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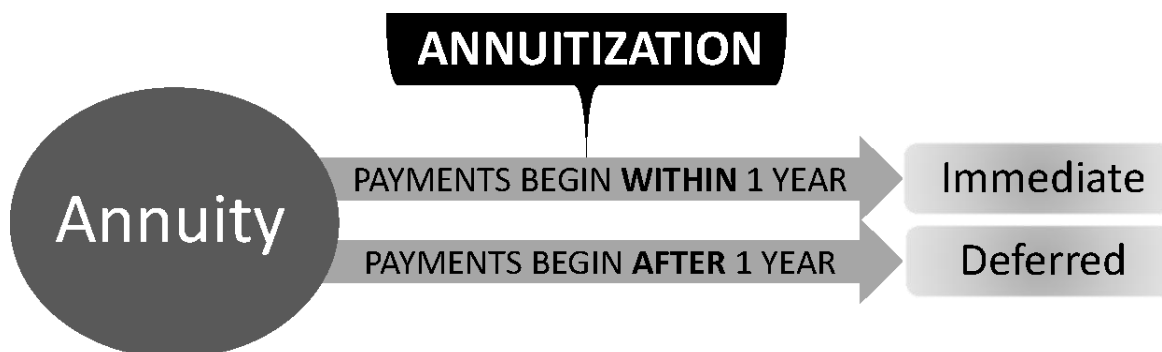


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Immediate Annuities

A. Introduction to Single Premium Immediate Annuities



Single Premium Immediate Annuities, or SPIAs as they are commonly known, are an annuity product designed for the person who needs income now, or at least within 13 months of purchase. This product, once much maligned by the financial press and many financial practitioners, is gaining popularity as demonstrated through its increasing sales results over the last several years. In fact, there are predictions that SPIA will one day emerge as a fundamental part of the income portfolio for every retiree.

Of all types of annuities sold today, SPIA accounts for the smallest sales totals. In fact, in 2010, fixed immediate annuities represented only about 3.4% of total annuity sales. However, there is definite opportunity for the use of SPIA in helping people eliminate the risk of outliving their retirement savings.

Although SPIA may be appropriate for delivering secure retirement income for retirees of all financial demographics, a significant and underserved market may exist among middle-income seniors. Statistics indicate that many middle-income retirees, those with incomes between \$25,000 and \$75,000, tend to have a gap between their guaranteed income and their basic living expenses. These less wealthy retirees may not have access to rich pension plans or large saving balances. They also often have lower tolerance for risk, and tend to contribute primarily to conservative financial products such as CDs and cash equivalents. In recent times of low interest rates, the declining income generated from these investments is not always enough to keep up with retirement living expenses.

Often persons in this demographic are not approached with solutions to manage their income risk. Traditional brokers typically seek to serve the more affluent, or are selling investment products rather than protection against the longevity risk. In fact, 51% of pre-retirees and retirees with incomes between \$25,000 and \$75,000 have not been

contacted by any kind of retirement professional in the past 12 months. These persons, who may be particularly at risk for not being able to maintain their standard of living during retirement, are often unaware of products like SPIA that may offer them the retirement security they need.

It is important to recognize that the objectives of accumulating income for retirement and distributing it when retirement occurs are very different. Persons who have reached retirement are generally trying to maximize their income while maintaining a desired cushion or safety net of assets. Their risks differ from the risks that face those saving for retirement as well.

1. Types of Risk

The most apparent of these risks is **longevity risk**, or the risk of outliving one's resources. We have discussed the uncertainty factor around two other retirement "annuities" that retirees today rely on heavily: defined benefit plans and Social Security benefits. We have also focused on the strength of annuities in eliminating longevity risk with their lifetime guarantees.

Two other risks that are equally important to protect against in retirement are withdrawal risk and sequence of return risk.

Withdrawal risk is the risk that the retiree draw too much from their investments to be sustainable throughout life. This risk can lead to wiping out the value of the portfolio too early. Many financial advisors have used a "4% rule of thumb." They have advised that most people will not outlive their savings by following the rule of taking no more than 4% from their savings each year. However, with market performance of recent years, and interest rates at record lows, this rule may no longer apply.

