 3%. And, yes, we even used <u>the</u> <u>annuity</u> to fund IRAs!

<u>*So please forgive me, Ms. Rowland, if I find you rather disingenuous in your above remarks. Where, exactly, was the "empty promise" in the 12% -14% average annual returns we generated for our clients? And for the record, I've been advocating fees over commissions on the securities side of my business since 1993*</u>.

She continues …

Craig McCann, Ph.D. and CFA, and Dengpan Luo, Ph.D. and CFA, of Securities Litigation and Consulting Group in Fairfax, Va., wrote in a 2006 research paper that the annuities carry "exorbitant and indeterminable costs, lack of federal regulation and an inability to decipher what the investments will earn," among other problems. "Equity-indexed annuities are complicated investments sold to unsophisticated investors without the regulatory safeguards afforded to purchasers of similar investments," the two researchers said. "We estimate that between 15% and 20% of the premium paid by investors in equity-indexed annuities is a transfer of wealth from unsophisticated investors to insurance companies and their sales forces."

Although the complexity of these products "makes it virtually impossible even for brokers and agents to properly evaluate the annuities," McCann and Luo wrote, "salesmen can readily determine that commissions paid for selling equity-indexed annuities—as high as 10% or 12%—are much larger than commissions paid on mutual funds and variable annuities."

My Remarks: This firm was founded by McCann in <u>2000</u> to provide finance, economics and investment management consulting to <u>parties in conflict</u>. In other words, McCann sells his services as an "expert witness" who is hired by the attorneys for one side of a dispute to counter the other side's testimony. Specifically, he offers himself up as an expert witness in <u>stock</u> <u>market</u> issues, as his credentials clearly indicate.

In short, if you read this above mentioned 2006 "research" paper I think you will quickly come to the same conclusion I did. Specifically, you will see it is nothing but his attempt to drum up some new business for his firm by piggybacking on the NASD hoopla over who gets to regulate the Index Annuity marketplace. That is not to say Mr. McCann isn't entitled to his opinion or that some of his comments are not without merit.

But let's cut to the chase. The fact is, the sale of Index Annuities substantially reduce potential securities industry profits. The $25 Billion mentioned above came from somewhere last year didn't it? Could it be that the securities industry is simply feeling a little heat from the Independent Marketing Organizations that now control distribution of most Index Annuities that are on the market today? And could it be that the securities industry simply wants to eliminate that competition before it gets even more costly?

All one has to do is look at the wording here to see this might just be the case. For starters, what, exactly, are "exorbitant and indeterminable costs", Mr. McCann? On the one hand you say the costs are exorbitant, and on the other hand you say the cost can't be determined. You can't have it both ways. You have to be able to first determine the costs to say they are exorbitant. And if the actuaries who designed the products can do that, why can't you? After-all, you're putting yourself out as an "expert" here.

Next, what stock market index (the link to the policy's returns) gives one the ability to "decipher what the investment will earn"? No one … not the insurance companies or the advisors recommending these products … tell clients what they will earn each year. You know that.

Further, to say Index Annuities are not regulated is pure poppycock. Every state in the country closely regulates these insurance products.

In short, throughout this article Rowland uses every inflammatory trick in the book to "prove" her point that Index Annuities are "bad". But it won't work. And one day soon she will have to change her tune as the financial press finally starts to understand that the Index Annuity is simply a tool that has many benefits for the client when properly implemented into the financial plan.

In other words, one could just as easily use similar inflammatory rhetoric like Rowland is using in this article to highlight all the hidden and exorbitant fees charged by the mutual fund industry for actively managed mutual funds. But I'll leave that task to Jack Bogle, founder of the Vanguard Funds … who can do it so much better than I can!

Lastly, for the record, my favorite Index Annuity right now has a current 8% cap for $100,000 of premium or more, using an annual point-to-point reset strategy. Further, the policy has a relatively short 10 year surrender period and it pays a 7% one time commission, or a lower first year commission and a small ongoing .25% trail commission. Needless to say, this newer generation product is much different than Rowland's "example" in this article. Is the commission I earn on this product "too high"? You be the judge.

