THE SOCIETY FOR FINANCIAL AWARENESS
DC Metropolitan Chapter www.dcsofa.org

The Truth About Annuities

2 Main Purposes of Annuities

Principle Protection/Accumulation

Deferred income annuities allow you to prepare for your retirement, helping you to create a future stream of income, while helping protect savings from loss.

Guaranteed Income

Immediate income annuities can offer peace of mind knowing that you have a source of guaranteed income that will last as long as you want, or as long as you live.

What Kinds Of Annuities Are There?

There are three basic types of annuities: fixed, variable and indexed. Here is how they work:

- **Fixed Immediate annuity. The insurance company promises you a minimum rate of interest and a fixed amount of periodic payments. Fixed annuities are regulated by state insurance commissioners. Please check with your state insurance commission about the risks and benefits of fixed annuities and to confirm that your insurance broker is registered to sell insurance in your state**

- **Variable annuity. The insurance company allows you to direct your annuity payments to different investment options, usually mutual funds. Your payout will vary depending on how much you put in, the rate of return on your investments, and expenses. The SEC regulates variable annuities**

- **Fixed Indexed annuity. This annuity combines features of securities and insurance products. The insurance company credits you with a return that is based on a stock market index, such as the Standard & Poor's 500 Index. Indexed annuities are regulated by state insurance commissioners**

VARIABLE ANNUITIES

ACTUAL CASH	GUARANTEED ACCOUNT
Initial Premium → \$100,000	Initial Premium → \$100,000
FEES 3.5% (M&E 1%, Rider Charge 1.5%, Mgmt 1%)	Bonus 8% +\$8000
FEES -\$3500	Income Rider (simple interest) 6.5% = \$6500
	Annuity Period 7 years
	\$100,000 x 6.5% x 7 yrs + bonus = \$153,000

VARIABLE ANNUITIES

Actual Cash Account Growth over 7 years

- **$100,000 growing 5% for 7 years**
- **Minus 3.5% in fees per year ?**

$110,984

VARIABLE ANNUITIES

Guaranteed Account Growth over 7 years

$100,000 x 8% bonus = $108,000

$108,000 x 6.5% (Guaranteed RoR) x 7 years = $157,140

Simple Interest?
OR
Compound?

VARIABLE ANNUITIES

CASH ACCOUNT	GUARANTEED ACCOUNT
$110,984	$157,140
- $3500 -> fees - $7857 -> G W/D - - $11,357	x 5% (withdrawal rate) $7857 Single? Or Joint?
∅ - 15 years	Lifetime