Sequence of returns risk is another acute challenge for those drawing income from investments. This risk centers on the order, or sequence, of market fluctuation, and how it affects portfolio growth. This sequence becomes highly critical in retirement when retirees are "drawing down" from their portfolio to provide regular income. If a retiree's portfolio suffers negative returns early in retirement, the growth of the nest egg will not keep pace with the annual withdrawals. Unless the portfolio funds are increased, continued withdrawals can have a drastic impact on the amount of income that can be withdrawn. The only "fix" for the sequence of returns risk is to reduce the income taken from the portfolio, or improve the market performance.

These risks combined can greatly jeopardize the probability of maintaining the regular and targeted amount of income needed to ensure a secure and comfortable retirement. SPIA can be an ideal solution for mitigation of these risks, and bears [consideration](#) in the distribution planning for nearly every retiree.

B. The Basics of SPIA

The SPIA is a straightforward, uncomplicated product concept. Individuals purchase these annuities when they want to begin receiving a stream of income within a short period of time. Quite simply, purchase payments go to an insurer, and the insurer converts those payments into a stream of income. While other annuity products are important for the accumulation of savings for retirement, SPIA is designed solely for the distribution of income. Unlike other annuity products, there is no accumulation phase. Instead, purchase payments are converted to income within 30 days to 13 months of [contract](#) purchase.

Any lump-sum purchase payment of cash can be converted into an income stream for the preferred duration, which could be for the lifetime of one or more individuals, or for the period specified by the annuity purchaser for the designated annuitant to receive payments. Annuitants can receive their payouts on a monthly, quarterly, semi-annual, or annual basis based on their income needs and lifestyle.

People typically purchase SPIAs at the time of their retirement to ensure that their basic income needs are met, or when already in retirement to boost the income they are already receiving from other sources. SPIAs are often marketed as a "personal pension plan" or a "retirement income paycheck" that can be guaranteed for life. They bring peace of mind to retirement because the income they provide is stable and secure, and cannot be outlived.

SPIAs can be purchased at other times during life, as well. Persons that receive lump sums of cash from inheritances, legal settlements, lottery winnings or the sale of a large asset, like a business or home, have also used SPIAs to dependably deliver a constant paycheck that could potentially last for life.

C. How Income from SPIA is Determined

SPIA is one of the most efficient retirement income products available to retirees. It maximizes the cash flow that is available per dollar of retirement saving. This is possible because of the pooling of the risk of outliving assets among large groups of contract holders. The pooling of mortality risk among insureds is one of the basic concepts that enables insurers to offer the unique guarantees which differentiate their products from any others in the financial marketplace. In pools of hundreds of people, statisticians know that at least some persons will die before their life expectancies, while others will live well beyond what actuarial tables predict. These staggered results allow insurers to maintain guarantees for life from the investment of these purchase payments.

SPIA payments are also maximized due to the fact that the purchase payment principal is liquidated as the payouts are made. This concept is easiest to understand when compared to a CD. Retirees who depend on CD income receive only the interest that the CD principal generates. The interest amount is locked in for the term of the CD, but when the CD matures, the retiree faces reinvestment risk. In other words, if interest rates are lower, the retiree must accept a lower rate of return when investing in a new CD at that time. Between the years of 2005 and 2010, for example, the average rates of CDs with a one-year term have dropped from near 5.25% APR to 1% APR or less. An investor with a \$100,000 CD would have seen annual income drop from \$5,250 to \$1,000. This lack of certainty can cause great concern for retirees that rely on CD income for a significant portion of their retirement income.

Because immediate annuity payments include both liquidated principal and earnings, the payout rates that can be guaranteed generally compare very favorably to other fixed rate investments. Depending on the age of the annuitant, payout rates for income for life option can range from 5% – 10% or more. As you can imagine, this type of income boost can be very important for those persons that truly need additional income to live in retirement. Furthermore, there is no uncertainty about the amount of payment that will be received in the future. The payment is locked in for the term of the payout, with no uncertainty regardless of changes in the economic and interest rate environment. Unless the individual is willing to take more risk, and has little concern for payment stability, most individual investment plans are hard pressed to match the guaranteed income an immediate annuity can provide.