But let me simply add this comment about fees vs. commissions: If a client, or prospective client, has a lower risk tolerance that demands a conservative to moderate asset allocation, they are going to very likely earn less than a net 6% annually over time based on Modern Portfolio Theory expected returns for this type of allocation. That's the net amount they get to keep after they pay mutual fund fees on an actively managed balanced portfolio of no load mutual funds of about 1% - 1.25% a year, and ongoing advisory fees of about 1.5% per year on the entire account values for the average investor. Of course, they are also accepting significant downside risk in this actively managed mutual fund wrap account scenario, too.

Further, my income will keep going up every year in the fee-only actively managed wrap account if the account values increase, because my 1.5% base advisory fee is figured on the total account values each quarter. On the other hand, with an 8% average cap, my client is likely going to earn <u>about the same net 6%</u> on the Index Annuity over the 10 years based on Modern Portfolio Theory expected returns for the S&P500 Index (without dividends). In short, any way you cut it, this is better than what shorter-term intermediate bonds will likely earn in this time frame based on today's low, but rising, interest rate environment. That's the <u>real</u> comparison that advisors should be looking at here, in my opinion.

So what I'm really doing by recommending an Index Annuity (when appropriate) is showing the client how to enjoy better potential returns with <u>less</u> risk. And I'm actually earning <u>less</u> income from the client over the 10 year period, too. *<u>So please forgive me, Ms. Rowland, but you are just full of hot air on this issue. But thanks for trying to help all of us "stupid" financial advisors who can only understand "commissions" finally see the light</u>!*

She continues …

Again, many financial advisors understand all of this. But many retail investors do not. And so it was that a client of Glenn Daily, a fee-only insurance consultant in New York, brought him a number of the annuities her mother had purchased and asked Daily to evaluate them. He examined several fixed annuities. Although he knew an analysis of the equity-index annuity would not fit in his client's budget, he was intrigued by the challenge and he started poking around at the annuity's assumptions on his own time.

My Remarks: Let me be clear here. I certainly have nothing against Mr. Daily. He seems to have a strong educational background and his work looks well thought out and professional. But in my state all you have to do to become a "fee-only insurance consultant" is <u>take a test</u>!

As for his new service: One can't help but notice that it seems rather <u>convenient</u> that he had completed doing his <u>first analysis</u> of an Index Annuity just in time to share his story with Ms. Rowland. *<u>Now, she can use this one isolated case to, in turn, imply that the policy he analyzed is the norm for the entire Index Annuity marketplace when, in fact, that is so far from the truth that it is simply ludicrous!</u>*

She continues …

In 2001, his client's 76-year-old mother had put $50,000 into an equity-indexed annuity with an initial surrender charge of 17.5%, which declined over 16 years. The annuity's return was tied to the Standard & Poor's Index of 500 stocks with a 3% guaranteed floor. "Mom" initially liked the insurance agent but they'd had a falling-out by the time Daily was asked to look at the contract last year. The contract was under water. The surrender charge was 15%. "The sales pitch was 'no risk,'" Daily says.

My Remarks: I'll skip past Rowland's rather apparent innuendo that insurance agents are bad guys that can't be trusted ("Mom's" falling-out with her agent). She has a right to think whatever she wants about commissions vs. fees. I would, however, be interested to know more about <u>the specifics</u> of this case she's discussing here. Usually, Index Annuity products with longer surrender periods and these type surrender charges have a "bonus" attached, but Ms. Rowland makes no mention of that.

She also doesn't mention how "Mom" actually had this money positioned <u>before</u> she bought the Index Annuity. So let's fill in the blanks and assume that "Mom" had been losing money in the stock market for almost two years when she bought this Index Annuity in 2001, as many "unsophisticated investors" (McCann's words, not mine) were doing about that time.

Let's also, for the record, assume "no risk" wasn't a "sales pitch" (Rowland's words, not mine). Instead, let's assume risk was a very real concern for "Mom" … and that she had already lost 15% - 20% of her money in the stock market when the Index Annuity was recommended to her. As for the large surrender charge mentioned in this example: Assuming the product did give “Mom” a bonus up front, the insurance company needed a way to get that money back if she surrendered early. And these longer and larger surrender charges are how insurance companies accomplish this. After all, there is no free lunch.

Was the product appropriate for this client? We don’t really know, do we? Maybe “Mom” is worth Big Bucks and told the person who recommended the policy that she had no real need for this $50,000, but simply was getting very uncomfortable with stocks in her portfolio. If that is true, I can see why the advisor might have recommended taking the bonus because it would let her leverage this extra money over time for the family or her favorite charity.

