

Annuities

For the Sacramento Bogleheads

Mel Turner

Four Important Annuity Points

- Insurance products, **not** investments.
- Protections can be expensive.
- Many are complicated long-term contracts.
- No bad annuities, just bad salesmen.

History of Annuities

1500 Churches
Designed Annuities
for Profit

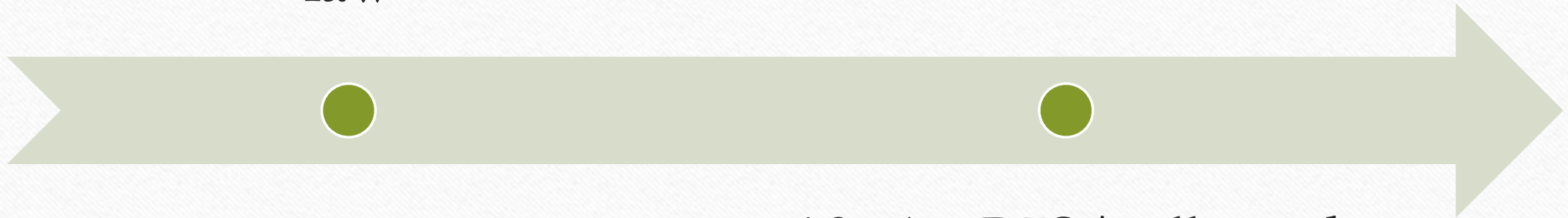
1953 TIAA-CREFF
Offered First
Modern Annuity

1929 Stock Market
Crash



History - continued

1958 403(b) becomes
law



1974 ERISA allowed
mutual funds in 403(b)

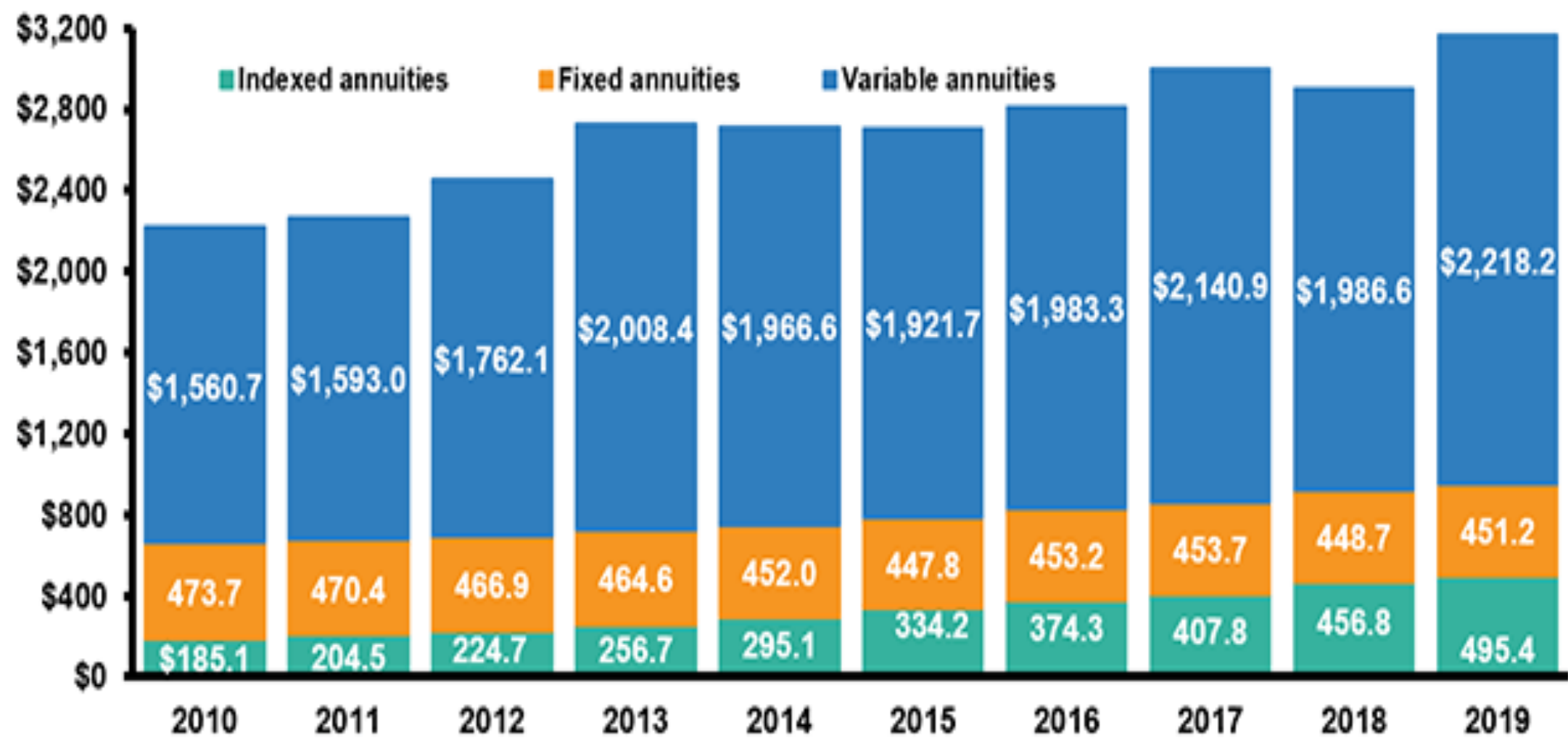
State of the Industry

- Assets in Annuities
 - \$2 Trillion+ in Effect
 - \$240+ Billion in sales in 2019-record year
 - 75% of Sales are in Deferred Variable and Index Annuities

