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The Importance of Sustainable Retirement Savings

A. Retirement Income Planning & Concerns

1. Retirement Planning Options

We've all heard the statistics: Our nation has reached a retirement demographic milestone. The first of the baby boomers reached the age of 65 on January 1, 2011, and 7,000 more are turning that age each day. An estimated 79 million individuals will participate in this retirement boom between now and 2029. Many individuals who are grouped within this "silver tsunami" are approaching retirement with fears and worries that did not exist in previous generations. The well-publicized concerns of this group center on not having sufficient financial assets to live successfully in retirement.

Probably the greatest impact on retirees today is the blessing and possible curse of living longer than ever. Life expectancies have increased dramatically. Today, the average 65-year-old male is expected to live 17.2 years to age 82; the average female for 19.9 years to nearly 85. Moreover, for married couples, where each spouse has reached the age of 65, there is a 57% chance that one spouse will live to age 90, and an 11% chance that one spouse will live to age 100. When approaching retirement, many people do not fully realize that the assets they have accumulated, and other outside retirement income sources, may need to last for 30 or more years. These extended retirements also increase the strain on government programs, which are already on shaky ground. In fact, it is a sign of these times that, according to a recent survey, the number one concern of those nearing or living in retirement is whether their money will last – 96% of retirees say it is their biggest worry. Other trends also influence traditional approaches to retirement income planning.

Pension Plans

Pension plans were once a primary source of retirement income for many Americans. Today, traditional defined benefit and defined contribution pension plans have become the exception rather than the rule. Consider that in 1985 there were more than 114,000 private pension plans maintained by corporations for their employees. Today, this number has fallen to 38,000. Although 401(k), 403(b), and 457 plan participation has grown rapidly, these plans do not guarantee a lifetime of income, and many of their balances are far below the amount needed to support life in retirement. Government employees are one of the few employee groups that continue to enjoy this type of pension benefit.

Social Security

Retiring workers rely heavily on Social Security benefits. However, the newspapers and airwaves have relayed countless stories about the uncertain future of this system.

Yes, Social Security has money problems, and after continuing benefit payments at current rates, the program's trust fund could be depleted by the year 2037. At that time, Social Security will be able to pay only about 78¢ on the dollar. It is no wonder we have come to this point when you think of the origin of Social Security in 1935. Consider that in 1930, the life expectancy at birth for men was age 58, and for women it was age 62. The Social Security designated retirement age was 65! Because life expectancies increased greatly since then, many people of this era have lived long years in retirement.

There is substantial emphasis on improving the future of the Social Security system. Increasingly, individuals are advised to delay the receipt of benefits to age 70 to increase their payout amounts, and to continue working longer. Establishing delays in the retirement age (currently 67) are another method of addressing this issue, and other options, such as limiting payments and increasing taxation on those in higher income brackets, are continually evaluated. In any case, it is clear that Social Security is important to many for a comfortable retirement, but that there will be changes to the benefits it delivers in the future.

Cost of Health Care and Inflation

Two other concerns rank very high on the list of those living in or nearing retirement. As you might guess, they are the cost of health care and inflation. Healthcare costs continue to grow, and it is estimated that on average, a healthy 65-year-old couple will need \$260,000 just to pay for healthcare and long-term care costs for the remainder of their lives. Medicare provides substantial coverage for most over the age of 65, but it is not complete, and the cost for Medicare and other medical and long-term care coverages continue to grow at a rapid rate.

Since the financial turmoil of 2008-2009, inflation has had less impact than in years past. However, it is certain to reappear with a growing economy, and it is recommended that retirement plans should factor in an average inflation of rate of 3%. The detrimental effect of inflation can take a healthy retirement balance and reduce its value and buying power dramatically over a long retirement.

Every one of the issues just described places significant stress on funds available for retirement income. However, with a good planning process and continued commitment to preparation for the future, the risks can be mitigated.