In other words, every case is different and Ms. Rowland does our entire financial services industry as a whole a real disservice by specifically using this isolated case to justify her obvious dislike of Index Annuities!

She continues …

After Mom bought the contract, the S&P went down.

My Remarks: We should be more precise here, Ms. Rowland, and say that when “Mom” bought the Index Annuity the S&P500 was on its way to going down for the third year running … and this last time it would go down by almost 24%!

Again, we don’t know how “Mom” was invested before she bought the Index Annuity … or how much she had lost if she was actually invested in stock mutual funds as Ms. Rowland strongly advocates. Maybe some rep actually had her invested 100% in tech stocks! I actually had a 72 year old widow that had dropped a TON in the market come to me as a referral who had done exactly that (on her own) using no load mutual funds and individual stocks. Hum … maybe she had actually read one of Ms. Rowland’s previous articles touting stocks from that time period. Hadn’t thought about that!

But let’s assume “Mom” wasn’t an “unsophisticated investor” and, instead, even believed in index funds over actively managed funds. Let’s further assume she was invested in the Vanguard S&P500 Index Fund like a lot of other “smart” folks were doing during this period. Had she “stayed the course” she would have lost **9.95%** in 2000, **13.11%** in 2001 and **23.36%** in 2002. I’ll let YOU do the math as to what she might have actually had invested at the start of 2000 … an amount that left her with exactly $50,000 when the life insurance agent/advisor came on the scene and recommended the remaining $50,000 go into this Index Annuity.

Also, be sure to do the math on what she would have had left had she stayed in the market. Lastly, while it is true that you need an insurance license to offer Index Annuities, the fact is the NASD came out with its Memo to Members 05-50 in August of 2005 because the Index Annuity is being sold extensively by dual licensed individuals who have both a securities and an insurance license. Was this a legitimate response because the NASD found there was rampant abuse in the Index Annuity marketplace? The facts don’t back this up. And the only other answer would seem to be that it was simply the first step in a major money grab by the broker/dealer community and the NASD to start making money off the sale of these insurance products (which until Memo 05-50 were generally considered an outside business activity by most broker/dealers). Of course, that’s just my personal take on this and I’ll let you come to your own conclusions.

She continues …

The cap on the indexed account, which was 11.5% when she bought it, minus the 1.5% asset fee, had gone down to 9% with no explanation. In November 2005, the indexed account value was $50,653. The minimum guaranteed value was $53,460. If she chose to cash it in, she would be left with $44,907 after the surrender charge, a loss of 16%.

My Remarks: I'm sure that some agents who sell these products may not cover in detail the reason caps move from year to year, but most (including me!) do. In other words, if I want to continue to build my business via referrals/introductions and have satisfied long-term clients, I'm going to explain how the company sets the caps on these policies as well as all of the other policy features and benefits.

After-all, how the company sets the caps isn't rocket science. The insurance company is simply taking an amount that is approximately equal to the declared interest they would otherwise pay to the client on a traditional fixed annuity and hedging the potential return by buying one year call options (LEAPS) with this money. The bottom line: *Her cap went down primarily because the market was more volatile the following year, which caused the price of the options to go up. Higher option prices with approximately the same earnings on the insurance company's general account = a lower cap. End of story.*

Further, "Mom" was presented with, and signed, a policy disclosure form when she bought the policy. In short, there is such a thing as personal responsibility here on the part of the client. Also, we can't tell from the way Rowland words this article if "Mom" was age 76 in 2001 when she purchased the Index Annuity, or was age 76 when her daughter hooked up with Mr. Daily in 2006. Is it, perhaps, just possible that Rowland is being so vague here on purpose?

And while I personally would not have recommended a product like this to someone age 76 without compelling reasons to do so, this is a good opportunity to examine how most seniors look at their retirement nest eggs. The reality is most seniors are quite conservative. And they don't normally spend their nest egg money in a lump sum. Most of them, frankly, don't even like to spend the interest! So how does the Index Annuity fit into this scenario? It fits quite nicely, actually, because the vast majority of Index Annuities give the client the right to access at least 10% of their money every year with no surrender charges … and even more if they require long-term care in a nursing home. In other words, a product's liquidity is important, but it is not the only issue here. So my question is this: Was "Mom" the one who was looking for Mr. Daily's help here? Or was it her daughter, who at this point in the game may have her own agenda for her mother's money?