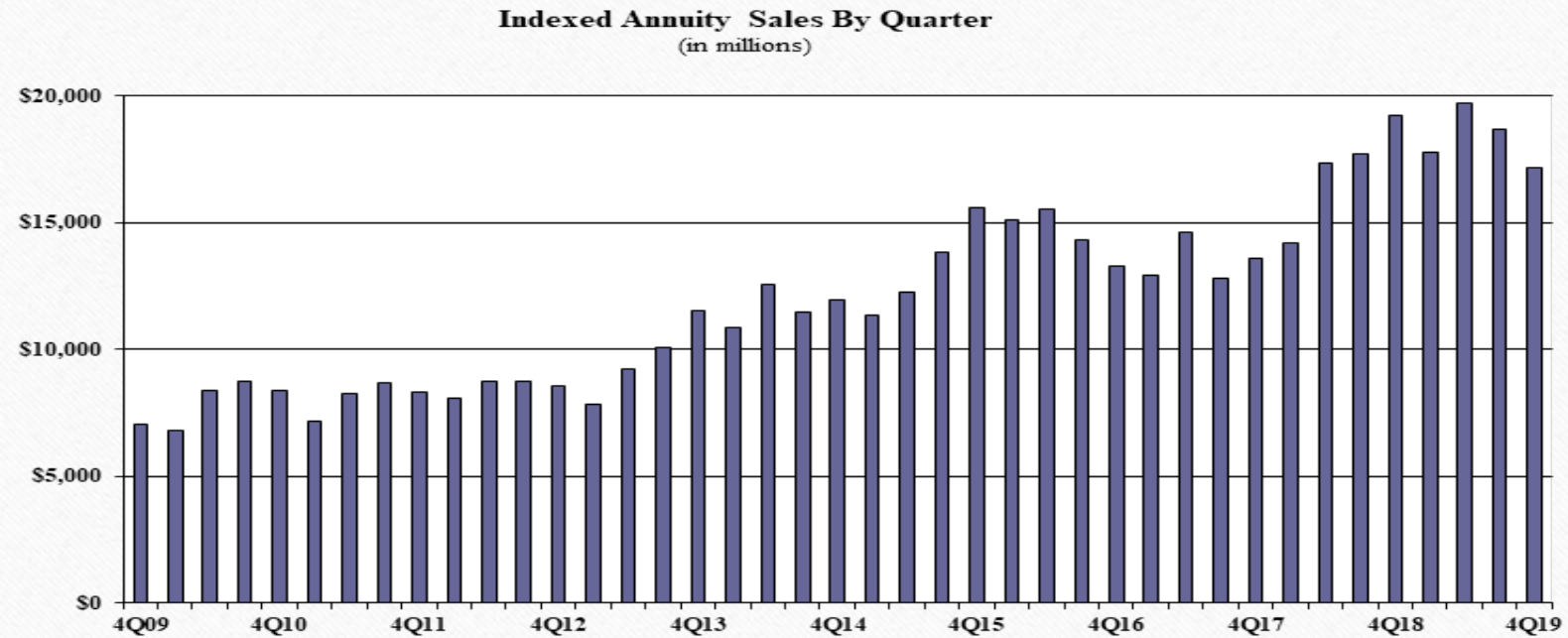
A few words about the Fiduciary Rule







Index Annuity Sales 4Q09-4Q19



U.S. Individual Annuity Sales

2019 (\$ in thousands)

Rank	Company name	Total	Company name	Variable	Company name	Fixed
1	Jackson	19,626,719	Jackson	14,693,766	AIG Companies	13,264,328
2	AIG Companies	19,419,511	Equitable Financial	11,697,921	New York Life	9,863,105
3	Lincoln Financial Group	14,837,778	TIAA	9,858,000	Allianz Life of North America	8,368,418
4	New York Life	13,239,522	Lincoln Financial Group	9,752,988	Global Atlantic Financial Group	8,292,011
5	Allianz Life of North America	12,369,631	Prudential Annuities	8,523,711	Athene Annuity & Life	6,766,852
6	Equitable Financial	11,734,276	AIG Companies	6,155,183	Pacific Life	6,194,836
7	Nationwide	10,809,100	Brighthouse Financial	5,767,867	Nationwide	6,114,900
8	Prudential Annuities	10,477,707	Nationwide	4,694,200	Lincoln Financial Group	5,084,791
9	TIAA	9,858,000	RiverSource Life Insurance	4,086,723	Massachusetts Mutual Life	5,079,675
10	Pacific Life	9,511,941	Allianz Life of North America	4,001,212	American Equity Investment Life	4,963,206
11	Global Atlantic Financial Group	8,397,573	Transamerica	3,633,533	Jackson National Life	4,932,953
12	Athene Annuity & Life	6,782,132	New York Life	3,376,417	Great American	4,545,638
13	Brighthouse Financial	6,157,641	Pacific Life	3,317,105	Fidelity & Guaranty Life	3,595,367
14	Massachusetts Mutual Life	5,544,547	Thrivent Financial for Lutherans	2,291,067	Symetra Financial	3,497,556
15	American Equity Investment Life	4,963,206	Fidelity Investments Life	1,545,727	Principal Financial Group	2,890,424
16	Great American	4,649,120	Northwestern Mutual Life	1,045,025	Western Southern Group	2,838,241
17	RiverSource Life Insurance	4,435,381	CMFG Life Insurance Company	998,448	Security Benefit Life	2,540,018
18	Transamerica	4,196,306	Principal Financial Group	568,663	Delaware Life	2,405,953
19	Symetra Financial	3,622,527	Massachusetts Mutual Life	464,872	Midland National	2,257,659
20	Fidelity & Guaranty Life	3,595,367	Securian Financial	364,198	North American Company for Life and Health	2,216,537
	Top 20	\$184,227,984		\$96,836,625		\$105,712,466
	Total industry	\$241,727,000		\$101,900,000		\$139,827,000
	Top 20 share	76%		95%		76%

