

Immediate Annuities: The Official Report

Introduction

Immediate annuities are the most traditional form of annuity. Like any other product, features have been added over time to offer additional benefits. For the most part, the initial product has evolved as a result of competition between insurance companies as they compete for your investment dollars.

How Immediate Annuities Work

In its simplest sense, with an immediate annuity you make an initial deposit with an insurance company and in return, the company pays you a guaranteed monthly income for the rest of your life.

In order to calculate the payment you will receive, the insurance company will estimate your life expectancy according to your age and gender.

This produces a factor that is multiplied by the intended initial investment to arrive at the guaranteed payment amount.

Of course, there are variations on this theme that can complicate things, but this is the general framework of an immediate annuity.

Pros and Cons

The benefit of immediate annuities is that you will receive a higher guaranteed income than you could get from any other product.

The major disadvantage is that when you pass away, any unrecovered principal is surrendered to the insurance company.

This is a one-way contract. To put it bluntly, if you outlive the average you'll win big... if you die early then the insurance company wins big.

Contract Structure and Options

There are several variations on the general theme of immediate annuities that add flexibility, options, and costs, that help tailor the annuity income stream to your needs.

- **Single Life** The basic form mentioned earlier. This works best for one person with no desire or need to leave a remainder benefit to heirs.
- **Joint Life** In this case, the payout will be based on two lives such as you and your spouse. Payments continue as long as both people are living. To increase the initial payout, it is possible to reduce the payout to the surviving spouse. Many people that elect this option reason that living expenses will be reduced with only one living spouse. That can be true, but I like to analyze everything. Don't take an advisor's word for it unless a side-by-side comparison has been shown. Remember: "Trust but verify."
- **Period Certain** With this option, payments will be guaranteed for lifetime or a specified period, whichever is greater. This works well when the contract owner wants to guarantee payments for heirs and can be a good way to ensure that the initial investment principle is recovered over time. Again, do the math and make sure you understand the deal you're getting.
- **Remainder Guarantee** This guarantees that income payments will at least equal the invested amount regardless of how long the contract owner lives. Similar to period certain contracts, this is done to ensure a certain level of asset recovery. In most cases, a period certain will guarantee slightly more aggregate income.
- **Inflation Adjustments** Many people are justifiably concerned about the negative effect of inflation on retirement income. This may also come in the form of a cost of living adjustment, or COLA. Immediate annuities with an increase index can be a great hedge. Inflation indexed immediate annuities start with a lower initial payment that increases in relation to the consumer price index (CPI) annually. On these contracts, payments start quite a bit lower so it is very important to compare them to a more straightforward contract.

Also there is a big difference between the CPI and a COLA. COLAs generally guarantee a 3% annual income increase, whereas increases in the CPI are not guaranteed. Some years the CPI may increase by 8%, for instance, and some years it may not increase at all. With a COLA, annual increases happen no matter what but may not increase enough to combat current inflation. There is a lot to think about here so take your time and seek high quality advice.

Approximate Payout Rates

The primary factors that determine immediate annuity income are age and gender.

As discussed above, there may be two gender and two ages to factor in. Further, specific “impaired risk” rates may be available to individuals who, for some reason, have a shorter than average life expectancy, subject to an extensive medical exam in addition to the basic factors.

At the end of this report, you will find a table that posts some base rates under three options at different beginning ages. Use this as a reference point as you research your retirement income options.

Comparison of Alternate Strategies

There are several combinations of products that generate income that may be offered to you. Depending on your situation they may or may not be appropriate. Please, Contact us for advice navigating these waters. We will outline some of the many flavors of annuities and immediate type annuities, below:

- **Guaranteed Income Variable Annuities-** These are covered extensively in the separate GLWB report so I won't go into tremendous detail here. My biggest concern with variable annuities with income guarantees is the confusion they cause. Most people don't quite understand how the contract works and that is enough of a red flag for me to call these products out.
 - These contracts work well for someone who is willing to accept a much lower initial payment than is available with an immediate annuity. The trade off is that a level of income is guaranteed and can increase if and when the stock market performs well. There is no doubt you will see a rosy scenario that shows your annual income shooting sky-high. Stop right there!... a serious evaluation is recommended. Before you go any further, read our GLWB Report.
- **Traditional Asset Management-** This is the name I'll give the general retirement income strategy that dictates you invest your assets in a diversified portfolio of funds or securities, and draw a certain percentage (usually 4%) of those assets as income annually. This leaves you invested and exposed to the market.

