EDUCATIONAL COMMENTARY

For consumers

THE MANY BENEFITS OF ANNUITIES MIGHT SURPRISE YOU

Annuities date back thousands of years to the Roman Empire. In fact, the word annuity is derived from the Latin annua, meaning "annual payment", and was used to describe the money paid to soldiers for their years of service. Benjamin Franklin included annuities for the cities of Philadelphia and Boston in his will. (The Boston annuity endured until 1993 when lawmakers voted to use the lump sum that remained.) In 2007, then Federal Reserve Chairman Ben Bernanke disclosed that his largest financial assets are annuities.

While the benefit of lifetime income remains a significant benefit of annuities, they have evolved dramatically in recent years to meet the increasingly complex needs of investors preparing for retirement. Annuities now span three basic categories—fixed, indexed and variable—and many can be customized to achieve your particular financial objectives.

But the one universal aspect of all annuities is that they can provide "protection" in retirement.

Today's annuities provide a wide variety of benefits. Here is a quick look at some of the most popular.

PROTECTED LIFETIME INCOME

Since pensions have virtually disappeared (only 15% of private sector workers have access to pensions today), and Social Security typically provides only 40% of your pre-retirement income—the steady income that annuities provide is one of the most unique and important benefits sought by investors. Many use the income to pay for such essential (i.e., non-discretionary) living expenses as a mortgage, utilities and groceries.

The great news is that we're all living much longer these days. Having certainty that you won't run out of money in retirement gives people confidence in the ability to live the life they want in retirement. Essentially, annuities deliver cash flow that you can rely on for either a predetermined period of time or for the rest of your life. Deferred income annuities, for example, let you lock in a stream of protected income years before retirement, while reducing the effect of market volatility on your retirement income plan.

PROTECTED GROWTH

The ability to limit the downside risk of an investment, while still providing upside benefits—also known as stop-loss strategies—has long been favored by investors active in the stock market. Some deferred annuities—such as variable and indexed variable annuities, designed for people who want to take advantage of both income protection and growth—provide a similar benefit, allowing you to create a retirement plan that provides some protection from market declines while allowing you to capture gains from your investment.

Fixed indexed annuities, a type of deferred annuity, also offer the opportunity for growth based on a market index. The growth is typically capped at a certain level which may be less than the actual market gains achieved by the index, in exchange for protecting your principal investment. Both variable and fixed indexed annuities may also offer optional lifetime income benefits.

PROTECTED INITIAL INVESTMENT

As an optional benefit, many annuities offer the ability to protect your principal, where the initial money you've invested is not at risk due to market losses. This is a real benefit for those looking to improve their potential returns through the various types of investment options available within these annuities. The opportunity to seek higher returns while limiting downside losses is an attractive feature for many investors.

TAX-DEFERRED EARNINGS

A smart retirement portfolio weighs the potential impact of the many types of taxes that can affect your nest egg and income in retirement, including capital gains and ordinary income tax obligations. A

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Morningstar analysis found that, on average, over a 93-year period ending in 2019, investors gave up about two percentage points of their annual returns to taxes.

All annuities offer tax-deferred growth, meaning taxes aren't paid on the assets or investment gain in an annuity until they're withdrawn. In this way, the tax treatment of annuities is similar to other tax-advantaged accounts like a 401(k) or IRA, with one big difference: there is no cap on how much you can invest in a non-qualified annuity or income limitation to consider. You can fund an annuity with pre-tax money—in which case tax would be due on the original investment and any gains, when withdrawn—or after-tax money—in which case you would only pay tax on investment gains.

The benefit of tax deferral can be immense, allowing your investment to compound tax free from investment growth, dividends and interest for decades, enhancing your investment and potential retirement income.

PROTECTED ASSETS

A common estate objective is to shelter assets from prying eyes—preventing a nosy aunt from learning what you bequeathed to a favorite nephew, for example—as well as unnecessary tax obligations. Insurance companies will work with you to create custom contracts that specify payout and beneficiary options to achieve these and other objectives that are important to you.

Because annuities are insurance contracts, and therefore not subject to probate, they can protect your estate's assets from public disclosure and taxation. Annuities can also be used to protect assets from creditors. In Florida and Texas, for example, annuities can be used to shield estate assets from creditors and even lawsuits.

PROTECTED FAMILY BENEFITS

Another common estate objective is to leave financial assets to one's loved ones or other beneficiaries. You can use an annuity, for example, to leave a legacy, including the only gift guaranteed to keep on giving for the lifetime of your designated beneficiary. Annuities can be customized to help pay for the living expenses of your child with special needs or your grandchild's college education, while avoiding the burdens arising from probate.

Annuities offer other benefits as well. Annuities don't have annual contribution limits, so you can use them to make unlimited contributions to make up ground in your retirement savings. They can also guard against the risk of having to manage your finances amid cognitive decline, among other pitfalls related to deteriorating health late in life.

The evolution of annuities—and the variety of benefits they now provide—explains why they are a mainstay in the retirement portfolios of tens of millions of Americans. They offer many opportunities and solutions that are unique to annuities and can play an important part in a truly diversified retirement portfolio today. To learn more about annuities and their potential benefits to you, speak with the right financial professional who can show you how.

Annuities are long-term investments designed for retirement purposes. The value of variable annuities is subject to market risk and will fluctuate. Product guarantees are subject to the claims-paying ability of the issuing insurance company. Earnings, when withdrawn, are subject to federal and/or state income tax, including a 10% tax penalty for withdrawals before age 59½. Some income guarantees offered with annuities take the form of optional riders and carry charges in addition to the fees and charges associated with annuity products.

There is no guarantee that any investment will achieve its objectives, generate positive returns, or avoid losses. Investments in annuity contracts may not be suitable for all investors.

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