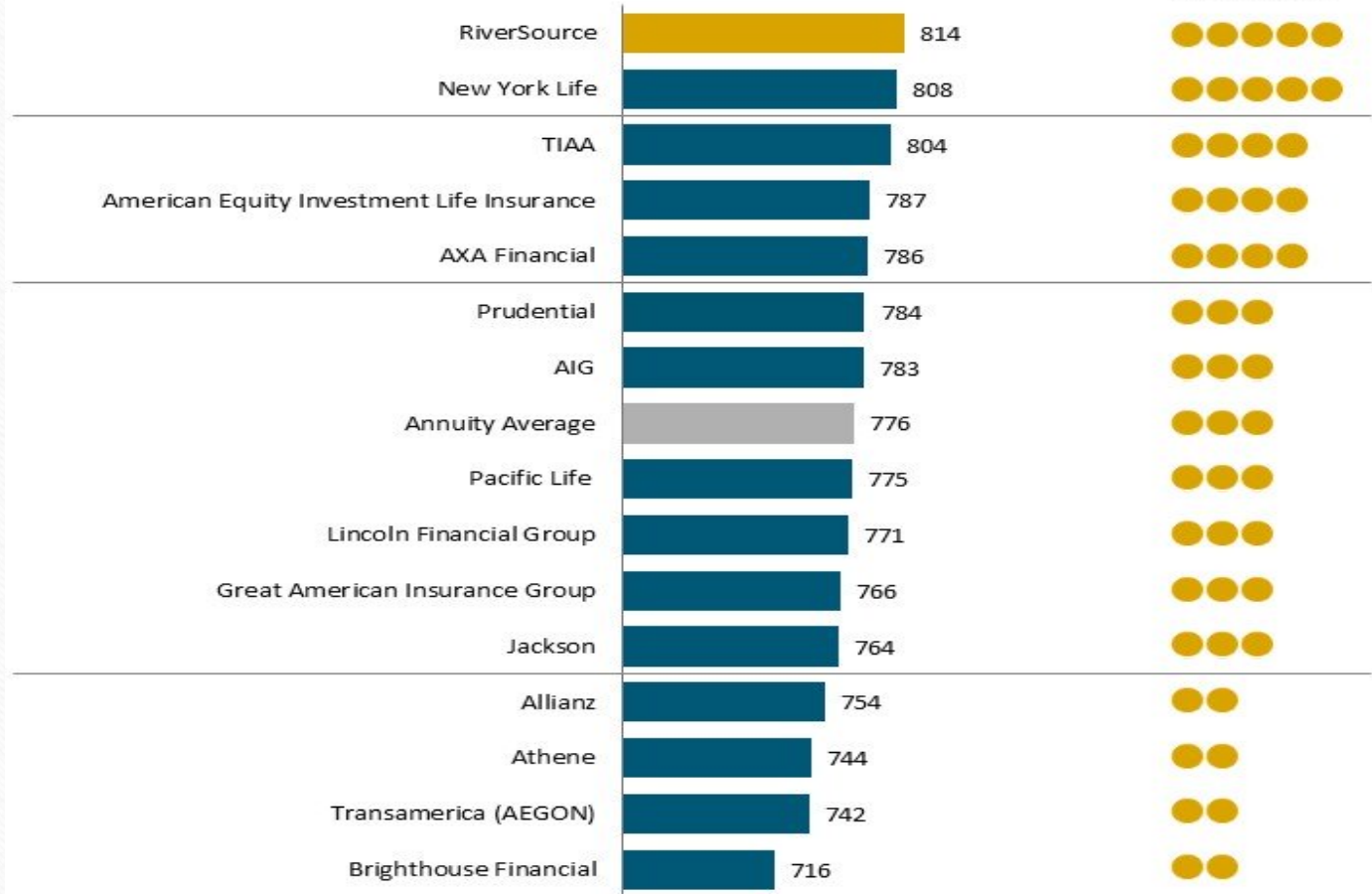
Source: Secure Retirement Institute® U.S. Individual Annuities Sales Survey

J.D. Power 2019 U.S. Life Insurance StudySM

Overall Customer Satisfaction Index Ranking Annuity

(Based on a 1,000-point scale)

JDPower.com
Power Circle RatingsTM
for consumers:



Power Circle Ratings Legend

Among the best
 Better than most
 About average
 The rest

Note: Included in the study but not award-eligible due to small sample size is Midland National Life.

Source: J.D. Power 2019 U.S. Life Insurance StudySM

Charts and graphs extracted from this press release for use by the media must be accompanied by a statement identifying J.D. Power as the publisher and the study from which it originated as the source. Rankings are based on numerical scores, and not necessarily on statistical significance. No advertising or other promotional use can be made of the information in this release or J.D. Power survey results without the express prior written consent of J.D. Power.

How Are Annuities Constructed

- Actuaries with Large Data Pools
- Developed. $A+B+C+D+E$ + **Profit Margin** = Cost
- Contract can be modified with Rider...at added Cost

How Annuities Are Regulated

- **If no securities involved** – (SPIA, Deferred Fixed, Fixed Rate, QLAC, Fixed-Index Annuities)
Regulated by State Insurance Commissioner
- **If securities involved** – (Variable Deferred Annuities)
Regulated by SEC and FINRA

Protections from Default

- State Guaranty Association will pay claims
- Coverage varies from state to state
 - \$100K to \$500K (CA covers 80% of \$250K)
- Coverage provided in the current state of residence

Asset Protections

Asset Protection from Bankruptcy and Litigation

1. Retirement Plans (Most states, but varies)
2. Homestead Exemption (Depending on state)
3. Cash Value of Life Insurance Plans
4. **Cash Value & Payouts of Annuities**

Annuity Commissions

- Highest commission = worst product and most difficult to sell.

SPIA	1% - 3%
Deferred Fixed Income	2% - 4%
Deferred Variable	4% - 7% with 1% Tail
Fixed Index	6% - 8%

1035 Exchange

- SPIAs, Deferred Income and QLAC **not** transferable
- VAs, MYGAs and FIAs are transferable
- Possibly starts a new surrender period
- New Annuity must be mathematically and contractually better
- Different company may not accept

Taxation

- **Qualified Account** (TIRA, 401(k), 403(b), etc.) – Fully Taxable
- **Non-Qualified** – Calculate ‘Exclusion Percentage’ based on IRS PUB 939 (or TurboTax, etc.). Different calculation for:
 1. Fixed Period
 2. Single Life
 3. Joint and Survivor
 4. Variable
 5. Disability