Even more important, was the person who recommended the Index Annuity to "Mom" back in 2001 ever actually judged by the regulating body in the client's state of domicile to have sold an unsuitable product? Ms. Rowland never mentions that rather important consideration does she? Surely, the answer to this question is an important qualifier as to the validity of her example, don't you think?

Or is this entire article by Rowland and this so-called example case just a sham designed to knock Index Annuities in general … and help sell Mr. Daily's new service?

She continues …

When customers buy such an annuity, they see it as the best of both worlds. What will their situation be if the market drops? "I won't be losing any money," they reason. "I can just get out later." Daily's calculations revealed just how expensive it could be to get out later.

My Remarks: In the 12 years I've been recommending Index Annuities NO ONE has told me they thought they "could just get out later". In short, every one of my Index Annuity clients understand there are surrender charges and what those charges are … and, more specifically, why we are recommending the product in the first place. The fact is, regardless of what columnists like Ms. Rowland and the NASD would like to have you believe, reaching retirement doesn't mean investors suddenly turn into total incompetents who can't make an informed decision on what to do with their money. Further, I can tell you first hand that I have had NOT ONE unhappy Index Annuity client over these last 12 years!

She continues …

Because Daily knew the cap was set at 9% for 2005-2006, he could predict that, after the asset fee of 150 basis points, the maximum "Mom" could have in her indexed account was $54,452 in November 2006. The guaranteed minimum contract value would be $55,064. So there was no chance the indexed account value could exceed the minimum account value as of November 2006. And there was no chance she could come out whole because of the surrender fee.

My Remarks: Again, because we have to fill in the gaps here that Ms. Rowland fails to provide, let's assume "Mom" had been invested directly in the Vanguard S&P500 Index Fund … and stayed invested that way from 2000 on. If that were the case, her 2000 account values would STILL have been underwater seven full years later. And if we assume only 2½% inflation that means she would have "enjoyed" a loss in purchasing power of approximately 18% on her money in the process. Further, she would have been subjected to a TON of market risk by staying invested vs. NO market risk in the Index Annuity.

Of course, she did buy the Index Annuity. And the <u>real</u> question here is <u>why</u> would she want to "get out" after only 4 or 5 years? That's NOT how annuities are designed to work … and it makes the entire premise behind this article <u>highly</u> suspect.

She continues …

The cap is reset every year by the insurance company with no explanation of what the new interest-crediting rate is based on. The indexing strategy on Mom's policy is based on the point-to-point increase in the annual value of the S&P 500. Some contracts are reset monthly and a number of other interest-crediting options exist, making it very difficult for a retail customer to guess what the return might be. Instead, the customer focuses on that "promise" that he will never lose money because he has a guarantee. Suppose the S&P gains 7.24%. You subtract the 1.5% asset fee and the indexed account grows at 5.74%. The return does not include the dividends paid by the S&P 500. And we know that the dividends are key to growing stock market investments.

My Remarks: Each interest crediting method tends to have its day in the sun and will outperform the other crediting scenarios during that time. This is why most Index Annuity policies now offer a variety of crediting options that can be changed each year. This allows the client and the advisor to sit down and determine if the point-to point, monthly average, monthly cap, etc. makes the most sense for the coming year. As for it being "very difficult for a retail customer to guess what the return might be", does Ms. Rowland want us to believe that she … or any of her other so-called experts … has a crystal ball that tells us how the Index is going to perform over the next 12 months? Well, that's the beauty of this index-linked product. You don't <u>have</u> to know exactly how the index will perform going forward.

<u>*You just have to understand that linking the return to the specific index gives the client a better than average opportunity to earn a better than average return vs. a traditional fixed annuity over time.*</u>

Ms. Rowland wants us to believe that the product is being sold extensively as an "investment" by all those "bad old <u>commissioned</u> insurance agents" and not as a fixed annuity with guarantees. This is absolutely ridiculous. Are there some agents that use sales tactics that are not appropriate for this product? Of course! But the total number of Index Annuity complaints vs. the total number of Index Annuities sales is really quite small. Particularly when you compare it to the ratio of mutual fund complaints to sales during 2000 -2002. Do we hear Ms. Rowland talking about the "dark hole" of actively managed stock mutual funds? I think not!

