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Empowering the Insured

# Guest Blog: Annuity Basics

There are good reasons why you might want or need to buy an annuity: You might want the tax-deferred growth they can offer. They can also provide a guaranteed income in retirement. In some cases, they can be used as an estate-planning tool. Over the years, annuity sellers keep increasing the commissions they pay to get agents to sell them.  This has led unscrupulous insurance agents to dream up all manner of schemes to get people who don't need one, into annuities.

It could be an invitation to a steak dinner at a nice restaurant. Maybe an offer for an inexpensive trust? Or perhaps your bank teller has suggested you talk with "that nice gentleman over there, he has much better ideas about CD and other things." Whatever the pitch, most anyone over 50 years old has bumped into someone who's tried to sell them an annuity.

So how do you know if an annuity is right for your financial goals? First, you should have a well-developed financial plan. Without that first step, knowing whether any investment product suits your needs isn't possible. If your current financial advisor hasn't or will not provide you with a plan, you should seek a new advisor. I suggest someone with a CFP® and also someone who will work with you as a fiduciary.

With a good plan, you can now determine the suitability of an annuity. The type of annuity chosen should fit in your financial plan and your advisor should be able to show you exactly why it works better than alternatives.

Ask questions to the selling agent and get answers in **writing**. "How much is your commission or acquisition fee?" "How long does the surrender period last?" "What exactly are the fees annually, in dollars, not percentages, please?" "What are my penalties for early withdrawal?" "What is my beneficiary's death benefit?" "Is my principle guaranteed?"
Here are the four most common annuities:

· **Fixed Annuities –** These annuities have no risk but also because of today's low-interest rates, no chance to truly utilize the main benefit of annuities- tax deferral. Be absolutely sure you understand the time frame and amount of penalties that would trigger on any withdrawals.   The only reason for this sort of annuity would be locking in a guaranteed income stream in the future as today's low-interest rates mean the tax deferral aspect becomes a very minimal advantage over more liquid but just as safe investments.

· **Equity Indexed Annuities –** Just don't buy this product. These annuities claim to tie return to an investment index, but with no risk. The way that works is always confusing for folks. Most people selling them don't even understand them. But they do understand how big their commission will be.

· **Variable Annuities –** This form of annuity is an investment, actually. Your return is based on stock or bond market performance. But unlike fixed annuities, your principal (original investment) is not guaranteed. In this arena, however, you can find products with very low fees, no surrender penalties and still have some guaranteed income. A good advisor can show you how such an annuity could work within your financial plan.

· **Single Premium Immediate Annuities (SPIA) –** Likely the most simple of them all. You give an insurance company your money and based on your life expectancy, they calculate a guaranteed income stream for you. Be aware that buying this annuity in today's historically low-interest-rate environment means you lock that rate for the life of the income.  That said, the income you will receive will not fluctuate. Placed in the proper financial plan, an SPIA can often help folks feel safe about their annual income needs and allow them to place other assets at more risk in order to generate better returns on other portions of their portfolio.

*This publication was written by retired financial advisor Matt Everson.  Matt volunteered with UP to help his Sonoma community recover from the devastating 2017 wildfires.*

For more on annuities, see [BACH TALK: Annuity "Whack-a-Mole"]