

Understanding Annuities vs. CDs



TURNER FINANCIAL

Annuities and CDs are similar because they are both financial vehicles with guaranteed rates of return based on interest rates. While annuities and CDs are similar in some ways, an annuity is generally designed to meet long-term financial goals and has several advantages:

Tax deferral

The interest credited to an annuity is completely untouched by current federal income tax during the accumulation period. As a result of tax deferral, interest is compounded and the investment grows at a faster rate. The owner pays no taxes on this interest until he or she begins to receive income payments or makes a withdrawal. Earnings on CDs are generally taxable in the year the interest is earned.

Liquidity

Annuities generally have provisions that allow the owner to withdraw some money penalty-free. Additionally, waivers may be available to allow owners with a terminal illness or extended care needs to withdraw all their money without penalty. CDs generally do not allow a similar level of liquidity.

Guaranteed income stream

Whether your client needs short-term, fixed period or lifetime payments, annuity settlement options can provide a guaranteed retirement income including options that can provide your client a stream of income for a fixed period or for a lifetime.

Interest rate guarantees

The interest rate an annuity earns will never fall below the minimum guaranteed interest rate, even if economic conditions cause interest rates to drop dramatically. The annuity contract, as a whole, will be credited with interest at an effective annual rate equal to or greater than that required by state law.

Here is a comparison of features of a typical fixed annuity and a typical CD:

	Annuity	CD
Tax-deferred growth	Earnings accumulate tax-deferred and are not taxable until they are withdrawn.	Earnings are taxable in the year the interest is earned, even if funds are not withdrawn.
Liquidity	Penalty-free withdrawals of a portion of the account value are typically available.	A penalty generally applies if funds are withdrawn prior to the CD's maturity date.
Avoidance of probate	Upon death, the annuity's death benefit is paid directly to the beneficiary(ies).	May be subject to probate.
Guaranteed lifetime income	Option is typically available.	Not available.
Loans	Available with many annuities.	Not available.
Extended care & terminal illness waivers	Waivers are typically available to allow withdrawal of all funds without penalty in certain situations.	Generally not available.

The comparison assumes that the CD is not held in a tax-qualified account.

Unlike a CD, surrender charges may apply to an annuity. Withdrawals and distributions may be subject to income tax and, for some tax qualifications, may be restricted. If withdrawals or distributions are taken prior to age 59½, a 10% federal penalty tax may apply. Also, annuities are issued by insurance companies and are not FDIC insured, while CDs generally are issued by financial institutions and are FDIC insured.

This information is not intended or written to be used as legal or tax advice. Clients should seek advice on legal and tax questions from an independent attorney or tax advisor.