She continues …

The interest crediting rate is not linked to anything, not to the cost of hedging with options on indexes, not to any stock market measure or published interest rate. “The most common arrangement is that it is guaranteed for the first year,” Daily says. Perhaps the 11.5% was a teaser rate. But nowhere in the contract does it say so. The policy says that, “Our board declares the cap for the year coming up,” but “they don’t have to file a reason for the change,” he says. “They would probably say that they have to be flexible in order to cover the cost of hedging.” So it’s “indexed,” but to what? “How can you call it indexing when the company controls the interest rates?”

My Remarks: Rowland is, frankly, taking some of the wording Daily uses in his analysis out of context here. But, hey, maybe she had a deadline to meet here and finds this type of journalism acceptable under those circumstances.

I really can’t say this more clearly: When a person buys an Index Annuity they are required to sign detailed disclosure statements at the time of the sale and they get ample time to review the policy after delivery. Are there companies that come into the Index Annuity marketplace and offer high commissions on aggressively priced products in an attempt to capture market share? Of course there are. Just like there are really bad mutual funds and other securities products that simply don’t make good economic sense for our clients. That’s why we, as advisors, need to do due diligence on these companies and products before we recommend them … just like we do on every other recommendation that we make.

Further, in defense of the Index Annuity concept, I should also add that there are many well known stock mutual funds (like Fidelity Magellan) which are little more than closet index funds that, in reality, are charging huge fees for the small portion of the portfolio that doesn’t mirror the index. Most advisors, myself included, first read about this in Ben Warwick’s Investment Advisor column in February of this year (2007). The article is titled “The True Costs of Active Management”.

Warwick was reviewing work done by Ross M. Miller of the State University of New York at Albany titled “Measuring the True Cost of Active Management by Mutual Funds” which should be must reading for every advisor and mutual fund owner in the country. Needless to say, I’d like to see the same kind of “moral outrage” from Ms. Rowland over this little mutual fund charade as she seems to be so willing to show when it comes to Index Annuities!

How about it, Mary Rowland, think you might do an article on this topic for us one of these days?

She continues …

Daily realized that it would be most difficult to decide whether to tell a client like “Mom” to just drop the bad policy and swallow the surrender fee or to stick it out. So he set to work analyzing it, keeping track of the two separate account values, the cap, the floor and the fees on it. This was the first time I ever analyzed an indexed annuity,” Daily says.

My Remarks: Let’s see … the Index Annuity concept has been around since 1995. Further, **$ Billions $** have gone into these products. And this is the first time he ever analyzed an Index Annuity? Well, I guess we all have to start somewhere! But wait … maybe the real reason Mr. Daily hasn’t been able to find any work in this arena until now is because there just haven’t been that many unhappy Index Annuity policy owners out there.

The fact is, even when you examine the sample case on Mr. Daily’s website (which has a 6% cap vs. the 8% cap in the policy I currently recommend), it is pretty easy to conclude that Index Annuities in general really are a great bond alternative like I’ve been advocating for the past 12 years. In other words … sorry Ms. Rowland, but I think you may have picked a wrong “expert witness” here. Did you even really look at this example … or did you just skim though his website to find some words you could quote that on the surface seem to “prove your point”?

In fact, please let me quote from his website, too: "Our goal is to help you avoid the dual mistakes of keeping an indexed annuity that you should get out of, or getting out of an indexed annuity that you should keep".

In other words, maybe Mr. Daily doesn't share Rowland's perceived rabid dislike of Index Annuities after-all! And while Monte Carlo simulations (the basis for his reports) are helpful as an analytical tool, I think there is an even more important issue here. **That's investor behavior.** All of us in the business are familiar with the DALBAR studies that clearly show people often get badly burned by the hoopla and marketing of the mutual fund industry. In short, the most recent DALBAR study shows that the average stock mutual fund investor actually only earned 3.9% annually over the last 20 years. And we can only conclude from that simple truth that the returns on Index Annuities over time, with no market risk, might be a far better place for most folks to put their money!

She continues …

"The pitch is that you get the best of both worlds, but the truth is people don't think about what will happen if you go below the floor. They think: 'What will be my situation if the indexed S&P drops? I won't be losing any money. I can just get out later.'" That is a lesson of this product that is subtle. How will you feel if the market goes down? Now "Mom" is sitting with $54,542 and the market went up more than that. She is under water by 1%.