Equity Index Annuities

Guaranteed principle

Growth *(linked to an index, ex S&P500)*

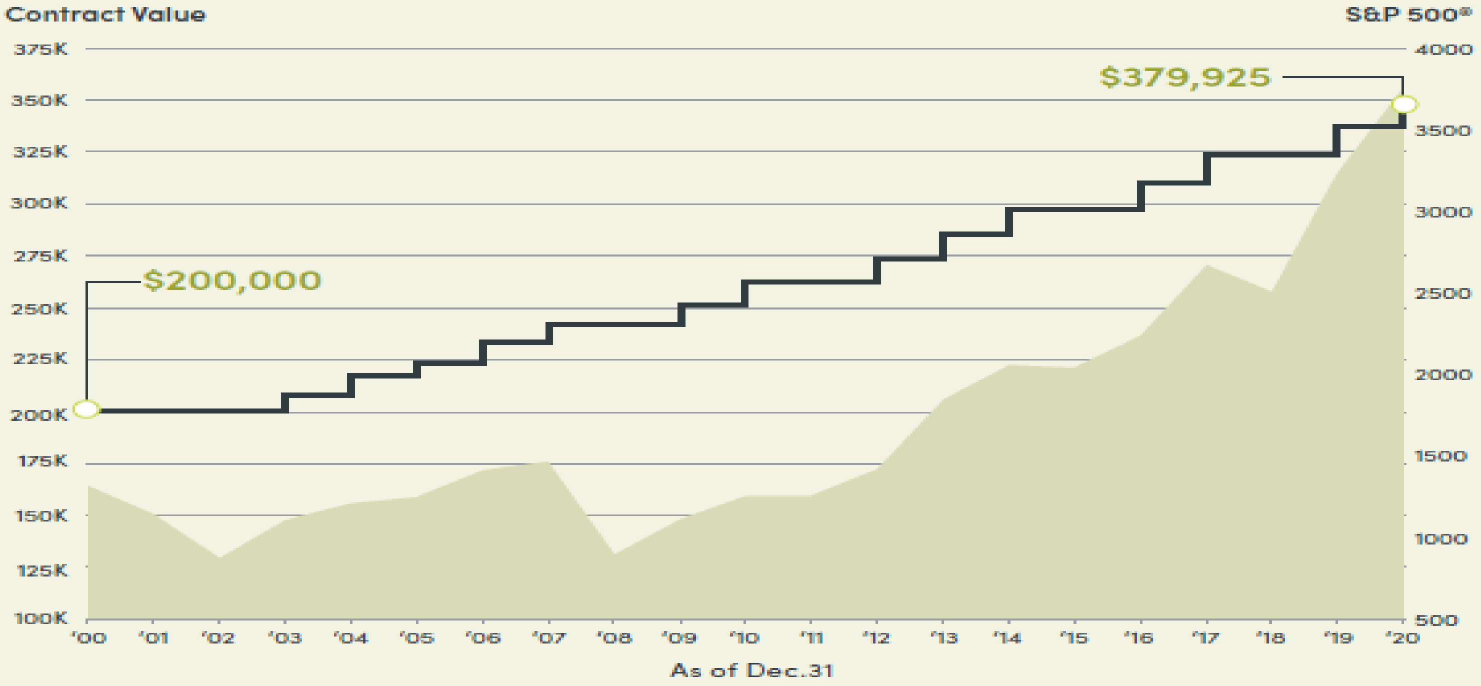
No Fees

Guarantees are subject to the claims-paying ability of the annuity issuer.

Annual Point to Point with Participation Rate

This assumes a Participation Rate of 30% throughout the 20-year time period.

Return Year	S&P 500® Index Return	% Credited to Contract
2001	-13.04%	0.00%
2002	-23.37%	0.00%
2003	26.38%	7.91%
2004	8.99%	2.70%
2005	3.00%	0.90%
2006	13.62%	4.09%
2007	3.53%	1.06%
2008	-38.49%	0.00%
2009	23.45%	7.04%
2010	12.78%	3.83%
2011	0.00%	0.00%
2012	13.40%	4.02%
2013	29.60%	8.88%
2014	11.39%	3.42%
2015	-0.73%	0.00%
2016	9.54%	2.86%
2017	19.42%	5.83%
2018	-6.24%	0.00%
2019	28.88%	8.66%
2020	16.26%	4.88%



Positive Index Return	In 2014 the Index returned 11.39%, so the credited interest would be 3.42%, the Index return multiplied by the 30% participation rate.
Flat or Negative Index Return	The following year, 2015, the Index return was -0.73%, so the interest credited to the contract would be $0. Since any previous interest credits are locked in, the contract value did not decline due to market losses.

In this example, at the end of 20 years, the contract has grown from the initial $200,000 to $379,925.