The amount of income that SPIA delivers is determined by these **4 elements**:

1. Interest Rate;
2. Size of the Initial Investment;
3. Pay Period; and
4. Length of the Contract.

The highest monthly payments are realized from larger investments with shorter payout periods.

The trade-off for the income boost that SPIA provides is the loss of control of the purchase payment. At the death of the annuitant, there may be no principal to pass on to heirs as there is with a CD. For this reason, and others yet to be discussed, it is usually important to recommend that immediate annuities are purchased only with a portion of retirement savings. Many financial practitioners have used a “rule of thumb” to recommend that no more than 25% to 40% of savings be allocated to SPIAs. By investing only a portion of retirement savings into an immediate annuity, a liquid fund remains for emergencies, and the remainder of the savings can be invested for long-term growth.

When SPIA is used as a portion of an overall retirement income portfolio strategy, it can take pressure off of the performance of the rest of the portfolio. *For example*, if based on the assets a retiree has accumulated, it is determined that a retiree needs income of 5% annually, the use of SPIA in the mix can allow for the rest of the portfolio to return less in down years and still meet the income needs of the retiree. If the retiree’s goal is to have 5% income from the retirement nest egg and 40% is allocated to SPIA (at 6.5%), then the rest of the portfolio only needs to produce 4% income. This, in turn, can allow for the remainder of the portfolio to be invested more aggressively for growth as well as income. The amount of the savings that are not invested in the SPIA can also be used to pass an inheritance to heirs.

This portfolio strategy helps offset the discomfort that some people have with giving up control of the SPIA purchase payment amount. In the long run, the investment growth of the assets that weren’t used to generate income can offset the liquidated SPIA assets, and grow to a generous legacy over a long retirement.

D. Immediate Annuity Contract Features

At the time of the purchase of a single premium immediate annuity, there are basic considerations that are part of the [application](#) process. Features may vary between insurance companies that issue the product. In addition to these contrasts in features, it is certainly important to consider the financial strength of the insurance company that stands behind the product guarantees. These insurers could be responsible for ensuring retirement security for as long as 20 to 30 years or more. Their financial ability to deliver on this promise should not be underestimated.

Issue Ages: Issue ages vary greatly, and can range anywhere from age 0 to 90 or 95. Although typically purchased at retirement, immediate income annuities can serve other purposes, such as for the payment of legal settlements and lottery winnings, which is why they are available to a broad age range. Younger purchase ages result in smaller payments when spread over a life expectancy. However, if a period-certain payout option is selected, there is no difference in the payout amount regardless of age.

Minimum Purchase Amounts: Although this varies, usually the minimum purchase is \$10,000 or more. At younger ages, the lifetime income generated by a relatively small

contribution may seem insignificant, but at age 80, it can be substantial. Many companies also stipulate a minimum payment amount, such as \$50. *For example*, if a relatively small purchase amount generated income of \$40 on a monthly basis, the insurer would not allow a monthly payment frequency because of the administration expense. Instead, a quarterly or annual frequency may be required.

Maximum Purchase Amounts: Many companies will state a maximum purchase payment of \$1 million-\$5 million, but often require home office permission before accepting applications for contracts of more than \$1 million. Financial advisors should also recommend diversification between companies for extremely large purchases. Although the risk of financial failure by insurance companies may be slight based on historical performance, it is a sound practice to divide large purchases among different high quality.

Contract Administration Charges: Although many companies charge no administration fees either initially or annually, some companies may charge a one-time only set-up fee particularly when the purchase amount is relatively small. An example of this type of fee is a \$100 charge for contracts of less than \$100,000. The fee is subtracted off the top, and the net amount that remains is used to purchase the income benefit.

Banding: Some companies may encourage larger purchase payment deposits by offering higher payout rates for larger deposit amounts. Other companies offset the smaller purchase payments by an administrative charge as just described above.

Rate Locks: Often the purchase process of SPIAs involves a [transfer](#) of funds from another source. Perhaps this process may involve waiting for a CD to mature to avoid an interest penalty, or an administrative process concerning a mutual fund or pension plan that takes several weeks. Insurers that issue SPIA contracts periodically revise their payout rates to reflect changing market [conditions](#) and affordability.