2. Annuities in Retirement Planning

How do annuities fit into this rather bleak retirement picture of the future? Annuities and the features they provide are a strong and worthy financial choice for the mitigation of these retirement risks, and should be considered for a portion of the retirement assets of nearly every retiree today.

Annuities offer unique value propositions that are unavailable in other financial product alternatives. Their guarantees can erase the fear of running out of money no matter how long an individual or a spouse may live. They offer tax-deferred growth that can help assets accumulate faster. They pay death benefits to beneficiaries that ensure that no less than the principal invested is paid from the contract.

There are other less advantageous considerations with these products. For example, they are known to have high fees, limited liquidity, and may require that control of funds be given to the insurance company for a defined period. They also pay high commissions compared to certain other financial products. In spite of all the good they can provide, annuity products are not appropriate for all situations. In addition,

annuities have been sold improperly by financial representatives who have not kept the best interest of customers in mind.

NAIC Suitability in Annuity Transaction Model Act

The protection of the financial assets that individuals have accumulated for retirement is a primary concern of financial regulators. They are committed to protecting against bad retirement planning advice and sales motivated by greed alone. As such, there is continued evolution in regulatory requirements that apply to representatives who provide retirement advice, and in particular those who work with seniors. A critical focus over recent years has been on suitability of annuity sales, and **the NAIC 2010 Suitability in Annuity Transactions Model Act** is especially centered on this important topic.

As stated in an executive summary prepared by participating commissioners, the National Association of Insurance Commissioners (NAIC) adopted the Model Regulation *“to set standards and procedures for suitable annuity recommendations and to require insurers to establish a system to supervise recommendations so that the insurance needs and financial objectives of consumers are appropriately addressed.”*

Three primary objectives of the Model Annuity Suitability Act include

1. The establishment of a regulatory framework that holds insurers responsible for ensuring that annuity transactions are suitable;
2. The requirement that producers be trained on the provisions of annuities in general, and the specific products they are selling; and
3. The intention of creating consistency with suitability standards imposed on registered financial products by Financial Industry Regulatory Authority (FINRA) whenever possible.

Industry Regulation

Individuals within the financial industry today recognize the vast opportunity this retirement need presents. With this incredible opportunity comes the responsibility to ensure that the products and services that are recommended are appropriate for the needs of these individuals. Bad financial decisions can steal "golden years" away from persons that have worked all of their life to attain their retirement dream.

Unscrupulous practitioners can urge trusting and vulnerable seniors into inappropriate investments that are solely motivated by greed. With the plethora of financial products in the market today, many people rely heavily, sometimes with blind trust, on advice from others in making critical life decisions. It is because of these concerns that financial industry regulators have focused on the protection of consumers who are considering the purchase of these products.

B. Guaranty Associations

Guaranty Associations are formed to protect policyowners, insureds, beneficiaries, and anyone entitled to payment under an [insurance policy](#) from the incompetence and insolvency of insurers. The association will pay covered claims up to certain limits set by state law. The Association is usually funded by its members (through assessment). All authorized insurers, which are required to be the members of the Association, contribute to a fund to provide for the payment of claims for insolvent insurers.

The Guaranty Association, under the direct supervision of the state department of insurance, usually is required to maintain **separate accounts** for each type of products: life insurance, annuities, and health insurance. The liability of the Association may not

exceed the lesser of the contractual obligations for which the insurance company is liable or a specified dollar amount (which varies by state and type of coverage).

1. California Life and Health Insurance Guarantee Association (CIC 1067-1067.19)

The California Life and Health Insurance Guarantee Association is designed to protect consumers against the failure of insurance companies to fulfill contractual obligations under life and annuity contracts due to financial impairment or insolvency.

To provide this protection, an association of insurers has been created to pay benefits and continue coverage. **All admitted insurers in California are required to be members of this association**, and are assessed membership fees in proportion to the amount of premiums written, to provide funds to carry out the purposes of the association.