Main Purpose of Annuities

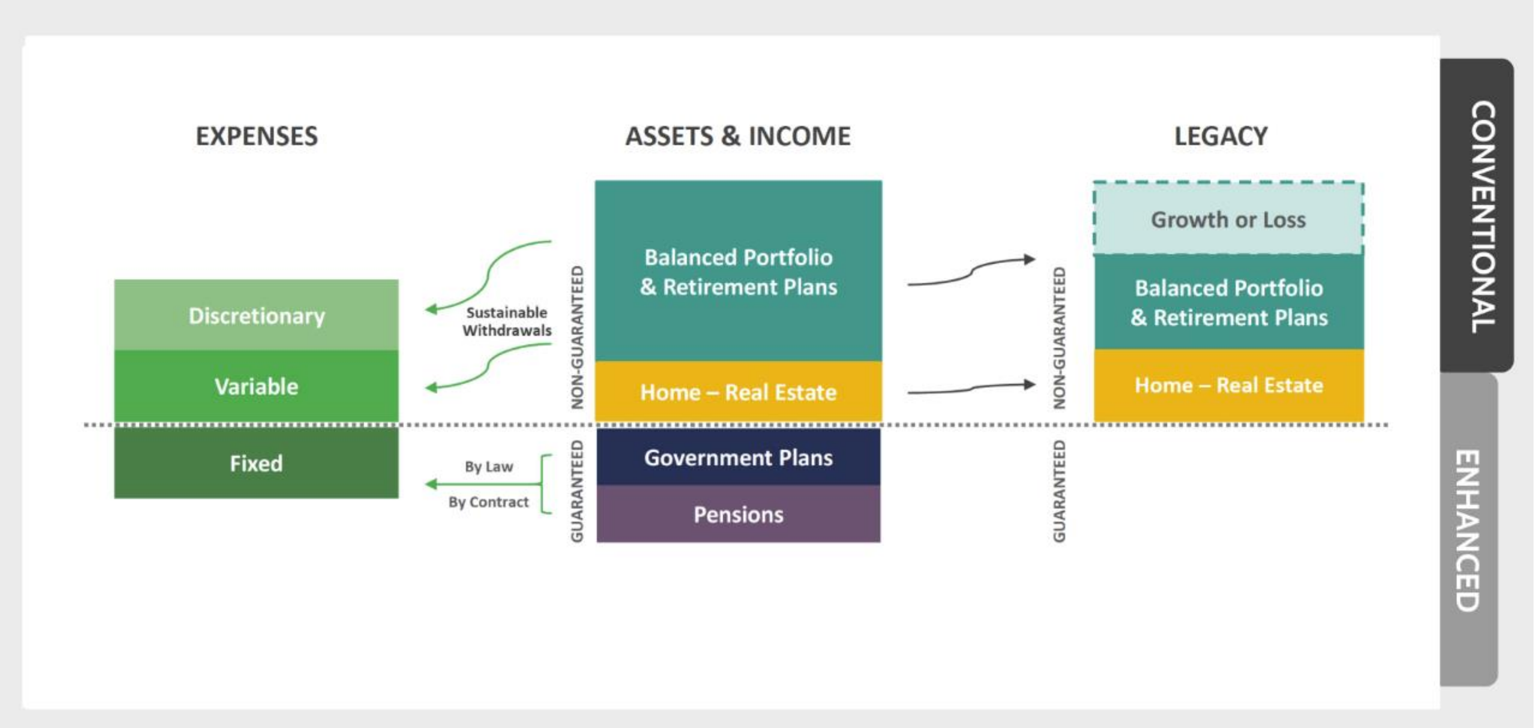
- ✓Principle Protection
- ✓Guaranteed Income
- ✓Max Income
- ✓Deferral
- ✓Legacy

Main Purpose of Annuities

Principle Protection

- Never Sell Low
- RMDs
  - TSP   U/D Issues
- IRA
  - RMD → Distribution Strategies

Conventional Retirement Approach



Portfolio

$500,000

20%	20%	10%	25%	25%	0%
C	S	I	F	G	
$100,000	$100,000	$50,000	$125,000	$125,000	$0
4%	4%	4%	4%	4%	0%
$4,000	$4,000	$2,000	$5,000	$5,000	$0