Taxation - continued

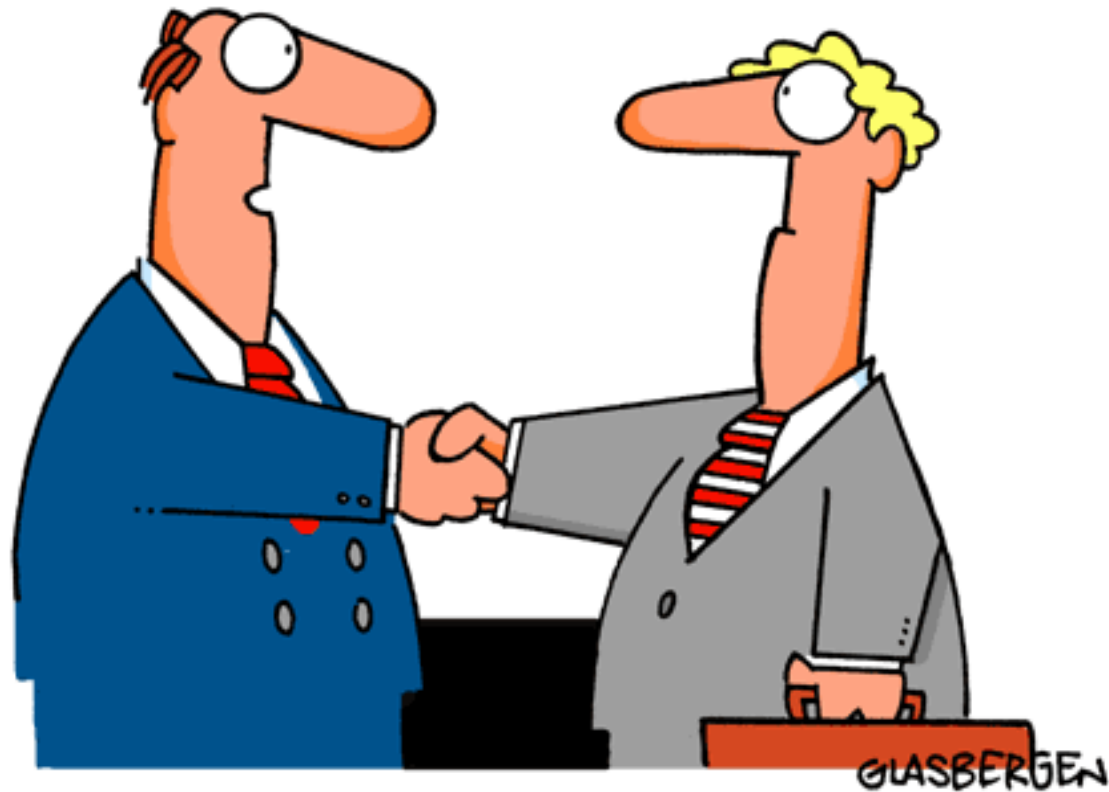
- Portion will be taxable (earnings)
 - Turned possible LTCG into ordinary income
- Portion will be non-taxable (return of premium)
 - Until principal is returned then 100% taxable
- **If inherited there is no “step-up” in cost basis**

Where to Buy?

- SPIA – Least Complicated
 - Compare quotes at immediateannuities.com
 - Fidelity, Schwab, Agent
- VA's – More Complicated
 - Start with Fidelity, Schwab

(Vanguard is out of the business starting June 2019)

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www.glasbergen.com



“You’re a pretty good sales rep, except for the nine times you called me ‘wallet’ instead of ‘Walter’.”

How They Are Sold

- Scare ‘em
- Shame ‘em
- Confuse ‘em
- Wait for it...
- Game over!

Should set off BS monitor

*8% Guaranteed growth

*Upfront Bonus

*Market upside - no downside

*Too good to be true

“Free look in CA is 30 days”



" WE HAVE A WIDE RANGE OF
ANNUITIES "

Four Basic Types Of Annuities

Immediate

Fixed

Variable

Deferred

Fixed

Variable



Immediate

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graph TD; Immediate[Immediate] --- Fixed1[Fixed]; Immediate --- Variable1[Variable]; Deferred[Deferred] --- Fixed2[Fixed]; Deferred --- Variable2[Variable];
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The diagram is a hierarchical tree structure. At the top level, there are two orange rounded rectangular boxes: 'Immediate' on the left and 'Deferred' on the right. From the bottom of the 'Immediate' box, a vertical line descends and then branches into two horizontal lines. These lines connect to two green rounded rectangular boxes: 'Fixed' (top) and 'Variable' (bottom). The 'Fixed' box has a thick black border, while the 'Variable' box has a thin green border. Similarly, from the bottom of the 'Deferred' box, a vertical line descends and branches into two horizontal lines connecting to two green rounded rectangular boxes: 'Fixed' (top) and 'Variable' (bottom). Both boxes in this branch have thin green borders. The entire diagram is set against a light gray background within a white frame, which is itself on a textured brown surface.

Fixed

Variable

Deferred

Fixed

Variable

Immediate Fixed

- SPIA/Income Annuity
- Person makes lump sum, “single premium”
- Insurance contract starts payments within year
- Match payout to needs - lifetime, joint, period certain

Immediate Fixed Advantages

- Income is a known quantity, makes planning easier
- Protects against poor returns and outliving assets
- Higher annual payout than stock/bond portfolio due to mortality credits
- Some offer one-time partial withdrawal
- Avoids probate

Immediate Fixed Disadvantages

- It's no longer your money.
- No inflation protection (Principal last to offer COLA stopped in 4Q 2019). In 2018 only 4% had step-up COLA but you take a 28% haircut, ex. \$650 to \$468. Remember, Inflation was 13.5% in 1980.
- Die before life expectancy
- Majority of payout is ordinary income (review taxation)
- At end of exclusion period (life expectancy) it is all ordinary income