My Remarks: Again, she is 1% under water vs. the S&P500 Index. But the Index Annuity isn't attempting to compete with the S&P500 Index. Rowland can imply that until the cows come home, but she's singing an old song that fell off the charts a long time ago. What we have here is simply a fixed guaranteed annuity with the return linked to the S&P500 Index's returns (without dividends). Period!

And frankly, Ms. Rowland, I can't help but ask: Do you really think intelligent professionals are going to let you cherry-pick the years you want to use here in this "example" and let it go at that? The S&P500 was down from its high for over seven years running … and that's just the way it really is! How far down might "Mom" be had she stayed invested?

Not to beat a dead horse, but losses on the Vanguard S&P500 of **9.95%** in 2000, **13.11%** in 2001 and **23.36%** in 2002 are rather substantial. And no Monte Carlo Simulation like Daily uses in his analysis can make that simple fact go away. Not to mention the reality that, on average, 80% of the active stock fund managers can't even beat the index in any given year … let alone repeat that feat for even two years in a row!

Lastly, can the stock market take another major hit any time soon? **You Bet It Can!**

She continues …

Just about then, Daily was approached by another client, this one a chartered financial analyst whose client was an engineer—Daily's kind of client. "That put me on the road to thinking that there is a need for a service to do this," he says. Both the advisor and client understood Monte Carlo simulations and were able to follow Daily's analysis. On this contract, the indexed credit cannot be negative. There is no maximum cap; there is a minimum of 8%.

This time, Daily decided to go to the library, do some research and develop a prototype for his analysis that he could offer through his Web site, www.whatsmypolicyworth.com. "I don't know how you could give competent advice without doing a simulation," he says. "What are the chances, if I hold this for ten years that I'll do better than some benchmark?"

My Remarks: I've said above that Mr. Daily's report is pretty good as far as it goes. But there is no way a report like this can tell the whole story because reports don't address the emotional part of the investing equation. With many investors safety is a key consideration and in my opinion that is a main reason Index Annuity sales are so robust.

She continues …

Once he'd analyzed the two annuities, Daily figured he could piggyback on the work he'd already done and offer to analyze equity-indexed annuity contracts for $495 for one interest-crediting method and $125 for each additional method. He prefers to work with financial advisors rather than the annuity holders because of the complexity of the product. His new service became available in mid-April.

My Remarks: Daily uses reasonable after-tax benchmarks of 6% and 4.5% in his analysis. The 6% is used to compare the Index Annuity against a diversified portfolio and the 4.5% is used to compare the Index Annuity against bonds. Yet Rowland doesn't tell us this, and the implication here that every Index Annuity ever brought to market will fail this test. This is far from true … and I don't have to pay $495 or more to make this statement!

The fact is even the Index Annuity in Daily's sample report on his website clearly shows the value of the Index Annuity as an alternative for conservative investors; or as an alternative to bonds in almost anyone's portfolio who isn't using bonds for current income. That's a far cry from Rowland's derogatory opening remarks in the first paragraph of this article!

Rowland finally sets us free and ends her little tirade as follows …

Isn't it frustrating when being a financial advisor means you're required to clean up other people's messes? And the worst products are always the most complex—the better to eat you with, my dear, said Grandma the wolf to Little Red Riding Hood.

So Here Are My Final Remarks: That's nice … give Index Annuities one more final slam as you wrap up this nonsense, Ms. Rowland ***. But who is the "real wolf" in all of this?***

I submit that in this case the "wolf" is you, Ms. Rowland. This article is written with all the authority of a piece you might find in one of those tabloid rags at the checkout of your local grocery store. And for the record, it isn't frustrating when I have to clean up "other people's messes". That's actually what financial advisors often do!

Sometimes the messes are caused by the clients because they made dumb choices. Sometimes they are caused by some ill-trained securities rep that doesn't have a clue and sells inappropriate products, or outright unsuitable products that slip by compliance. And sometimes the messes are caused by some greedy salesperson who attempts to grab all of the client's money and put it into inferior Index Annuities that pay the highest commissions on the street when that clearly isn't appropriate or suitable either.

But as often as not, the messes are caused when the public reads an article by some muckraking financial columnist with their own personal agenda who could care less if they present a fair and unbiased review of the facts. I put this nonsense you've "shared" with us today clearly in that category, Ms. Rowland. We simply deserve better from you … and that's just the way it really is!

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June 14, 2007