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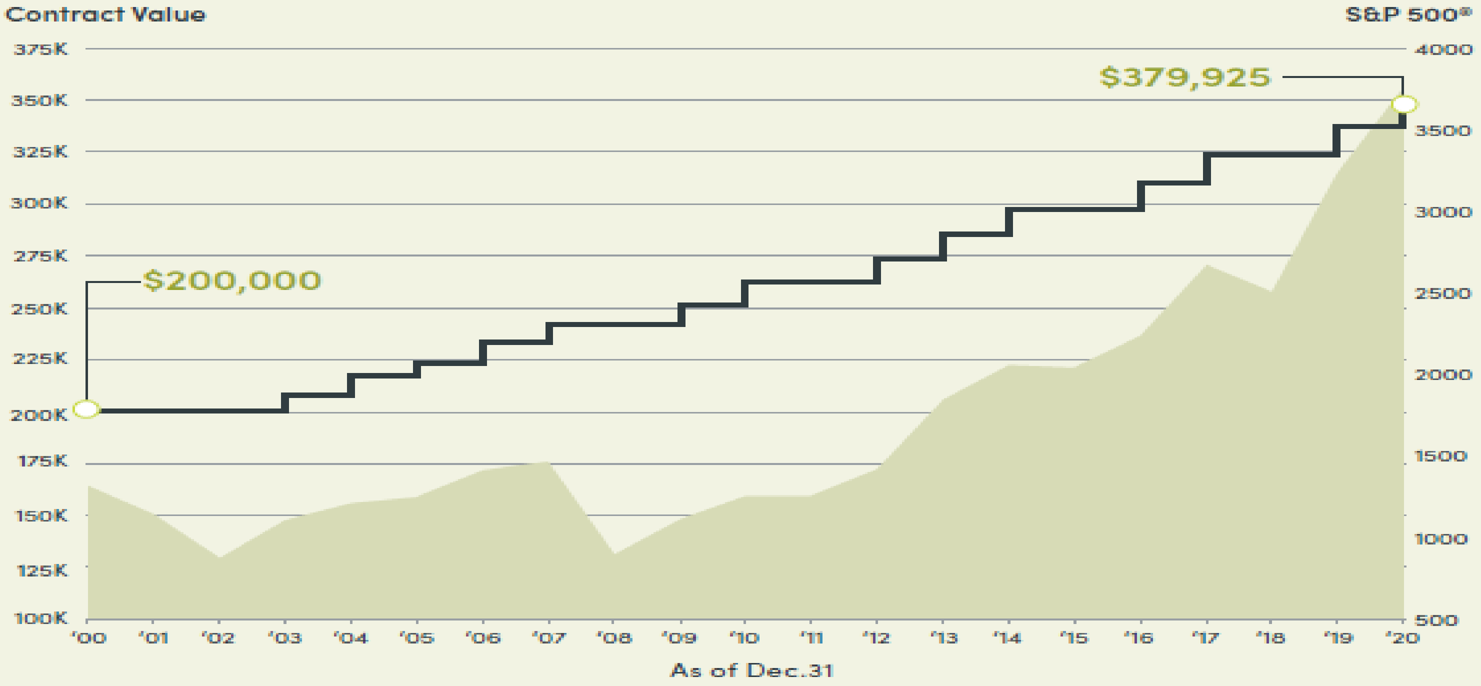

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Main Purpose of Annuities
Principle Protection

Below Median and Above Median Bond Return Environments (1927–2016)

	Below Median Bond Return Environments Average Return	Above Median Bond Return Environments Average Return	Overall Period Average Return
Long Term Gov't Bonds	1.87%	9.00%	5.43%
Large Cap Stocks	11.43%	9.84%	10.63%
FIA	4.42%	7.55%	5.98%
60/40 (Stocks & Bonds)	7.60%	9.50%	8.55%
60/20/20 (Stocks, Bonds & FIA)	8.12%	9.21%	8.66%
60/40 (Stocks & FIA)	8.63%	8.92%	8.77%

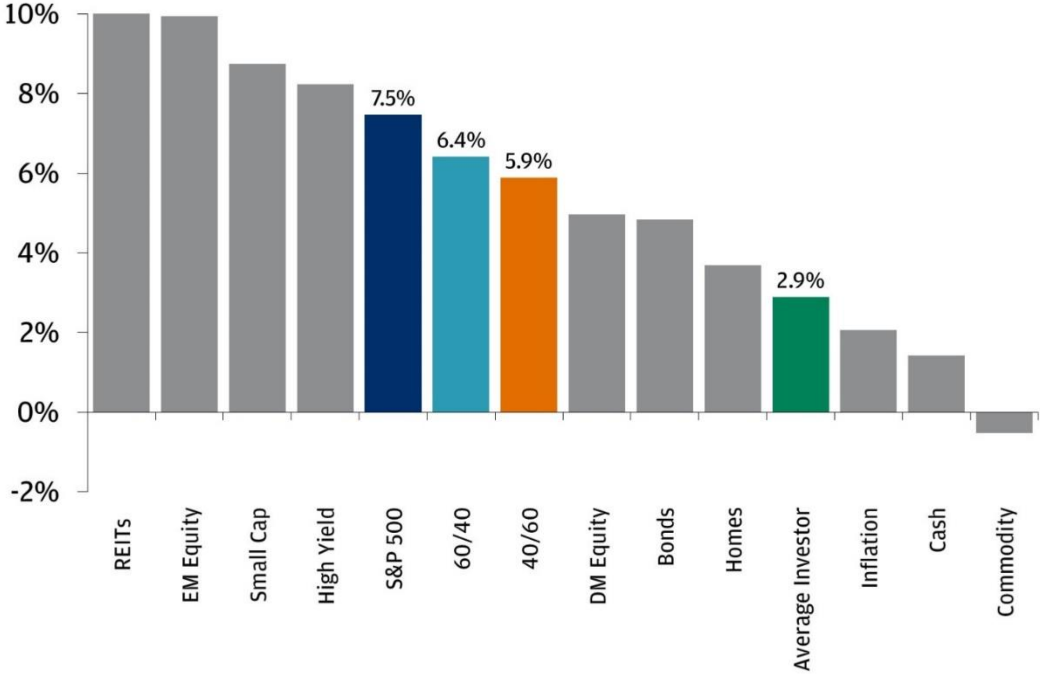
Source: 2017 SBBI Yearbook, Roger G. Ibbotson, Duff & Phelps; Zebra Capital; AnnGen Development, LLC

