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Who's Preying on Your Grandparents?

ABSTRACT:

Continuously looking to extend the life of their financial nest eggs, seniors are looking for better ways to invest their life savings. A recent story by the New York Times reports more and more seniors are selecting deferred annuities, a vehicle considered by some as an inappropriate investment vehicle for seniors because of actuarial life expectancies and high surrender charges.

BACK in February, Jose and Gloria Aquino received a flier in the mail inviting them to a free seminar on one of their favorite topics: protecting their financial assets. As retirees, they were always on the lookout for safe investment strategies as well as tips on how to make sure they didn't outlive their savings. Besides, the flier promised a free lunch for anyone attending the workshop, so what did they have to lose?

Potentially plenty, they would soon discover.

On March 1, Mr. and Mrs. Aquino stepped into the Coral House restaurant, not far from their home in North Baldwin, N.Y., on Long Island. They found themselves surrounded by about 50 like-minded retirees, most in their 70's and 80's, they said.

Over lunch, the crowd listened to a presentation by two investment executives from Diversified Concepts Inc. of Manhattan. Using charts and graphs, the men gave advice on how to invest wisely during retirement. Then they passed out forms and asked the retirees to list all their assets and financial holdings.

The Aquinos filled out theirs and left. Two days later, they said, one of the executives came to their home and described an investment with the American Equity Investment Life Insurance Company that would provide 7 percent interest on their money - immediately.

"When somebody tells you he will give you a 7 percent upfront bonus on your money and that you'll get that 7 percent even if the market goes down, you get interested," said Mr. Aquino. He said he signed the necessary documents and the executive left, handing a brochure to the couple.

That evening, the Aquinos told their daughter, Caroline, about their investment. "She said, 'Oh, don't invest like that before searching farther,' " Mr. Aquino recalled. "Then she went on the Internet and found these lawsuits going on in California against the company and we realized that we were not making a good decision."

The investment the Aquinos had chosen was an annuity, an insurance product that not only tends to carry high fees but also requires that most of the money stay locked up for years, making it especially inappropriate for many older investors, regulators say. In fact, the one they bought carried a staggering 17.5 percent surrender charge if it was cashed in during the first year, their daughter explained. Exit charges were not scheduled to disappear until 17 years after the purchase.

This meant that Mr. Aquino, who is 65, and Mrs. Aquino, 63, could not cash in the annuity without paying a surrender fee until they were in their 80's. The executive had not told them about the lockup requirement, the

Aquinos said, although the brochure he left with them described the fees in small print.

Thanks to their daughter, they were able to phone the company in time to cancel their purchase. Others, however, have wound up stuck in an investment that they cannot liquidate without severe penalties.

Meetings like the one attended by the Aquinos take place thousands of times a year in restaurants, American Legion halls and senior centers across the nation - and are a growing problem, securities regulators say. The seminars are usually described as a way for retirees to receive free advice on estate planning, asset protection and tax reduction. After a short presentation, the attendees are approached by a sales representative, who almost invariably encourages them to liquidate their stocks, bonds and 401(k)'s and to buy an annuity.

"We started getting all these complaints from children of seniors who found out that their stock portfolios or other investments had been transferred into these annuities," said Joseph A. Ragazzo, deputy attorney general of California. "We see this investment abuse as a real problem. These cases are metastasizing all over the country."

David J. Noble, chief executive of American Equity Investment Life Insurance, the company that wrote the Aquinos' policy, said: "I deeply differ with anyone saying we have serious problems. We have over 200,000 annuity policy holders, and the percentage of complaints we have is 0.002. We are extremely market-conduct aware."

Mr. Noble also said that annuities' guaranteed rates of return and protection of principal make them attractive to people worried about how they are going to pay their bills.

The president of Diversified Concepts did not return several phone calls.

