Variable Annuities, Variable Insurance and Separate Accounts

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PART I: VARIABLE ANNUITIES AND VARIABLE INSURANCE

I. INTRODUCTION

The variable annuity is a novel retirement plan. It was devised to minimize the inadequacies of a fixed-dollar annuity as a retirement device. Inflation¹ and an accelerating standard of living have left persons receiving fixed-dollar annuities with only a fraction of the income required to meet their needs.

The variable annuity was the result of a study published by the Teachers Insurance and Annuity Association of America (TIAA) in 1951. The study showed that over a long period of time, the average performance of equity securities far exceeded the rise in the cost of living. This study led, in 1952, to the establishment of the College Retirement Equities Fund (CREF), a fund invested in equity securities in order to provide a variable annuity for its members.² Benefits under this annuity are not fixed-dollar amounts. They vary according to the investment performance of a fund; hence the name "variable" as distinguished from "fixed" annuity.³

The new concept greatly appealed to some, but by no means all, insurance companies. The industry was bitterly split between the advocates of variable annuities, led by Prudential Insurance Company of America, and the more conservative "establishment" life insurance companies, represented by Metropolitan Life Insurance Company.⁴

The split among life insurance companies is not new.⁵ For decades small

¹ The search for a hedge against inflation is continuing. The Occidental Life Insurance Company has produced an annuity tied to the U.S. Labor Department's consumer price index. Business Week, Nov. 23, 1968, at 126. See also Note, Commingled Trust Funds and Variable Annuities: Uniform Federal Regulation of Investment Funds Operated by Banks and Insurance Companies, 82 Harv. L. Rev. 435, 438 (1968).
³ Id. at 4. The TIAA continues to offer fixed-dollar annuities. It was recognized that the higher yield of equity securities might be offset by a higher risk to capital; therefore, not more than 50% of the total paid to both TIAA and CREF can be placed in CREF. Id. at 9-10. This was increased to 75% on January 1, 1967. G. Johnson & D. Grubbs, The Variable Annuity 15 n.9 (1967).
⁵ The split in the industry is manifested in its two organizations: The Life Insurance Association of America (LIAA) and the American Life Convention (ALC). The efforts of