Why Buy Immediate Fixed Annuity

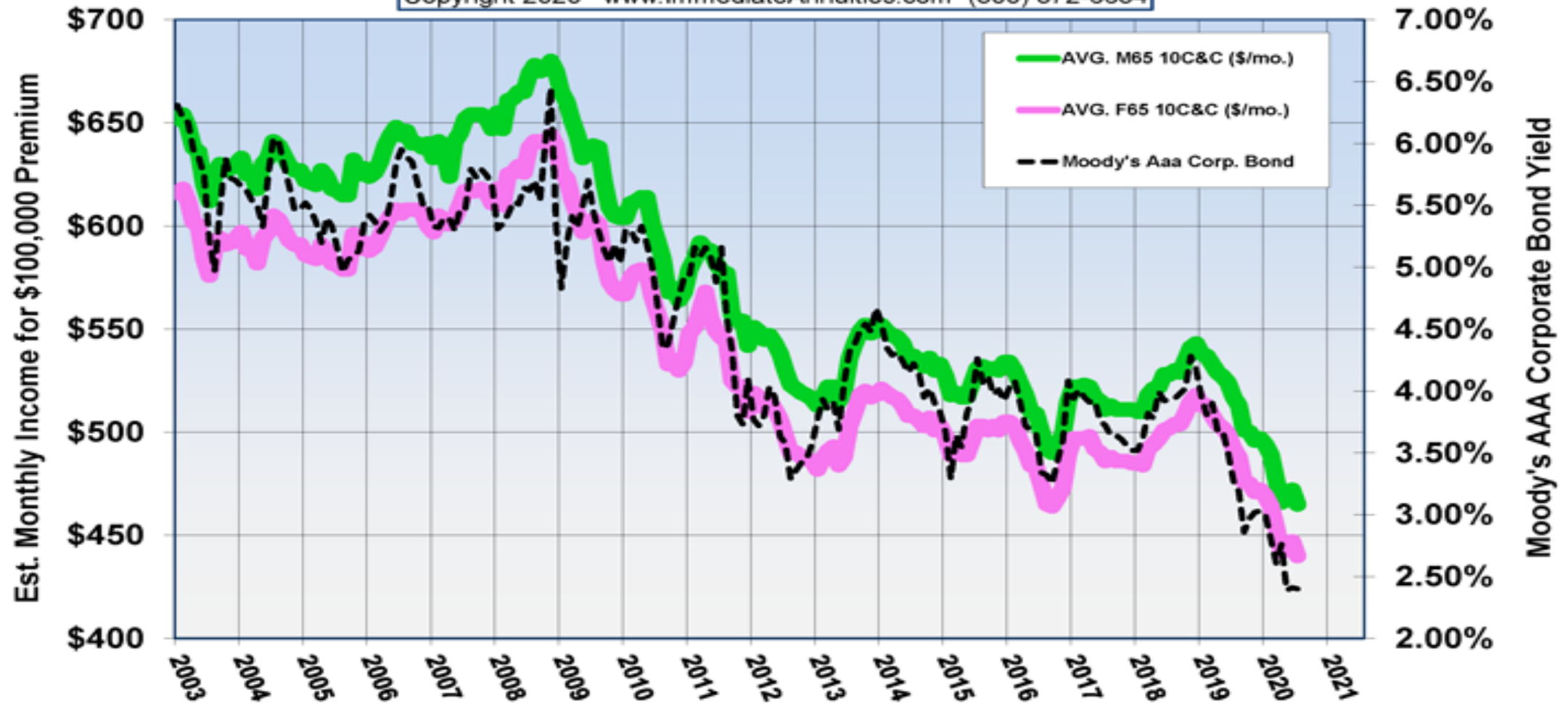
- Fear of depleting assets
- Simplifies a portion of planning and investing
- Peace of mind knowing it will always be there
- Easy to shop for

Immediate Fixed Considerations

- Never annuitize entire investment assets
- Consider staggering annuities
- Annuitize less if legacy is important
- Delay to receive larger payout
- Consider delaying Social Security because of COLA

Male 65 / Female 65
Life & 10 Years Certain Annuity Rates
and Moody's AAA Corporate Bond Yield
Updated July 2020

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Immediate

Fixed

Variable

Deferred

Fixed

Variable



Deferred Fixed Annuity

- Multi-Year Guaranteed Annuity
- Longevity Annuity

Multi-Year Guaranteed Annuity

- Replacement for CD with a Surrender Charge
- Taxed Deferred
- Interest compounds
- Not FDIC insured
- Withdraw 10% penalty free
- Have beneficiary if die but Surrender Charge applies
- Examples on ImmediateAnnuity: 5-10 year @ 3.0-3.5%

Sentinel Security Life Personal Choice Annuity 5 (MVA)	5 yrs.	\$2,500	**3.35 %	B++	Get My Quote
Fidelity & Guaranty FG Guarantee-Platinum 5 Annuity (MVA)	5 yrs.	\$20,000	2.90 %	A-	Get My Quote
Oxford Life Multi-Select 5 (MVA)	5 yrs.	\$20,000	2.75 %	A-	Get My Quote
Guggenheim Life and Annuity Preserve MYGA 5 High-Band (MVA)	5 yrs.	\$250,000	2.70 %	B++	Get My Quote
Guggenheim Life and Annuity Preserve MYGA 5 Low-Band (MVA)	5 yrs.	\$10,000	2.60 %	B++	Get My Quote
Delaware Life Pinnacle MYGA 5 (MVA)	5 yrs.	\$10,000	2.55 %	A-	Get My Quote
Midland National Life Guarantee Ultimate 5 High-Band (MVA)	5 yrs.	\$100,000	2.50 %	A+	Get My Quote
North American Guarantee Choice 5 High-Band (MVA)	5 yrs.	\$100,000	2.40 %	A+	Get My Quote
American National Palladium MYG 5 High-Band (MVA)	5 yrs.	\$100,000	*2.30 %	A	Get My Quote
American National Palladium MYG 5 Low-Band (MVA)	5 yrs.	\$5,000	*2.20 %	A	Get My Quote
Midland National Life Guarantee Ultimate 5 Low-Band (MVA)	5 yrs.	\$10,000	2.20 %	A+	Get My Quote
Equitrust Life Certainty Select 5 (MVA)	5 yrs.	\$10,000	2.10 %	B++	Get My Quote
North American Guarantee Choice 5 Low-Band (MVA)	5 yrs.	\$10,000	2.10 %	A+	Get My Quote
American General VisionMYG 5 High-Band (MVA)	5 yrs.	\$100,000	2.00 %	A	Get My Quote
American General VisionMYG 5 Low-Band (MVA)	5 yrs.	\$10,000	1.70 %	A	Get My Quote
New York Life Secure Term MVA II 5 High-Band (MVA)	5 yrs.	\$100,000	1.60 %	A++	Get My Quote
Lincoln National MYGuarantee Plus 5 High-Band (MVA)	5 yrs.	\$100,000	1.05 %	A+	Get My Quote
Lincoln National MYGuarantee Plus 5 Low-Band (MVA)	5 yrs.	\$10,000	1.00 %	A+	Get My Quote
Minnesota Life SecureOption Choice 5 High-Band (MVA)	5 yrs.	\$100,000	**1.00 %	A+	Get My Quote
Minnesota Life SecureOption Choice 5 Low-Band (MVA)	5 yrs.	\$25,000	**1.00 %	A+	Get My Quote

Deferred Fixed

- Often called “Longevity Insurance” or Deferred Income Annuity
- Pay premium, interest accumulates, receive fixed amount
- Will often come with Bonuses along the way
- Interest often guaranteed 3-10 years
- 10% withdrawal penalty free, penalty prior to 59 ½
- Method of tax-deferral and *usually* no amount limit

Deferred Fixed Considerations

- Allows smaller premium for same level of coverage
- Most have guaranteed death benefit for beneficiary
- Best example is Social Security
- Address Qualifying Longevity Annuity Contract (QLAC), 2014
 - Purchased inside TIRA, Reduces RMD, 25%/\$135K, No variable or index annuity
 - Single or Joint Life only(or cash) and delay up to age 85