The association performs its functions under an approved plan of operation and exercises its powers through a board of directors.

Protection is afforded to California life, health, and annuity policyowners, contractholders, and their beneficiaries, assignees, and payees. The association provides coverage for direct, nongroup life, health, or annuity policies or contracts, and supplemental contracts to any of these, and for certificates under direct group policies.

Annuity contracts and certificates under group annuity contracts include allocated funding agreements, structured settlement annuities, and any immediate or deferred annuity contracts.

The benefits for which the association may become liable for life insurance and annuity policies in no event may exceed the **lesser** of the following:

- 80% of the contractual obligations for each policy or contract for which the insurer is liable or would have been liable if it were not impaired or insolvent;
- With respect to any one life, regardless of the number of policies or contracts:
 - \$300,000 in life insurance death benefits, but not more than \$100,000 in net cash surrender and net cash withdrawal values for life insurance;
 - \$250,000 in the present value of annuity benefits, including net cash surrender and net cash withdrawal values;
- With respect to each payee of a structured settlement annuity, or beneficiaries of the payee if deceased, \$250,000 in present value annuity benefits including net cash surrender and net cash withdrawal values.

When a member insurer becomes impaired, the association may:

- Guarantee, assume, or reinsure, or cause to be guaranteed, assumed, or reinsured, any or all of the policies or contracts of the impaired insurer;
- Provide moneys, pledges, loans, notes, guarantees, or other means and assure payment of the contractual obligations of the impaired insurer; and
- Provide notice of termination of benefits and make efforts to provide annuitants with replacement or substitute coverage.

The commissioner oversees the Guarantee Association and has the following rights and duties:

- When an impairment is declared and the amount of the impairment is determined, serve a demand upon the impaired insurer to make good the impairment within a reasonable time;
- In any **liquidation** or rehabilitation proceeding involving a domestic insurer, be appointed as the liquidator or rehabilitator;

- Suspend or revoke, after notice and hearing, the [certificate of authority](#) to transact insurance in this state of any member insurer which fails to pay an assessment when due or fails to comply with the plan of operation.

To aid in the detection and prevention of insurer insolvencies or impairments, the Commissioner must notify the commissioners of other states when a member insurer has its license revoked or suspended, or when the Commissioner formally orders a member company to restrict its premium writing, obtain additional contributions to surplus, withdraw from the state, reinsure all or any part of its business, or increase capital, surplus, or any other account for the security of policy owners or creditors.

The Commissioner must report to the board of directors when he or she has reasonable cause to believe from any examination that a member company may be an impaired or insolvent insurer.

According to the California Insurance Code (CIC) 1067.17, agents may not publish or make any claims, written or oral, which use the existence of the California Life and Health Insurance Guarantee Association for the purposes of inducing the purchase of an insurance or annuity [contract](#) or to imply that insurance or annuity contracts are in any way financially backed or "guaranteed" by the Association.

Insurers must provide a standard document prepared by the Guarantee Association describing the general purposes and limitations of the Association coverage to the [policyowner](#) or contractholder at the time of delivery of the policy or contract. The document must be available upon request of the policyowner or contractholder, and must not be used to imply that the policy or contract would be covered in the event of an insurer impairment or insolvency. The disclaimer must include the following:

- The name and address of the Life and Health Insurance Guarantee Association and insurance department;
- A warning that the California Life and Health Insurance Guarantee Association may not cover the policy or, if coverage is available, it will be subject to substantial limitations and [exclusions](#) and conditioned on continued residence in the state;
- That the insurer and its agents are prohibited by law from using the existence of the California Life and Health Insurance Guarantee Association for the purpose of sales, solicitation, or inducement to purchase any form of insurance; and
- That the policyowner or contract owner should not rely on coverage under the California Life and Health Insurance Guarantee Association when selecting an insurer.