3.5%

Despite strong index returns over time, the "average investor" has underperformed a basic, indexed 60/40 portfolio by 3.5% annualized.

DIVERSIFICATION AND THE AVERAGE INVESTOR

20-year annualized return by asset class (2001 – 2020)



Source: DALBAR Inc., MSCI, NAREIT, Russell, J.P. Morgan Asset Management. Data as of December 31, 2020.

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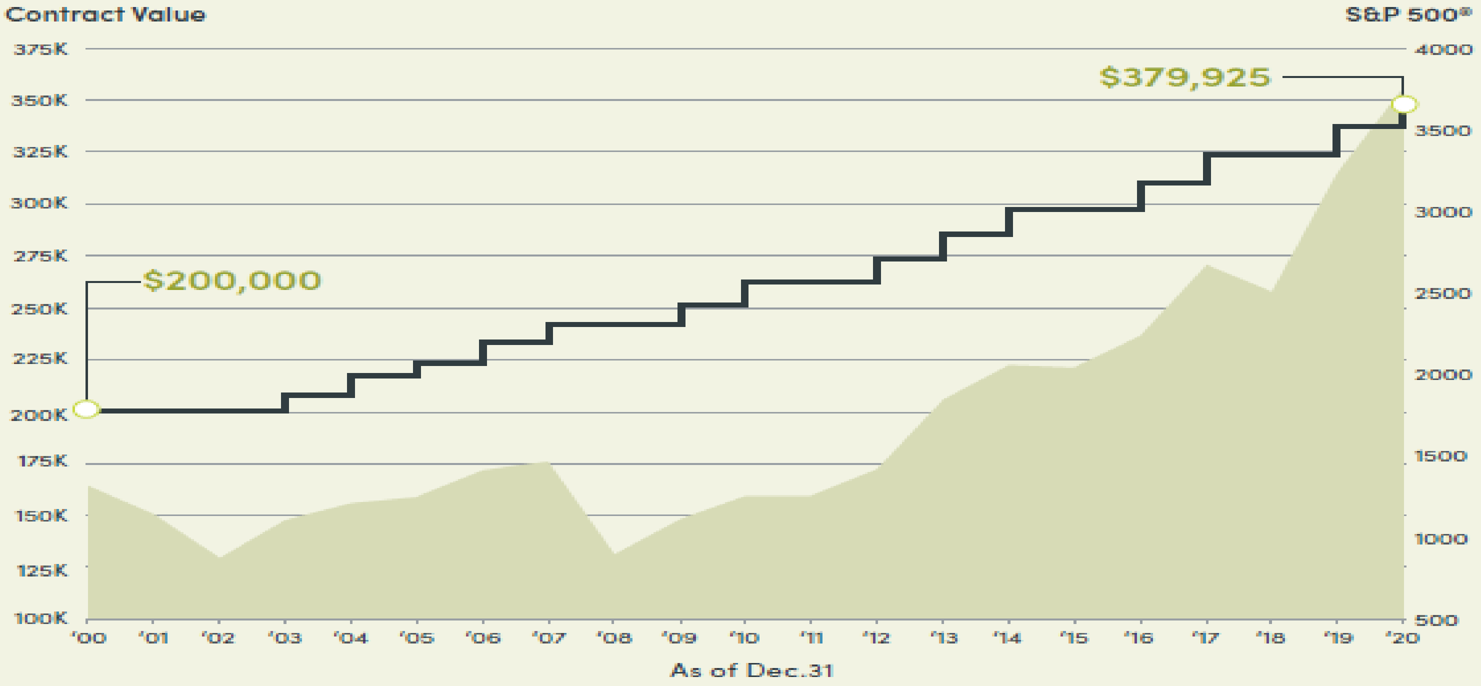

