



# The Real Deal: Do You Know the True Cost of Your Group Variable Annuity?

I recently had the opportunity to provide a review to a prospective qualified retirement plan client. The plan assets were between 3 and 5 million and the underlying investments were separate accounts of a group variable annuity product. A variable annuity separate account will typically either invest its assets into a retail mutual fund or retain an outside money manager as a sub-advisor to manage the account's assets.

There are some professional advisors working in the retirement plan arena that have a rather strong bias against group variable annuity products when being used as funding vehicles for qualified retirement plans such as 401(k)s. I am not personally one of those who feel that they should never be used. I have seen situations where these solutions have been a good fit for the plan sponsor. With that being said, having investment options that are held within an annuity wrapper does not relieve plan sponsors of their responsibility to monitor the investment options that they are making available to their participants.

Additionally, because of how variable annuity products are packaged, it can be difficult to determine if there is a retail mutual fund being used as the underlying investment vehicle or if the insurance company sponsoring the product has retained an outside sub-advisor to manage the assets. In many cases there are recordkeeping and administrative fees that are also layered into the asset-based charges assessed against the plan. These asset based charges are removed prior to the calculation of the unit price of the

separate account investment option, making it tough for most plan sponsors to determine the true cost to their participants.

Again, I want to emphasize that I am not inherently against group variable annuity products but do feel that they require an additional level of diligence from the plan sponsor, particularly as the size of the plan grows. I have observed many situations where a group variable annuity product was justifiable and reasonable for a small or startup 401(k) but over time, as the plan assets increased, was no longer the best solution.

During the recent product review I conducted for our prospective client, I was able to identify the underlying retail mutual fund within most of the group annuity separate accounts. For those retail mutual funds where I could identify the specific fund being used, I matched that fund with the least expensive share class for that same fund on an open architecture platform.

I went on to demonstrate that the plan sponsor could have obtained many of the same investment managers, funds, etc. by using a recordkeeping solution that allowed them to go directly to the fund managers outside of that group annuity shell. The savings available for each fund compared was between 0.05% and 0.55%. In most cases the savings on a per fund basis exceeded 0.25%. **These small, incremental savings could add up to a meaningful amount over the course of the participants' years of investing for their retirement.**

Keep in mind, I was not attempting to show the client the best or most cost competitive solution in each asset class. I was simply attempting to demonstrate that the client could have obtained the very same investment option less expensively outside of the annuity wrapper. In many cases, further cost savings would have been available to the client when considering other no-load or institutionally priced investment options in the same asset class. Setting aside any considerations with respect to the fiduciary responsibility of a plan sponsor to make certain that the fees being assessed to their participants are reasonable, as a business person, if you can obtain the same service from the same provider 25 to 50% less expensively, why wouldn't you?

In conclusion, group variable annuity products are not inherently bad choices as 401(k) investment options. However, the plan sponsor should appreciate that these are packaged products built by insurance companies and the underlying investment options are not considered retail mutual funds, but are annuity separate accounts. Consequently, the underlying fees associated with each separate account should be compared to the fees for the same retail investment option. I have seen cases where the separate account was priced less expensively than the publicly traded mutual fund, but this is not normally the case.



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