WHILE prosecutors in New York and Washington investigate questionable accounting practices in the insurance industry, regulators elsewhere say they are fielding more and more complaints about aggressive sales practices by insurance companies that design annuity products and by the people who sell them. Under the guise of estate planning, regulators say, retirees are being pushed into annuities that carry commissions of up to 12 percent and that require their holders to keep them for as long as 15 years, or to pay big penalties.

It is easy to see why older people find such investments attractive. Annuities produce higher income than other investments and can provide payments for life. They are often sold as a way to allay retirees' fears of outliving their assets.

There are several kinds of annuities. Fixed annuities guarantee that a set amount of money will be paid regularly, regardless of how the underlying investments perform. Variable annuities, by contrast, are based on a portfolio of stocks that rise and fall, so their payments can fluctuate.

With interest rates near historical lows, the first-year rates of 7 percent to 9 percent on some annuities make them alluring to people on fixed incomes. And with the stock market going sideways, people are looking for investment alternatives, giving annuity sales representatives a ready audience.

But because of the fees associated with these products and the restrictions on cashing them in, they are hardly ideal for investors who may need the money quickly, or who die before the investment matures. In many cases, if the holder dies during the annuity period, the beneficiaries cannot redeem the annuity without paying a surrender charge.

Companies that sell annuities say that the higher rates they pay justify the surrender charges. Most investors, they add, are happy with their purchases.

But last February, Bill Lockyer, the attorney general of California, and John Garamendi, the state's insurance commissioner, filed a lawsuit against a group of companies and individuals that state officials said had tricked retirees into using their retirement investments to buy annuities. The suit said that the companies employed up to 300 sales agents and 80 telemarketers and sold annuities worth "hundreds of millions of dollars."

The defendants in the case included American Investors Life Insurance of Kansas, a unit of the AmerUs Group in Des Moines; and Family First Advanced Estate Planning and Family First Insurance Services, both of Woodland Hills, Calif. The complaint seeks \$110 million in civil penalties, consumer restitution and damages.

AmerUs said that it does not comment on pending litigation; however, the company said that it was taking the accusations very seriously and that it has strong sales and compliance practices. The Family First companies could not be reached.

Increasingly aggressive marketing has made annuities one of the hottest investments around. Money invested in variable annuities totaled \$994 billion at the end of 2003, up from \$771 billion in 1998, according to the Insurance Information Institute. Although total annuity sales fell slightly in 2003, they have almost doubled since 1997.

The growing ranks of the nation's retirees are a main focus of annuity sales agents. Next week, the Senior Market Expo opens at the San Diego Convention Center. "Now in its fifth year, Senior Market Expo is the only place you'll find the powerful strategies and ideas you need to boost your sales of life insurance, annuities, long-term care insurance and more," its Web site says. "This sales-centric event focuses on giving you - the senior market adviser - sales and marketing skills to earn more money selling to seniors."

Annuity sales can be highly lucrative. Commissions can reach 12 percent of the money invested, far greater than fees typically generated on stocks and other investments. Mr. Ragazzo, the deputy attorney general of California, said his office had found that some companies selling annuities sponsored trips to Hawaii and Europe for top agents. "Some of these guys are former used-car salesmen bringing in \$600,000 a year," he said.

Ads for asset-preservation seminars often use scare tactics. "Your family's assets are in danger!" reads one; "Trust me! You need a living trust!" goes another.

As sales of annuities have grown, so have investor complaints related to them. According to the N.A.S.D., annuities were at issue in about 600 arbitration cases in 2004, more than twice the number from three years earlier. Of the seven types of securities typically involved in arbitrations, annuities were the third most common last year, behind stocks and mutual funds.

Sellers of annuities are also the subjects of civil lawsuits. The American International Group, the insurance company whose accounting practices are under investigation by regulators and federal prosecutors, has been sued recently in California by elderly investors who bought annuities the company issued. The investors are also suing Estate Preservation Inc. of El Segundo, Calif., which sold the annuities.

One plaintiff is Beverly Buhs, 80, of Millbrae, Calif. In 1997, Ms. Buhs, then 73, and her husband Art, then 76, attended a seminar at an American Legion hall. Like the Aquinos, the Buhs filled out a form detailing their

assets; it was supplied by the seminar leader, an agent from Estate Preservation.