C. California Annuity Training Requirement (CIC 10509.915)

Even before the NAIC acted on annuity suitability, California required producers selling individual annuity products to receive detailed training on sales and suitability practices. These rules have been in effect since 2004.

An insurance producer may not solicit the sale of an annuity unless the producer has adequate knowledge to recommend the annuity purchase and is in compliance with the insurer's standards for product training.

An insurance producer may rely on insurer-provided product-specific training standards and materials to comply with this requirement.

A licensed life producer must complete a **one-time 8-hour annuity training** course provided by an approved education provider, before transacting annuity business.

In addition, every producer who engages in annuity sales in California must complete **4 CE credits** of annuity training prior to license renewal **every 2 years**.

The required training must include all of the following topics:

- The types of annuities and various classifications of annuities;
- Identification of the parties to an annuity;
- How fixed, variable, and indexed annuity [contract](#) provisions affect consumers;
- The [application](#) of income taxation of qualified and nonqualified annuities;
- The primary uses of annuities; and
- Prohibited sales practices, the recognition of indicators that a prospective insured may lack the short-term memory or judgment to knowingly purchase an insurance product, and fraudulent and unfair trade practices, as well as California replacement and [disclosure](#) requirements.

Courses must cover all topics listed in the prescribed outline and not present any marketing information, sales training or specific information about a particular insurer's products. Additional topics may be offered in conjunction with and in addition to the required outline.

Annuity course providers must register as a California CE provider and must comply with CE course rules and guidelines, including certification and reporting requirements. Courses may be completed by classroom or self-study.

An insurer is required to verify that an insurance producer has completed the annuity training before allowing the producer to sell an annuity product for that insurer. An insurer may satisfy its responsibility under this paragraph by obtaining certificates of completion of the training course or obtaining reports provided by commissioner-sponsored database systems or vendors or from a commercial database vendor that has a reporting arrangement with approved education providers.

D. Importance of Reviewing Sample Contracts

It is important for the consumer to know whether an annuity fits their situation before entering into a [contract](#). A best practice is for the agent to review sample contracts with the prospective insured so they are fully informed about the contract's features and benefits.

Individual needs change with time and what may have benefited them in the past may not be in their best interest now. Clients must consider their long-term goals, including whether they:

- Might need access to the money for unexpected family emergencies;
- Might need access to the money for long-term care or health care;
- Can afford to lock up these funds for a period of several years.

Some annuity products carry high surrender charges during the initial years the contract is in force. Always discuss the drawbacks as well as the benefits. California requires individual annuity contracts for seniors to contain a [disclosure](#) regarding the surrender charge period unless the contract does not contain surrender charges.

E. About this Course

This course is designed to meet California's 8-hour annuity suitability training requirements, as created by the following:

- SB 620 (Chapter 547, Statutes of 2003), Annuities: life insurance: required disclosures and prohibited sales practices and how annuities affect Medi-Cal as stated in SB 483 (Chapter 379, Statutes of 2008). Medi-Cal: home and facility care; and
- AB 689 (Chapter 295, Statutes of 2011) Insurance: annuity transactions.

It is designed to help you improve your understanding of annuity products and features so that you confidently and appropriately recommend suitable solutions for your customers. Through studying and contrasting various types of annuities and reviewing customer situations, it will heighten your awareness of how and when certain products and features may fit well with a client's needs. It will explain both the benefits and the risks associated with each product type to help you give fair and balanced product presentations to your customers.

The course will explore the following topics with an emphasis on how knowledge of these topics impacts the sales process and the determination of suitability:

- Annuity basics and terminology;
- Parties to annuity contracts;
- Product overview, including fixed, immediate, index and variable annuities;
- Annuity Taxation;
- Annuity Replacements and Exchanges; and
- The Producer's Role in Suitable Sales.

The retirement planning field presents a phenomenal opportunity for financial practitioners today. Your commitment to continued education, professionalism, and just doing the right thing for your customers will help ensure that your career in this field is long and prosperous.

Chapter Complete

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