- Like any other strategy, this doesn't offer as high a level of income as do immediate annuities. Also, you run a significant risk of negative performance in the market at some point which will force you to take lower income at an unknown future date. This is generally the sort of risk and unknown that investors considering annuities are seeking to avoid.
- Call me crazy but I just don't like taking that option when there are guarantees available. Since immediate annuities offer greater payouts, it takes less money for an equal income level. I favor contributing a portion of the assets to an immediate annuity that will generate your desired level of income and contribute the remainder to an investment account for continued growth in the market and additional future income planning opportunities.
- **Fixed Annuity/ Immediate Annuity combination-** This is a strategy of my own invention. In a nutshell, we use fixed annuities to guarantee appreciation and income, while preserving asset values, then at a future point, transition into an immediate annuity to maximize income. It only works with the right asset mix inside a well-documented plan. But because immediate annuities are calculated using long-term interest rate assumptions and life expectancy, by combining these two annuity types we are able to match the payout and maintain greater control and flexibility of client assets.
 - The interest rates used for immediate annuities are conservative and slightly exceed the low rates available in many products today. In the right scenario, you can purchase a fixed annuity and take income via the free withdrawal provision to match a comparable payment from an immediate annuity. This way, you will position yourself to really take advantage of future inflation when the contract term expires and lock in a higher rate, which will either increase future income or your asset base.
 - Again, this will require the right blend of assets and someone who is capable of devising a plan and sticking to it. You'll have to call me if this sounds like something you'd like to explore because I don't think there are many people familiar with the proper design of this strategy.

Immediate Annuity Payment Rates

The payment rate in an immediate annuity is kind of like the meat in a sandwich: why bother without it? My apologies to all the vegetarians in the crowd.

I have compiled a general list of available rates under different contract options. I'll explain the specific rates I present but you must know that there are many more options available than can be displayed here. Basically, you can do just about anything you want to tailor immediate annuity payments to your situation.

I used identical ages for each spouse in the illustrations so many people who have even a one year age differential will see a slight adjustment accordingly. The principal owner of the contract is the initial variable in the calculation. The spouse is a secondary variable. If you, as the contract principal, are one year older than your spouse then you will see a lower payment than you'd otherwise see with identical ages. Ages of married couples vary greatly so I'll save the details for specific consultation. If you are single, the calculations are much easier and the choices of options simpler.

Actuarial science tells us that women generally live longer than men so payment rates are lower for women since a company plans on having to make payments for a longer period of time. The payouts are listed as a percentage rounded to the nearest hundredth. In order to find an expected payment, multiply your planned investment by the percentage that corresponds with your preferred payment method.

*For instance, for a 64 year old single individual with no remainder and a \$100,000 investment, expect \$7430 (7.43% * \$100K) for males and \$6970 (6.97% * \$100K) for females.*

This figure is expressed on an annual basis. Divide by twelve to find monthly income amounts of \$619.17 and \$580.83 respectively.

Here is a basic explanation of each option in the table.

- **Single Life:** This income amount is payable to the contract owner for the remainder of his/her life, regardless of how long that is.
- **Single Life with 20 Year Period Certain:** Similar to the single life option, 20 year period certain means income will continue through the contract owner’s life or 20 years, whichever is longer.
- **Joint Life:** This contract makes payments over the life of two people. As long as either is living, payments will continue.
- **15 Year Period Only:** This is very straightforward. Payments are made for 15 years to the contract owner or his/her heirs for 15 years.

This is a decent sample of the various options available for immediate annuity payouts. There are several more options to consider to tailor an Immediate Annuity to your specific situation. There is no substitute for good advice, and we’re available to help.

Starting Age	Single Life	Single/ 20 Yr Period Certain	100% Joint	15 Year Only
	<i>male/female</i>	<i>male/female</i>		
60	6.88/6.48	6.34/6.19	6.01	8.66
61	7/6.64	6.4/6.24	5.88	8.66
62	7.14/7.73	6.46/6.3	5.95	8.66
63	7.27/6.85	6.50/6.35	6.04	8.66
64	7.43/6.97	6.56/6.41	6.12	8.66
65	7.58/7.09	6.61/6.47	6.22	8.66
66	7.76/7.04	6.64/6.51	6.32	8.66
67	7.94/7.38	6.7/6.56	6.59	8.66
68	8.14/7.56	6.73/6.64	6.71	8.66
69	8.36/7.72	6.78/6.67	6.83	8.66
70	8.59/7.91	6.82/6.77	6.97	8.66
71	8.84/8.34	6.85/6.82	7.13	8.66
72	9.12/8.34	6.88/6.82	7.3	8.66
73	9.42/8.58	6.91/6.84	7.46	8.66
74	9.73/8.84	6.92/6.88	7.67	8.66
75	10.08/9.13	6.94/6.91	7.87	8.66
<i>all figures are expressed as annual percentages of invested principal.</i>				

In Closing

Immediate annuities offer significantly higher payouts than almost any investment strategy available. This enables retirees more flexibility with assets as well as a way to mitigate any losses retained as a result of negative market performance.

Regardless of your individual position regarding overall assets, I can say confidently you will be very happy with the use of an immediate annuity. How you use them depends on your personal preferences and the quality of the advice you receive. A few years ago, New York Life and the Wharton Business School cosponsored a study that identified immediate annuities as the best way to ensure a high level of guaranteed income throughout retirement. So now you don't have to just take it from me.

If you are still interested in the use of immediate annuities, or any other type of annuity, I highly recommend The Annuity Report as a great base of information that lives up to the name of my website... Straight Talk!

Like you, I searched the internet... and found the comparable information lacking. I built AnnuityStraightTalk.com to fill in the gaps, and offer honest information freely available.

I look forward to hearing from you, to help you find the best combination of safety, security, and flexibility for your retirement.

Wishing you a Safe, Flexible and Profitable retirement.

Bryan J. Anderson