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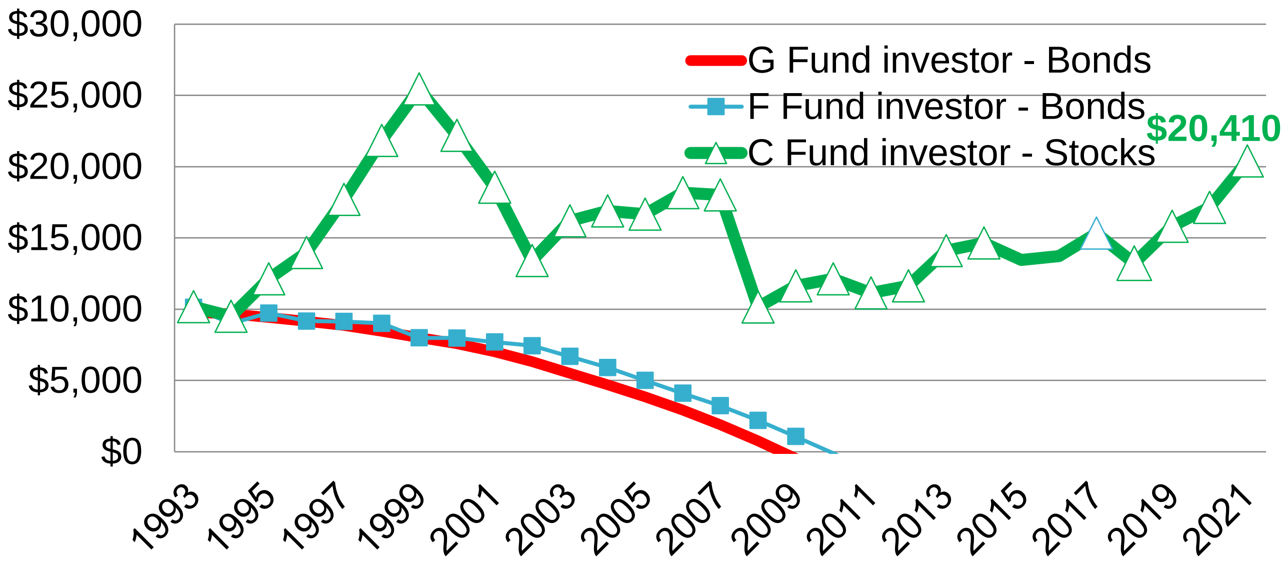
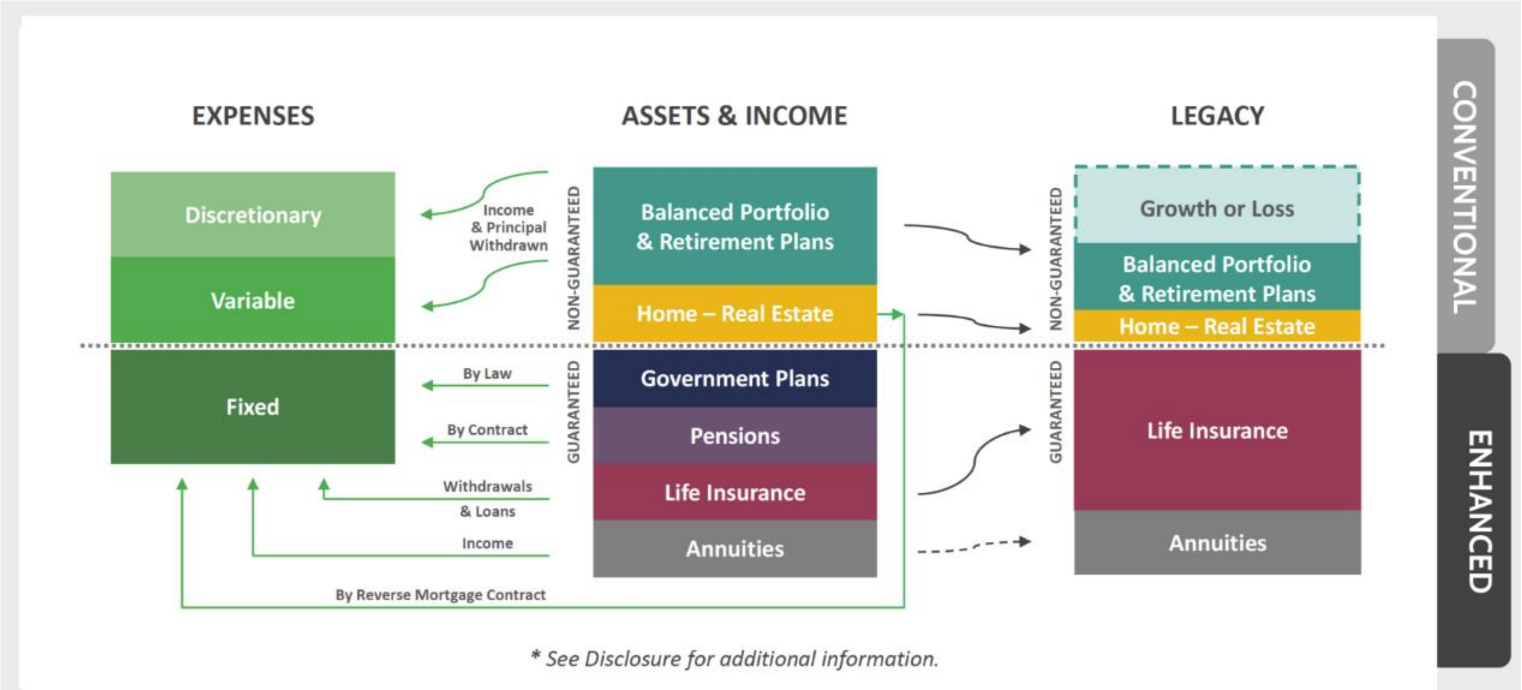
Loss of Purchasing Power:
What Happens When You Start Spending?