Mr. Buhs had previously invested in mutual funds, but he and his wife had never bought an annuity. With the agent's help, the Buhs set up a living trust, which they believed would help them avoid probate costs, according to the lawsuit. Shortly after setting up the trust, according to the lawsuit, the agent came to their home and persuaded them to sell their investments and to put them into a fixed annuity issued by SunAmerica, a financial services company bought by A.I.G. in 1999.

In December 2002, Mr. Buhs died of complications from an aneurysm. Only then did Ms. Buhs learn that the living trust did not protect her from probate costs and that she could not cash in the annuity without significant penalties, she said.

Ms. Buhs said she had to hire an estate lawyer to restructure the trust and wound up losing \$20,000 of a \$90,000 death benefit. Now she is still dealing with tax problems associated with the trust. "I tried to talk to SunAmerica, but I get so stressed out," Ms. Buhs said. "I don't know how to talk the jargon and don't know where to go. It's sad to think the world is like this. How many other seniors are being taken and deceived?"

Ms. Buhs's lawyer, Ingrid M. Evans of Renne Sloan Holtzman & Sakai in San Francisco, said: "The majority of annuity policies are going to seniors because those are people who have the money and are scared of the stock market and most susceptible to fear. But over a certain age it's not acceptable to sell someone a deferred annuity because they are going to pass away before it annuitizes," or matures.

Ms. Evans said Ms. Buhs had sued A.I.G. because SunAmerica "implicitly or explicitly ratifies the sales agents' unlawful and unfair schemes."

Chris Winans, an A.I.G. spokesman, said that the company would not comment on the litigation but said that the claims in the suits were unfounded. Ms. Buhs' annuity provided good returns - almost 20 percent from 1997 to 2002, after surrender charges, he said.

Mr. Winans added that A.I.G. has suitability policies and procedures that it monitors and enforces and that it requires the same of the brokers who sell its products.

Estate Preservation did not return a phone call seeking comment.

A.I.G. is the nation's top seller of fixed annuities through banks and the fifth-largest seller of variable annuities, according to the Insurance Information Institute. The company sold \$8.8 billion in fixed annuities in 2004 and sold \$8 billion of new variable annuities in 2003, the most recent figures.

In the first nine months of 2004, A.I.G.'s life insurance and retirement services group, which includes its SunAmerica unit, accounted for 45 percent of the company's total revenue. Sales at the group rose 24 percent from the corresponding period a year earlier and its operating income rose 23 percent, the fastest growth registered by any of A.I.G.'s four business segments. Premiums from annuities sold domestically rose 20 percent in the first nine months of 2004.

TYPICALLY, the people pushing annuities are registered only as insurance agents and not with government securities regulators who have large staffs to root out dubious practices. As a result, many fall through the regulatory cracks.

Last July, the California Department of Corporations filed a "desist and refrain order" against the Gentry Group, a Dallas company that sells annuities. The company had induced an elderly woman in Oroville, Calif.,

to authorize the sale of \$98,470 of securities without her knowledge and to buy two American Equity annuities with the money, according to the order. The Gentry Group, the American Equity Life Insurance Company and the saleswoman who sold the annuities were not authorized to conduct business as investment advisers in California, so the desist order was issued.

The Gentry Group did not return a phone call seeking comment. American Equity said that it was resisting the order in court.

Mary L. Schapiro, the vice chairwoman of N.A.S.D., said that her agency had proposed new rules related to the selling of annuities to the elderly; they await approval by the Securities and Exchange Commission.

"Some of the worst advertising we've seen has been in equity-linked annuities," she said, "very promotional, talking about growth without any risk, all the kinds of push-button expressions that really resonate with senior citizens." But, she said, she oversees only a small percentage of the firms and people selling these annuities.

Alas, not every retiree can rely, as the Aquinos did, on a daughter to help them steer clear of an investment they might later regret.