What if an illustration using a certain payout rate was presented to a customer, and then there is a subsequent payout rate change while waiting for funds to arrive from other sources? The concept of rate lock defines how long the quoted payout rate that was presented at the time the sale took place will be maintained.

For example, if an insurer establishes a 60-day rate lock, this usually means that the payout rate quoted will prevail for 60 days from the date of application. If payout rates for other new contracts were to fall during that period, the additional funds to complete the contract under rate lock would qualify for the higher payout rate. What happens if payout rates for new contracts increase during the rate lock period? Some insurers extend the new higher payout rate, while others may hold the original payout quote. Provisions like the length of rate lock and impact of rate changes on fund transfers vary from insurer to insurer, and are important to understand when money for funding the contract is coming from other sources.

Potential Tax Benefits: Immediate annuities that are funded with nonqualified assets can provide some significant tax benefits to annuitants. Because a nonqualified [contract](#) is funded with assets that have already been taxed, each payment is considered part a return of principal, which is not taxed, and part earnings. Only the portion of the payment attributable to earnings is taxable, which can present a significant tax advantage over other investment earnings. Our course will address taxation of annuity benefits in greater detail within a later section.

Note that if funds for the immediate annuity purchase payments come from IRAs, 457 plans, 401(k) plans or other qualified plan rollovers or transfers, this special tax treatment does not apply. Payments based on funds from these qualified sources are fully taxable to the annuitant because they include no cost basis of already taxed earnings. However, taxation is at least partially postponed since it is spread out over the entire length of the annuity distribution instead of applied to a lump-sum distribution.

Contract Type: While the majority of SPIAs that are sold are fixed benefit contracts, variable immediate annuity benefits are also available. A fixed immediate annuity contract offers the consistency and stability that many retirees find important. Once determined, the amount of income that is payable for each period is a specified amount. Variable immediate annuities may guarantee a minimum benefit that is payable for life, but the amount of the regular payments benefit will vary with the performance of the insurance company's investment portfolio.

Payout Options: Insurers that issue SPIAs offer great flexibility in income payment options that annuity owners may choose from. An important part of determining suitability in the sales process is to determine the payout option that best fits the needs of the annuitant. The options that an insurer makes available for immediate annuitization are often the same options that are available for annuitization of other annuity contracts that insurer issues. In other words, when annuity contract holders are ready to annuitize other fixed, index or variable annuities of that issuer, they typically have access to the same payout options available to purchases of SPIAs.

As you might expect, both the length and the strength of the guarantee affect the payout option. Those payout options that offer more guarantees will result in lower income for the same purchase payment. Insurers usually offer a choice in payment frequency, and typical choices include monthly, quarterly, semi-annual or annual payment modes.

1. Annuity Payout Options

The standard payout options that are available in immediate and deferred annuities are described below.

Fixed Period

Fixed Period: Also called fixed installment or period-certain payout options, a fixed period guarantees the time for which annuity payments will be made. Common periods include 5, 10, 15 or 20 years. If the annuitant dies during the payment period, the remaining benefit is paid according to the terms of the [contract](#). If the annuitant lives beyond the fixed period, a benefit is no longer paid.

This choice is often useful for retirement distribution planning when it makes sense to defer receipt of other benefits for a period of time. *For example*, many retirees choose to defer receipt of Social Security payments to take advantage of the increase in benefit payments that results from deferral. By waiting until age 70, the Social Security payment amount can increase nearly 70% over the benefit available at the early retirement age of 62. The use of a period-certain annuity payout can maximize income during the waiting period. It can take the place of Social Security until the payments begin on the delayed date retirement. The net result of this strategy can be a higher stream of income for all of retirement.

When considering this strategy, it is important to consider the impact of low interest rates on period certain payout options. The shorter the payment period, the less time

the insurer has to achieve profitable investment returns to offset contract charges. There may be situations when the total payouts of a short installment period do not equal the total purchase payments. *For example*, if a 5-year period certain is elected during a time of low interest rates, and 60 monthly payments are to be made, after the contract charges (administration, sales commissions, premium taxes, spread, etc.), the total of the 60 monthly payouts could be less than the lump sum invested. Many insurers will not allow the election of period certain options in this circumstance.

