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Dangerous Trends In Annuity Marketing Put Industry And Brokers In Jeopardy

It's hard to know where to begin or whom to blame: the annuity broker trying hard (and very creatively) to market indexed annuities? Or the carrier(s) he represents? The regulators? Maybe it's just a manifestation of "the process" in which negative results emerge from the efforts of good people.

Until it was withdrawn recently, you could find on *YouTube.com* a stark example of why the indexed annuity industry may be destined to implode unless it finds a way to reign in misleading marketing and sale practices used by some brokers. While I believe the video medium is one of the most powerful tools we have to market ourselves and annuity products, the story content in this situation was fraught with problems and raises issues that put both the industry and brokers in jeopardy.

A Flawed Video-Based Marketing Strategy

In the video, the broker told viewers that he is "president and financial wealth strategist" for his company, a nationwide wealth management firm. The nicely produced video extolled the virtues of the broker's "strategies" that "guarantee a minimum rate of 13.68 percent over the next 12 months." According to the broker, consumers "pay nothing to implement these strategies." He invited viewers to receive more information about retirement accounts and strategies and to become part of the informed group of "successful investors" versus the uninformed group of people be-

ing robbed each and every year. The video never explained what the strategy is or how it is able to pay 13.68 percent. It's implied that the answer will be discovered only by visiting the broker's website.

The broker's video and subsequent marketing tools targeted 401(k) plan participants who had left their employers and thereby had a critical decision to make about their accumulated 401(k) account values: what to do with them? In his video, the broker told viewers that it was a mistake for employees to leave accumulated assets in a previous employer's plan. To sway viewers away from doing that, he raised the specter of Enron and MCI/WorldCom, stating, "Ask some of the Enron and MCI/WorldCom employees how this worked out for them."

The broker explained that it is also a mistake to roll over retirement assets into a new employer's plan because it "limits investment choices."

In the video, the broker revealed that the "best solution was to roll retirement account assets into an investment in which you have total control over your money by investing in the best financial products in the marketplace." The "investment" was not described.

The marketing strategy gets even more interesting when you read the broker's free report. It was misleading to an astonishing level. Entitled "How to Maximize Your 401(k) or IRA after Leaving or Retiring from Your Previous Employer," the printed piece, like

the video, focused on examples of Enron and MCI/WorldCom to frighten readers into transferring their 401(k) retirement assets. The report stated that rolling over to an IRA is “the only practical way of regaining control of your life savings” and “hands-down the best choice.” This broker also appeared to be on the side of making life more convenient for potential clients as his report stated:

“Something else to consider is the convenience and ease of management that comes along with consolidating your retirement accounts into one professionally managed IRA account. If you receive statements from multiple fund companies, you might be less inclined to review each one and simply add them to your ‘financial stuff’ file, which you may not review often enough. Consolidating accounts will improve the ability to manage investment activity and maximize performance results.”

The report then extolled the virtues of his firm’s “no-fee accounts” that come with “phenomenal guarantees” and access to accounts offering a “13.68 percent guaranteed return program in writing from a top investment company.” Along with this tremendous-sounding guarantee, investors could get the following: No fees or commissions to pay *ever!* No stock market risk to your principle *ever!* No losses—all gains are automatically “locked in” each year! No taxes to pay—tax deferred until you need the money! *No kidding!*

What’s the “Top Investment Account”?

Additionally, the report was sharply critical of mutual funds. It stated that “even though millions of investors own mutual funds inside their 401(k) plans and IRAs, many would be better off transferring their mutual funds to an indexing strategy. Indexing participates in the upside gains of the market (like your stocks and mutual funds) without the downside risk of losing your principal (like CDs). In other words, you literally get the best of both worlds wrapped in one investment.”

The broker’s report also implied that mutual funds have expenses that are high, that the average portfolio manager has insufficient on-the-job experience, and that

the average mutual fund turns over “90 percent of its portfolio annually.” Even no-load mutual funds were hammered.

This broker wanted investors to: “Stop paying unnecessary fees and risking your investments in the market with all the political uncertainties that exist today. Why not get the same type of performance with no fees, and a guarantee that your principle is protected 100 percent of the time.” His report also advised: “Some of our most popular and sought-after ‘indexing strategies’ offer a 13.68 percent *guaranteed* first year return on your investment and a 10 percent bonus on day one.”

So what was the “top investment account” promoted by the broker? This broker’s agenda was primarily selling an indexed annuity that offered a 10 percent “bonus” on premiums paid. When added to the base interest rate, the stated total first year rate became 13.68 percent. Obviously, an indexed annuity cannot be described as an “investment account” or “indexing strategy” or by any other name except what it really is.