Immediate

Fixed

Variable

Deferred

Fixed

Variable



Deferred Variable_(1950s)

- Comparable to a tax-deferred mutual fund wrapped in an insurance policy. All other tax-preferred options should be funded first.
- Contract is complex and can be hundreds of pages with supplements. ~~Most~~ people don't know what they've bought.
- These are sold – not bought.
- Has high ongoing internal expenses but no contribution limits.
- Has two Phases: Accumulation Phase and Distribution Phase

Deferred Variable Accumulation Phase

- Mutual fund portion are called sub-accounts which frequently have AA limits.
- Account value rises and falls with sub-accounts. You can lose money!!
- Sub-accounts can be sub-par due to high ER (avg .97%) and activity, 12b-1 fees. Some even have front loads.
- There are many fees associated.
 - Administrative fees of flat fee (typical \$50yr) or %
 - Mortality and Expense Risk Fee (life insurance/admin) average is 1.25%, varies by age
 - Surrender Fees typically 7%-8%. I've seen 14yr/10%. Govt study says up to 20%.
 - Riders. Increased fees for each benefit. Always in Insurance company favor.

VA Accumulation Phase – cont.

- You are primarily buying protection and secondarily an investment
- According to 2012 Morningstar study average expenses = 2.44%
- Common to see VA internal expenses in excess of 3.00% annually. Takes 10 years minimum to recover costs, most say 20 years.
- Typically can withdraw 10%/yr. no penalty. All taxable.
- Basic insurance = if you die beneficiary gets account value or premiums paid.

BANKING & FINANCE

AIG Unit Settles Retirement-Plan Probe

Advisor to pay \$20 million over failure to tell teacher clients of promotional payments

BY DAVE MICHAELS
AND ANNE TERGESEN

A unit of American International Group Inc. agreed to pay \$20 million to settle claims that it failed to disclose payments intended to draw more business to the firm, the first case to emerge from a crackdown on practices in the market for teachers' retirement plans.

Florida teachers saving for retirement through 403(b) plans—similar to corporate 401(k) plans—weren't told about an arrangement by which the parent of Valic Financial Advisors Inc. paid hundreds of thousands of dollars to an entity owned by local affiliates of the Florida Educa-

tion Association, which in turn promoted Valic Financial Advisors' services, the Securities and Exchange Commission said Tuesday.

Valic benefited in two ways: Teachers bought its annuity products and signed up as clients of its investment-advisory business, paying Valic an annual fee to manage all of their assets.

The case against Valic, which neither admitted nor denied the SEC's civil claims, is the first to emerge from an enforcement crackdown launched in 2019 and focused on sales practices in the approximately \$1 trillion 403(b) market.

"We are pleased to have resolved these matters involving VALIC Financial Advisors, which is taking all necessary steps to ensure a robust program of disclosure improvements and governance enhancements," the company said.

The SEC didn't name the Florida Education Association or its affiliates in its settlement order, but The Wall Street Journal reported the SEC's investigation of Valic and the company's arrangement with the affiliate of the Florida teachers' unions in 2019.

"When I learned that our nation's educators—who provide such an important service, often at great personal and financial sacrifice—often were not appropriately informed regarding essential aspects of their investment options, I was disturbed," SEC Chairman Jay Clayton said. "We launched our Teachers Initiative with the objective of bringing our resources—including enforcement, examinations and investor education—to benefit these investors, including through rooting out fraud and misconduct."

The SEC continues to investigate the 403(b) market, peo-

ple familiar with the matter said.

The SEC's investigation found Valic paid the salaries of three employees at the entity linked to the Florida union. At meetings and seminars where teachers sought investment advice, the three touted Valic products, presenting themselves as workers for the union entity and not disclosing they were also paid by Valic, the SEC said.

The Journal reported in December that the union entity was known as Creative Benefits for Educators. As recently as October, teachers' unions in central Florida were advising members to take retirement questions to Mary L. Thomas, a consultant at the union-owned firm—and a longtime Valic sales representative, according to regulatory records.

After the Journal asked about her dual role, the Creative Benefits website went dark last fall. At the time, a

spokesman for Creative Benefits said that it no longer employed Ms. Thomas and two other consultants.

Teachers who bought Valic's Portfolio Director, an annuity popular in teachers' retirement plans, paid fees of up to 2.3% of assets annually. Valic earned \$29 million from its annuity products sold during the 13 years it dealt with Creative Benefits.

As part of the settlement with the SEC, Valic agreed to charge lower fees to teachers who signed up to have their money managed by the company, under a "wrap-fee" program.

Valic Financial Advisors manages over \$21 billion and has more than 318,000 individual-investor clients, according to its most recent regulatory disclosure filed with the SEC.

In a separate settlement with the SEC also announced Tuesday, Valic agreed to pay

\$19.9 million to resolve claims that it steered clients into higher-fee mutual funds without clearly telling them about cheaper alternatives.

The case involves 12b-1 fees, continuing charges levied against investor assets that typically reward financial advisers who sell mutual funds. Nearly 100 investment advisory firms last year agreed to deals with the SEC that required them to refund the fees to investors. The firms reported their own misconduct to the SEC under a program that waived penalties because they cooperated with the investigation.

Valic didn't participate in the self-reporting program, the SEC said. In Valic's case, clients were placed in funds that charged continuing fees even though they had deals with Valic that suggested they were eligible for a cheaper version of the fund, the SEC said.

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Variable Annuity Example

- Buy \$100,000 variable annuity with no riders with a 7% surrender fee which declines 1% per year.
- In second year you decide to withdraw \$50,000 so surrender fee is now 6%.
- No surrender fee on first 10% (\$10,000) but portion is taxable.
- Remaining \$40,000 will have 6% surrender fee of \$2,400.
- Assume 5% Rate of return so \$5,000 is return of principal and \$5,000 of earnings taxed assume 22% = \$1,100 tax plus any state tax (assume CA 8% = \$400).
- If withdrawn prior to 59 1/2 a 10% fed tax penalty on full \$50,000 or \$5,000.
- $\$50,000 - \$2,400 - \$1,100 - \$400 - \$5,000 = \$41,100$ remaining

You don't date an annuity, you marry it. An annuity isn't a mutual fund that you buy today and sell tomorrow. Nor is it a certificate of deposit, ready for any new use at maturity. When you buy an annuity, you are making (or ought to be making) a 15- or 20-year commitment, at least.