Fixed Amount

Fixed amount: A [contract](#) owner can determine the amount to be paid in each payment. With this choice, the term for which payments are made is defined at the time of annuitization, and varies based on the amount to be paid in each installment. There is no lifetime guarantee associated with this option. If death occurs before the full purchase payment amount has been distributed, the amount that remains is paid to beneficiaries according to the terms of the contract.

Life Options

Life only: A life only payout option ensures lifetime income to a single annuitant for the remainder of life. The risk with this option is that if death occurs before payout of the full value of the investment, there is no provision for payment to a [beneficiary](#). This option generally results in the largest payment amount, because the potential of the premature death of the annuitant is not protected.

Life with period certain: This option is one method of providing beneficiary protection to a lifetime income option. If chosen, this option guarantees payments made throughout the lifetime of the annuitant. However, if the annuitant dies before the [expiration](#) of the period certain selected (often 5, 10, 15 or 20 years), the named beneficiary receives payments for the remainder of the period. If death occurs after the expiration of the period certain, no benefit is payable to a beneficiary. A longer period certain creates a longer guarantee period, so the longer the guarantee period chosen, the greater the reduction in payout amount.

Life with refund: Under this option, the annuitant receives income guaranteed for life. However, if death occurs before the full amount of the purchase payment has been paid, the remainder is paid to a named beneficiary. If death occurs after full purchase payment amount has been paid, no benefit is payable to a beneficiary.

Life with refund can involve either a cash refund option or an installment refund option. When a cash refund option is chosen, the remaining benefit is payable to the beneficiary as a lump sum. If an installment refund option is chosen, benefits are paid to the beneficiary according to a scheduled frequency selected by the [contract](#) owner, and may be subject to certain IRS rules that require full distribution within 5 years of death. We'll cover this tax concept in more detail in a later section of this course.

Joint and Survivorship

Joint and survivorship options: Annuity payout options may guarantee benefits for 2 lives. With this option, the [contract](#) owner may also need to choose the amount of the benefit payable to the [beneficiary](#). The most common of these options are joint life with 100% to survivor, and joint life with 50% to the survivor, although there are others available. Under the 100% option, the payment after death of the first annuitant that continues for the life of the second annuitant is the same as the original amount. Under the 50% option, the payment is cut in half after the death of the first annuitant.

Inflation adjusted lifetime income: When surveyed, a large number of retirees identify inflation as one of their biggest concerns in retirement, as well it should be. Even if inflation averages a modest 3% over the next 20 years, the purchasing power of a fixed, never-changing payment declines by almost 50% over that 20-year period. Many insurers offer inflation protection as an annuitization option to address this concern. Both single and joint life payout options often offer inflation protection.

An inflation adjusted income payment comes with a price. It results in a lower initial payment when compared to non-inflation adjusted options. As inflation adjustments are made over time, the benefit can increase well beyond the amount paid by a non-inflation adjusted options.

As you can see, immediate annuity payments can be structured in numerous ways to meet the specific needs of your client, and to fill an important role within the overall retirement distribution plan.

2. Recent Innovations in SPIA Products

Insurance companies continually respond to the changing needs of the market and release new and improved features. When compared to other annuity products, the SPIA is much more “plain vanilla,” but [contract](#) innovations are popping up that address prior product restrictions and offer new planning [application](#).

Liquidity Features

One of the biggest considerations in the purchase of a SPIA is the loss of liquidity. Life happens, and often there are needs for access to funds that could not have been anticipated. A recent LIMRA survey found that the loss of control of the assets used to purchase the income annuity and the lack of liquidity are the two greatest objections to income annuity purchases. Having some element of liquidity allows for the benefit of an income stream for life, while mitigating the objection to loss of control of assets.

The types of liquidity benefits available are many and varied. In general, they can fall into several categories:

- Acceleration of benefits;
- Withdrawal of [contract](#) value; or
- Cash refund of the premium not yet received.

