RW CONSULTING GROUP

WHAT YOU SHOULD KNOW ABOUT ANNUITIES

P: 303-888-1406

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Annuities are similar to a pension you purchase for yourself.

Company pensions are pretty much a thing of the past in corporate America. While the ubiquitous 401(k) plan might help workers save pre-tax or post-tax dollars for retirement, they've also shifted the responsibility for retirement planning to the individual. And as many people saw in the 2008 economic crisis, 401(k)s can be fraught with market risk, including the risk of losing too much value, forcing the retiree to go back to work.

Annuities can be thought of as a way to transform savings into income. When you purchase an annuity, you are exchanging a sum of money for an agreed-upon monthly payment, generating a predictable income stream in retirement similar to a pension.

Tax-deferred, qualified annuities.

Annuities can be purchased with pre-tax or after-tax dollars. Sometimes people perform a 401(k) rollover into an annuity with money from a previous employer, or after they turn 59-1/2 years old, when they can access their money without a 10% federal tax penalty.

When purchased with pre-tax dollars, a properly-structured annuity can offer 100% tax-deferred growth, similar to other qualified accounts. You're not taxed on interest earnings while your money stays in the annuity, but once you start receiving payouts, just like a 401(k) or traditional IRA, they are taxed as ordinary income based on your income tax rate at the time. When you hold annuities in non-qualified accounts purchased with after-tax dollars, there are no penalties or mandatory distributions based on age.

They're not right for everyone.

There are a number of reasons annuities might not make sense for some people. Surrender fees apply if you want out of your contract early, and you should learn about any other fees involved with any individual annuity policy before you purchase. A qualified financial advisor can spell out the pros and cons.

But most people are worried about how they'll make it through retirement without running out of money, especially given the increased longevity predicted for most Americans. For them, a portion of their portfolio containing annuities might make sense, depending on their situation and goals.

There are many different types of annuities.

There are many different types of annuities available, including variable, fixed rate, fixed indexed and more, each having different features. Some types have become increasingly popular, like fixed and fixed indexed annuities. Annuity sales smashed through barriers in the fourth quarter of 2023, setting records along the way. In fact, for the last two years, annuity sales have exceeded records originally set in the Great Recession of 2008. "Indexed annuities have now sold over a trillion dollars since their introduction in 1995," said Sheryl Moore, CEO of Wink, Inc.

Many types of annuities come with guarantees.

One of the most appealing things about annuities is the guarantee. Because annuities are contracts between you and an insurance company, the insurance company often guarantees that your principal will be protected based on their financial strength and claims-paying ability. Some annuities also guarantee a certain amount will be credited to your policy based on contract terms; while many indexed annuities deliver "downside market protection" as well as "upside market potential." The exception is a typical variable annuity, which may be invested in the market and subject to losing value in a market downturn.

Some Wall Street experts are now advocating annuities as a replacement for part of your bond portfolio in retirement.

The inverse relationship between a bond's price and its yield pose one of the main risks with bonds. In a rising interest rate environment, the risk can be even greater for retirees.

Experts like Professor Wade Pfau, PhD and Nobel-prize winner and Yale Economics Professor Robert Shiller have each run the numbers in well-researched academic studies comparing bond performance to annuities. Yale Emeritus Professor Roger Ibbotson published a landmark study which ran hypothetical return simulations comparing stocks, bonds and fixed indexed annuities (FIAs) from 1927 to 2016. As a result, he concluded that "fixed indexed annuities have the potential to outperform bonds in the retirement portfolio."

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This information is for educational purposes only and should not be taken or construed as legal, tax or financial advice. In all cases, it is recommended that you consult with legal, tax and financial advisors who can provide you with personalized advice based on your unique situation and circumstances.

Guarantees and protections of fixed indexed annuities are subject to the claims-paying ability of the issuing insurance company. Fixed indexed annuities are contracts purchased from a life insurance company. They are designed for long-term retirement goals, and also intended for someone with sufficient cash and liquid assets for living expenses and unexpected financial emergencies, including, for example, medical expenses. Depending on the product, fixed indexed annuities may include surrender charges, rider charges and other fees.

A fixed indexed annuity is not a registered security or stock market investment. As such, it does not directly participate in any stock, equity or bond investments, or index. Gains on indexed accounts are based on participation rates and other conditions offered by the issuing insurance company. Withdrawals may be subject to income tax, and withdrawals before age 59½ may be subject to a 10% early withdrawal federal tax penalty if the annuity was purchased with qualified money.

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