~ Jane Bryant Quinn

OH MY GOD YOU'RE FLATLINING!

NO, IT'S JUST MY ANNUITY...



VA Riders

- Endless. Most common **Living Benefits**, simplified. Questionable value. 1%
- **Guaranteed Minimum Accumulation Benefit(GMAB)** – Guarantee minimum balance or lock in yearly gain
- **Guaranteed Minimum Withdrawal Benefit(GMWB)** – Guarantee that withdraw at least premiums paid. (Sometimes called Cash Refund Rider)
- **Guaranteed Minimum Income Benefit(GMIB)** – Guarantees minimum payout growth rate (usually 5%-7%) will be forced to annuitize.

VA Riders - continued

- **Guaranteed Lifetime Withdrawal Benefit(GLWB)** – Guarantees periodic income payments without annuitizing. Many twists to this.
- Long-Term Care Protection-Simplified Issue
- Stand Alone Living Benefit
- Death benefit for beneficiaries
- Disability, Nursing Home, Confinement – Guaranteed Issue
- Unable to remove Riders

A few words about Income Rider GMIB

-
- Often referred to as the “roll-up rate” or “step up rate”.
 - Often hear marketing pitch about “guaranteed 8% compounded for 10 years”.
 - Refers to amount in “Benefit Base” not actual lump sum withdrawal.
 - Can counterbalance with “Payout Rate” which is rate payout based on.
 - $\$100,000 / 8\% \text{ compound rate} / 4.5\% \text{ payout} = \$6,612$
 - $\$100,000 / 5\% \text{ compound rate} / 5.5\% \text{ payout} = \$7,020$

95% of Variable Annuities

were never Annuitized in 2018.

According to LIMRA

Fixed Index Annuity(1995)

- Formerly known as Equity Index Annuity, no equity involved
- Often deceptively sold at “Free-Dinner” seminars
- Very complicated – Most people don’t know what they bought
- Has Accumulation and Distribution phase like deferred VA
- Has Surrender period like the deferred variable annuity – you can lose money
- Often deceptively sold as market participation but should be compared to CD
- Less market risk than deferred variable annuity but less return

Fixed Index Annuity – How they work

- Interest credited is based on an index - Typically S&P500 but can be any
- Dividends generally not included
- Will guarantee account balance has floor of zero.
- There are administrative fees

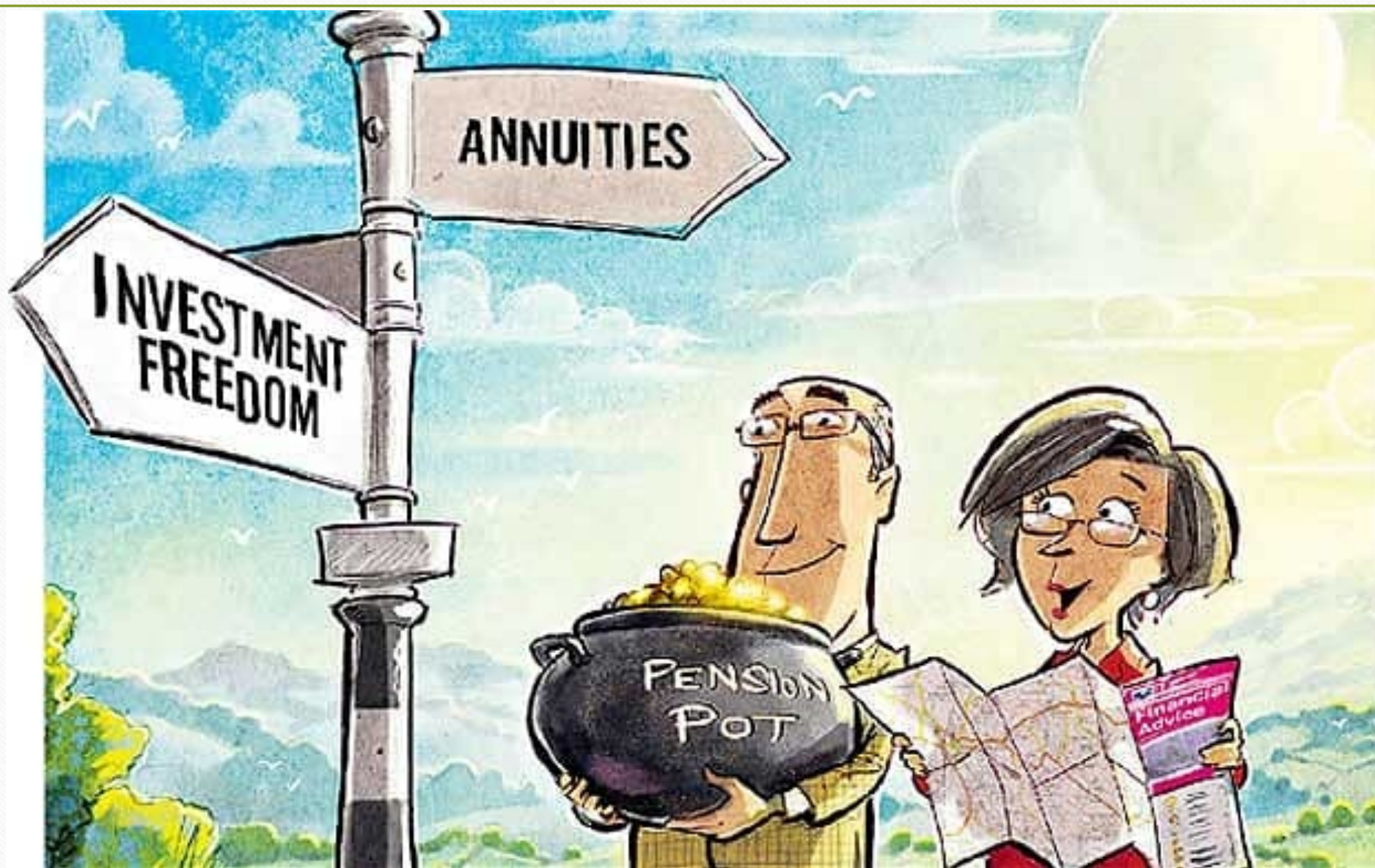
Fixed Index Annuity — How they work cont.

