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FACT SHEET

Annuity Basics

CANHR is a private, nonprofit 501(c)(3) organization dedicated to improving the quality of care and the quality of life for long term care consumers in California.

There are many types of Annuities

An Annuity is a purchased insurance policy that pays a fixed amount of benefits. Most annuities are "immediate" annuities that pay fixed monthly amounts for the life of the person who is entitled to those benefits, or for a determined period of time, e.g. 15 years. In a "simple life annuity" when the person receiving the annuity dies the benefits completely stop; there is no final lump sum payment and no provision to keep paying benefits to a spouse or other survivor. A "continuous annuity" pays monthly installments for the life of the retired person and also provides a smaller continuing annuity payment for the person's spouse or named beneficiary after the person's death. These annuity contracts are usually with insurance companies and often have high upfront commissions and severe penalties if money is withdrawn earlier than the contract allows.

The Two Most Common Types of Annuities

- The Immediate Annuity or Income Annuity - A lump sum of money is invested in the annuity and the annuity "immediately" begins paying out a stream of income to the designated person.
- The Deferred Annuity - Payment of proceeds is put off (deferred) to a predetermined future time, e.g., 5, 10 or 15 years after the money is put into the annuity.

Creating the Annuity – The Premium

- Single Premium- A one-time single cash contribution is made and no further contributions are allowed. Immediate and Income Annuities are always Single Premium.
- Flexible Premium- Multiple contributions at different times are being put into the annuity policy. These contributions will affect how much the policy pays out.

Getting Money Out of an Annuity - Annuitization Options

Annuitization Options are the choices an annuity holder has on how to receive the annuity value other than in a lump sum. The Annuity Owner chooses how he or she wants the payments to be made. Common annuitization options are:

- Life Only - Payments from the annuity stops when the annuity owner dies.
- Life With Period Certain – Payments are guaranteed to be made to the annuity owner for an agreed upon time or for as long as he or she lives, but if the owner dies before an agreed upon time period, then the beneficiaries will be receiving payments until that agreed upon time has lapsed.

- Period Certain – The annuity stops paying out at an agreed upon future date, e.g. 10 or 15 years, even if the annuity owner is still alive.

Rate of Payout and Crediting Methods

- Fixed- Interest rate is declared each year by the company. The interest rates tend to be fairly low, but these products are generally considered the most stable and conservative. Agents selling these products are required to have a Life Insurance License.
- Variable- The amount of payouts is tied to the performance of the investment accounts much like a mutual fund. The client can usually pick among different funds, depending upon his or her risk tolerance. This product requires the insurance agent to have a special license to sell securities.
- Index- The insurance company tags the accumulation value to an index like the S&P 500 or the Forbes 500. The cash value moves up or down in concert with the index. These products are complex and tend to be very difficult for the average person to understand. The interest rate can have a maximum "cap"; there can be a "participation rate"; some have "floors" while others have "thresholds"; and the crediting rate itself can vary, with "point to point", "annual reset", and "high water mark" the most common methods. Index Annuities only require the Agent to have a Life Insurance License.

Death Benefit

The amount the Beneficiary receives upon the death of the annuitant. The important thing to note here is that some annuities reduce the Death Benefit by the Surrender Charge while others do not.

Surrender Charges

A surrender charge is a penalty for making an early withdrawal. Surrender charges vary greatly from annuity to annuity. Generally speaking, the higher the surrender charge and the longer the surrender period, the higher the commission is to the agent. High surrender charges tend to be a common denominator in abusive annuity sales to seniors.

Take Your Time and Get Second Opinions

Never rush into a decision to purchase an annuity. Have the agent give you a written statement why he or she thinks the particular annuity is suitable for your needs.

Questions? Call CANHR at (800) 474-1116 or visit CANHR's website at www.canhr.org