A Long Way from Being Compliant

This example of the broker’s video and written report is a vivid reminder that some contemporary sales practices are a long way from meeting acceptable compliance standards. Here are just a few standards this material seemed to violate:

- ✓ Comparing investments invalidly and incompletely
- ✓ Categorizing the annuity as an investment
- ✓ Asserting that the “investment” was “insured”
- ✓ Alleging comparison to CDs
- ✓ Comparing the annuity favorably to mutual funds

The broker even asserted that the annuity was insured to an “unlimited amount by the National Association of Insurance Commissioners.” I’d say that his broker’s misleading marketing materials violated every rule and guideline covering appropriate sales practices that’s ever been enacted and maybe a few not yet enacted. *It was a textbook case of how not to present*

yourself to the buying public.

What Would a Consumer Think?

What would typical 401(k) investors think after watching the video and reading the report? They would probably be quite excited about moving their retirement assets into such “strategies” and “investment accounts” that pay a guaranteed rate of 13.68 percent. They’d probably like the fact that they could receive “the upside gains” of “stocks and mutual funds” without the “downside risk.” And they would be comforted by the fact that their monies invested in those “strategies” and “investment accounts” were protected against loss to an unlimited amount. *If only it were true!*

This example of indexed annuity marketing demonstrates the limitless creativity of producers. It also shows how misleading sales practices are making the leap to digital delivery—a development that brings with it new levels of liability potential for indexed product providers. Any pretense that a misleading marketing campaign might be confined to a broker’s local territory is blown away once it migrates to the Internet. Moreover, it’s potentially more difficult for an annuity provider to deny knowledge of its brokers’ poor sales practices when those practices are exposed for all to see on demand.

The lesson: *Think long and hard before you put anything on the Internet, and make certain that it has been vetted by competent compliance reviewers.*

A Dangerous New Trend?

More and more annuity producers are seeking to become investment advisors registered with various states. In my view, this is a dangerous trend that is likely to destroy careers and bring even more criticism to the already beleaguered annuity industry—unless executed with extraordinary care.

Why? When annuity producers become registered investment advisors (RIAs), they assume the role of fiduciaries obligated to place their clients’ financial interests ahead of their own.

Most annuity producers carry agent licenses with insurance companies. This is a relationship that obligates the agent

to represent the insurance company's best interests. Can an individual simultaneously serve two different agendas? Can RIAs simultaneously put their clients' interests ahead of their own while still carrying on their traditional annuity sales and marketing activities? To me these are oil and water paradigms in which the two competing agendas cannot coexist within the same client relationship.

Why, then, are annuity producers interested in becoming RIAs? The lure of side-stepping broker/dealer compliance oversight can be a powerful attraction. But no producer considering such a move should forget that RIAs take on the responsibility of becoming their own compliance officers, and also assume the big responsibility—and liability potential—arising out of their advertising activities. Moreover, RIAs are subject to regular audits including examination of their marketing materials and strategies. The sanctions for engaging in misleading advertising, not to mention failing to act as a fiduciary, can be severe.

Making a Change for Good

I've written extensively on how this free-wheeling marketing culture took root and how a vicious cycle made worse by negative press on annuities feeds on itself. Ever-increasing pressure is put on well-

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meaning brokers with each negative article that lambastes annuities in the consumer press. Brokers, therefore, see little hope in a marketing strategy that publicly identifies them as individuals with an explicit agenda to sell annuities. That this cycle must be interrupted is not in dispute. The only question is how. The benefits of annuities are too vital in the retirement income marketplace and too timely to not find a way.

One solution is for brokers and carriers to embrace technology and marketing packages that give them compliant, next-generation communications networks, streaming educational video, and advisor-branded micro sites that clearly communicate the features and benefits of EIAs and all financial products for that matter. This technology can also provide real-time monitoring

capacity for compliance officers—all designed to help annuity brokers transition to a better, more efficient and more compliant way of gaining new business.

Brokers cannot unilaterally implement such innovations, however. These are capabilities that annuity providers must adopt and introduce quickly if they stand a chance of saving the indexed annuity business from potential ruin. Sales practices like those used by this broker are a virtual invitation to the SEC to intervene in this messy situation. That would be tragic, especially at a time in the baby boomer retirement cycle when they need all the guarantees and reliable income opportunities that annuities can provide. The time has come for indexed annuity providers to take urgent action and their brokers should demand it. 🌐