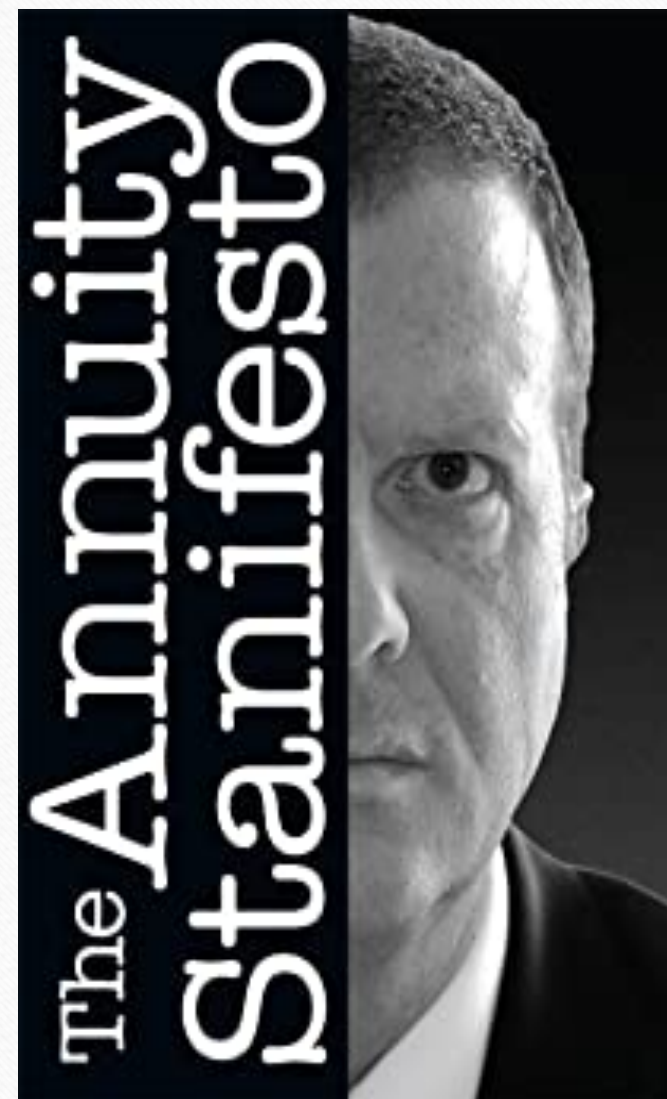
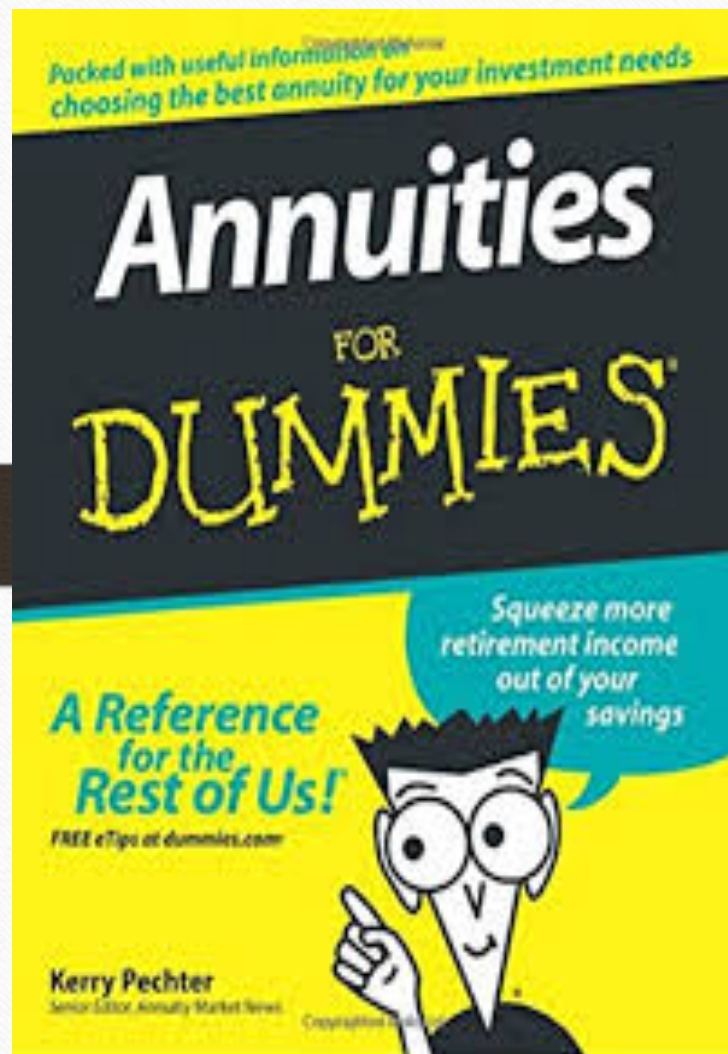
- Credit is usually based on three factors
 - **Participation Rate** — usually from 40% to 60%. Longer Accumulation = higher participation, FINRA example is 45%
 - **Cap Rate** — maximum amount allowed to earn — typically 5% to 7%
 - **Spread** — typically 3% - subtract spread from actual return.
 - Latest twist is Buffers

Compare Rate of Return

(2007-2012 Advantage Compendium Study)

-
- Average annual return of all fixed index annuities = 3.27%
 - Best annual return of all fixed index annuities = 5.5%
 - Worst annual return of all fixed index annuities = 1.2%
 - Recent 10-yr. average annual return of 50/50 VG TSM/TBM = **8.71%**
 - VG Tax-Managed Balance(50/50): 1-yr=5.76%, 3-yr=7.05%, 5-yr=6.79%, **10-yr=8.58%**
 - **Worst since 1950** rolling 20-yr 50/50 S&P500(6.2%) and Inter Bonds (4.2%) = **appx 5.2%, Best appx 14%**





Example of Returns

\$100,000 initial investment

- Annuity – 3.5% return (rule of 72) doubles in 20 years to \$200,000. Age 65 with 6.5% payout rate = \$13,000 per year, \$6,410 taxable. At 82 (life expectancy) 100% taxable. Illiquid. Beneficiary pay full taxes.
- Vanguard 50/50 TSM/TBM - 7% return (rule of 72) doubles in 10 years to \$200,000. Doubles again in next 10 years to \$400,000. 4% SWR = \$16,000 taxed at capital gain rate. Liquid. Step-up to beneficiary.