the pros & cons of annuities

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WHAT IS AN ANNUITY?

An annuity is a contract between you—the annuitant—and an insurance company. In return for your contributions, the insurer promises to pay you a certain amount of money, on a periodic basis, for a specified period. Many people buy annuities to use as a source of retirement income, guaranteeing them a regular income stream after they've left the workforce, often for the rest of their life.

There are three main types of annuities:

- Traditional Fixed Annuities
- Fixed Index Annuities
- Variable Annuities

Traditional Fixed Annuities

A traditional fixed annuity can guarantee an interest rate for a predetermined number of years. They can also provide stable income for those who prefer protection over growth.

Fixed Index Annuities

A fixed index annuity can provide guaranteed income with protection of principal from market losses and has the potential to provide higher interest earnings that are tied into a specified market index. There is typically a limit on how much interest you can earn.

Variable Annuities

A variable annuity is for those who are comfortable with a higher risk. This annuity is invested in your advisor-managed portfolio. Like fixed annuities, taxes are deferred until you receive income. However, variable annuities are linked to the market and have potential to lose money in a market decline.

PROS OF AN ANNUITY

Annuities are a unique way to grow your retirement savings portfolio. Because annuities can essentially work as an insurance for your retirement account, they have become popular.

1

YOU WILL RECEIVE REGULAR PAYMENTS

These payments provide supplemental income during your retirement and can help if you have not saved enough for regular expenses. The value and number of annuity payments varies depending on the type of annuity and terms of the contract.

2

CONTRIBUTIONS CAN GROW TAX- DEFERRED

The money that you contribute to an annuity grows tax-deferred, meaning you do not owe taxes on the growth of the account until you start receiving payments.

3

FIXED ANNUITIES OFFER GUARANTEED INTEREST CREDITS

For fixed interest and fixed index annuities, the insurance company will invest any money that you put into an annuity. While there is always some risk involved in

investing money, a fixed annuity contract include guarantees that prevent you from losing money. Fixed annuities guarantee you make a certain percentage on your initial principal.

4

DEATH BENEFITS ARE TYPICALLY AVAILABLE

Variable annuities carry the risk for you to lose money, but they also provide a death benefit. This means that the insurance company will make a payment to your beneficiary if you die. The death benefit is usually equal to the amount contributed to the annuity, regardless of how the annuity performs.

Fixed interest and fixed index annuities do not have market risks and they also provide a death benefit. Fixed annuities typically pay the account value of the annuity.

CONS OF AN ANNUITY

There are some disadvantages of annuities, for example fees and returns.

1

ANNUITIES CAN BE PRICEY

Any time you consider an annuity contract, you should understand all fees that come along with that.

At the core, fixed interest and fixed index annuities do not have any fees. However, you could get enhancements such as death benefits or income riders that may have a fee.

Surrender fees are common with variable and fixed annuities. A surrender fee applies when you make more withdrawals than allowed during the surrender period.

Variable annuities do have fees. These fees include maintenance and expense fees, investment management fees, and optional rider fees that may be added to the annuity.

2

RETURNS MIGHT NOT MATCH THE STOCK MARKET

While the stock market may make gains in a good year, your annuity will not grow by the same amount as the stock market. Variable annuity fees might be

one of the reasons for that difference. For fixed index annuities, caps or participation rates may be the difference in growth, as well.

Contributions to annuities are tax-deferred, but any withdrawals you make will be taxed at your regular income tax rate, not the long-term capital gains tax rate.

3

SURRENDERING YOUR ANNUITY

Some annuities have a surrender period. There could be a fee to exit during the initial period, subject to insurance company and annuity plan.

WHAT DOES THIS MEAN?

An annuity is a way to grow as well as supplement your income for retirement. For some, this is a good option because it can provide regular payments, tax benefits and a potential death benefit.

However, there are cons to keep in mind, the biggest one being the costs associated with variable annuities. Each annuity will come with different fees which will vary depending on your contract.

Reach out to a wealth advisor to be sure an annuity is the right move for you.

https://smartasset.com/retirement/pros-and-cons-of-annuities#q=annuities

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