The acceleration benefit typically allows the contract owner to elect an advance payment of benefits to be paid in a future period. *For example*, an acceleration of the next 12 months' worth of benefits might be payable if this benefit is exercised. There are typically a maximum of 1-2 elections of this benefit for the duration of the contract.

The withdrawal option is sometimes expressed as the option to take up to a certain percentage of the original purchase payment or current commuted value of the contract. Typically, there is a maximum percentage that ranges from 10% to as much as 30%. Usually there is a waiting period before this benefit can be utilized; a common waiting period is 3 years.

A cash refund feature may also be available, and could allow for cashing in a certain portion of the remaining contract value, up to the full contract value. The commuted value that remains after reduction by prior payouts, is then paid to the annuity owner. There may also be a waiting period before this benefit is available.

Regardless of the type of liquidity options, there are fees that must be paid when they are elected. The chance that any one of these benefits may be selected impacts the investment strategy of the insurer. To have flexibility to meet these benefits has a cost that the insurer passes on to the contract owner. These fees may be imposed in a variety of ways, including

- An upfront calculation that would reduce the subsequent monthly payment after the benefit has been received;
- Flat or percentage base fees that are imposed at the time the liquidity feature is exercised;
- An interest rate adjustment that is used to reduce the commutated value of the contract; or
- A flat percentage applied against the commutation value that reduces the amount available for future payouts.

Deferral Features

Delayed or deferred income options (DIOs) are a relatively new development that can be sold separately or added to existing products. Also known as longevity insurance, these contracts begin providing payments after the traditional window of up to 13 months that is defined by immediate annuities. Payments under DIOs are often deferred to a future established age, such as to begin at 85, so that retirees do not outlive their assets. The cost for these benefits is relatively low because of the payment delay. These contracts or riders can have great value in reducing the fear of outliving benefits. They can allow for maximization of other income streams from retirement assets since the risk of living beyond a certain age can be mitigated.

Medically Underwritten Immediate Annuities

Persons with known medical [conditions](#) may find that the normal lifetime expectancies that are factored into standard lifetime payouts are a disadvantage. Some companies have chosen to offer medically underwritten immediate annuities. The advantage of these contracts is that payouts are made based on a shortened life expectancy that reflects the medical condition, resulting in higher payments. Buyers that get the greatest value from a SPIA contract are those that live longer than the actuarial average lifetime calculations, so persons with known life-threatening medical conditions may not find nonmedically underwritten SPIA payouts with single lifetime guarantees to be of good value.

E. SPIAs and Suitable Sales

The benefit of immediate annuities — an income stream guaranteed for life — is a tremendous value as individuals become increasingly self-reliant in creating their post-retirement finances. They can be an advantage in most any retirement portfolio and warrant careful [consideration](#) along with the other portfolio components that will create the desired income stream.

Obviously, the sales process will require careful suitability determination, and the questions below are a start in determining when an immediate annuity is appropriate or if a different annuity or alternative investment is a better fit.

- What is the purpose of the income stream? Is it needed to cover basic expenses or for discretionary purposes?
- How much additional income do you need on a monthly or yearly basis?
- How long will you need this income stream?
- Are you more concerned with supplementing your income now or growing your assets for later use?

- Are you concerned with leaving a legacy? Do you have children or other family members who have special needs that you wish to support after your death?
- Do you have other assets that can be invested now for later use?
- Do you want to build in cost of living increases?

1. Application

Meet Mary. Mary is retiring in 6 months and is worried about what to do when she does not have a regular paycheck coming in each month. She has seen many ups and downs in the market, and doesn't want to worry about market volatility. The idea of a steady, worry-free retirement income is appealing. She will begin to draw Social Security in 6 months, and will also benefit from a defined-benefit pension plan payment of about \$500 per month. Although she thinks these sources will meet most of her basic needs, she likes the idea of an extra \$1,500 per month that she can use to travel and enjoy without guilt. She has \$300,000 of retirement savings in a 401(k) plan, and is willing to use some of this money to meet her retirement objectives. She also would like to leave an inheritance for her grandchildren to help with their college education in the event of her death.