Example: At the beginning of 1993, retirees Bill, Jack and Mary each have $10,000 in the TSP. They each invest in one fund: Bill in G, Jack in F and Mary in C. They annually withdraw enough to buy 2000 first class stamps (after paying taxes of 30%).



Note: This is for illustration purposes only. Past performance is no guarantee of future performance. All investments involve the risk of loss. The data assumes reinvestment of all income.

Alternative Retirement Approach: Guaranteed Income



Main Purpose of Annuities

Guaranteed Income

A	B	
Traditional -> $500,000	$500,000	
x 4%	Annuity $300,000	$200,000
$20,000	$20,000	Your Choice Inflation * Growth * Long Term Care

Main Purpose of Annuities

Max Income

A	B
Traditional -> $500,000	$500,000
x 4%	$500,000 Annuity x 8%
$20,000	$40,000 -> Lifetime

Purpose of Money

But Theresa...

The story of JIM…

Main Purpose of Annuities

Deferral

5 years

<u>$100,000</u>

- Qualified
- Non-Qualified

Growth Deferred

Tax = Ordinary Income

Main Purpose of Annuities

Legacy

- Restricted Beneficiary Form
- Spousal **OR** Inherited IRA

Your own RMD Schedule based on age 70 ½ *RMD based on current age*

- Probate

Tax Consequences

- Income tax imposed at ordinary income tax rates on earnings portion of withdrawals or payouts
- Withdrawals are considered to be made from earnings first; annuitization payments are part return of principal and part earnings
- With certain exceptions, an additional 10% premature distribution tax imposed on distributions of earnings made prior to age 59½

Long-Term Care Annuity

A long-term care annuity is a deferred annuity that includes a long-term care rider.

A long-term care annuity is different from long-term care insurance:

- With long-term care insurance, you’re buying an insurance policy specifically for long-term care. You may pay an upfront premium or monthly premiums. Once you need long-term care, the policy can pay out monthly or on a lump-sum basis to help with those costs.
- Long-term care insurance doesn’t have the growth component that a long-term care annuity would.
- If you don’t need long-term care, you don’t get the premiums you paid back unless you purchase a return of premium rider.
- With a long-term care annuity, you could still receive annuitized payments even if you don’t use the long-term care rider’s benefits.

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