After reviewing the options with her financial adviser, Mary selects a single life, fixed immediate annuity with the cash refund option. At her death, if the total of payments received is less than her net purchase payment, the difference will be paid in a lump sum to her grandchildren. She likes the comfort that the extra retirement paycheck provides, and is especially pleased that she doesn't need to worry about fluctuations in her monthly income. She feels that giving up control is worth the income security, and is confident that her retirement income choice will suit her needs.

Given Mary's objectives, risk tolerance, and other retirement assets, the SPIA option works extremely well in helping Mary ensure a comfortable retirement lifestyle.

Although it is clear that immediate annuities can deliver tremendous advantages in retirement income planning, they are not without risk and disadvantages. In ensuring suitability, producers and insurers must take a fair and balanced approach to every product recommendation. Understanding the advantages and disadvantages of this product can help you, as a producer, make appropriate recommendations for appropriate retirement solutions for your clients.

2. Seven Advantages of Immediate Annuities

1) **Predictable Income Stream for Life:** A steady retirement income paycheck is one of the greatest benefits that SPIA provides. With 96% of retirees worried about outliving their income, this is a critical risk management benefit.

2) **Income Your Way:** The income payout options that SPIA delivers are numerous. Whether for one or two lives, for a period certain, with or without [beneficiary](#) protection or with or without inflation protection, the SPIA owner can tailor payments to meet the needs of nearly any retirement income plan.

3) **Simplicity:** Sometimes the simplicity of this benefit is its greatest advantage. The idea of a steady stream of income that never changes, regardless of market performance, is peace of mind to many retirees who do not want to assume the responsibility of money management.

4) **Maximization of Cash Flow:** For those persons who need to maximize the income producing ability of limited amount of retirement assets, SPIA is the most efficient income maximization product available. Through [liquidation](#) of the principal and earnings combined, SPIA offers certainty and a payout percentage that is hard to beat.

5) **Improved Returns over other Alternatives:** Other investment alternatives like CDs, other fixed annuities, mutual funds, etc., can generate a steady income, but the payout rate that SPIA delivers is higher because the principal and earnings are combined in the income stream.

6) **Favorable Tax Treatment:** When SPIAs are funded with nonqualified dollars, only a portion of the income is taxed. By contrast, CD income, most mutual fund income, and other retirement income paychecks are fully taxable.

7) **Protection from Creditors:** Immediate annuities provide a constant income, even during financial hardship. Many states in the US offer protection from attachment by creditors, so that even in bankruptcy, the income stream continues.

3. Seven Disadvantages of Immediate Annuities

1) **Locking in Low Rates:** By making a single immediate annuity purchase when interest rates are low, annuity owners lock in a payout rate that will not change. Although the payout rates that may be received through the SPIA are potentially higher than other currently available alternatives, there is no opportunity for increased payments when rates rebound.

2) **Loss of Control:** Once the funds are turned over to the insurance company, the annuitant has lost the ability to direct the use of these funds. They are no longer available for emergencies, for alternative investment opportunities, or as an inheritance for heirs.

3) **Lack of Liquidity:** No one knows when life emergencies will occur. SPIAs offer limited, and in some cases, no liquidity for emergencies. Purchasers should always have sufficient emergency funds available if SPIA is chosen to supply retirement income.

4) **Low Returns:** The general account of the insurance company invests conservatively. The annuity returns that are combined with principal to determine the SPIA payouts, may be well below returns achievable from other investment vehicles.

5) **No Changes:** When a SPIA payout choice is made, there are almost no opportunities for change. It is difficult for anyone to be sure about making a choice that is right for potentially 30 years in the future.

6) **Commissions and Fees:** The payouts made from SPIA are reduced by commissions for sales representatives and fees for insurance company administration. These charges can be substantial, and may be a high price for the loss of control.

7) **Adverse Selection:** Although the pooling concept of insurers can benefit those that live beyond their life expectancies, according to actuarial tables half of the people will not achieve these life expectancies. This group is contributing mortality credits to the payouts of those that live long lives. The [beneficiary](#) protection options protect against this, but more of the mortality credits are extended to those that live beyond life expectancy.

Chapter Complete

