EDUCATIONAL COMMENTARY

For consumers

ANNUITIES CAN SERVE MULTIPLE ROLES IN YOUR RETIREMENT PLAN

When it comes to adding annuities to your retirement portfolio, there's no one-size-fits-all answer. Make a plan to see the different ways they might be a good fit.

When Jeannette Bajalia retired at 55 from an executive job at a major health insurer, she looked at her finances and asked: "Do I have enough to get to 105?" The underlying question — will I outlive my assets? — is a common fear among retirees, and with good reason.

The Center for Retirement Research at Boston College says that longevity is the biggest risk retirees face. In Bajalia's case, seeking answers to shape her retirement led her to embark on a second career in wealth management helping individuals and couples plan for their future. Now 69, as president of the wealth management firm Petros Financial Group in Jacksonville, Florida, she creates defensive retirement plans that typically include annuities.

"The plan will tell what you need, whether it's one annuity, two annuities or more, or none," Bajalia says. "We don't just put clients in annuities and say you're on your own."

START WITH A FINANCIAL PLAN

Having cared for her mom who lived to 93 and her aunt who lived to 100, Bajalia is keenly aware of the risks of longevity, widowhood, and outsized medical expenses. With her own plan, she was looking for predictability and safety, with some upside, so she could potentially leave a legacy to her four sisters. It was also important to build in flexibility. If you're single, what if you get married? If you're a two-earner couple, what if one or both or you get laid off? What if one of you dies prematurely? "A proper plan can lay the foundation that gives us flexibility if we encounter unexpected life events," Bajalia says.

THINK BEYOND SOCIAL SECURITY

One misconception many people have about retirement is that their monthly Social Security benefit check will cover their living expenses. "People think Social Security is the answer!" Bajalia says. When her dad passed away, her mom's Social Security check as a widow was just $562 a month. After one spouse dies, the survivor gets one Social Security check, not two, and still might have big ongoing expenses like a mortgage to pay off. A financial professional can help you project your Social Security benefits; it's a key first step of a retirement plan.

The next step is to assess any other sources of lifetime income. Do you or a spouse have a pension from your current or former employer? If so, what is the survivor benefit? Once you estimate your projected income from these sources, calculate how much you expect you'll need for core retirement expenses, including housing, transportation, food and healthcare expenses. That's the gap you'll need to cover. One way to provide that extra income to fill the income gap is with annuities.

THINK OF THREE BUCKETS TO HOLD YOUR WEALTH

Bajalia uses a three-bucket approach to wealth planning. Each one might contain annuities, depending on client needs and risk tolerance.

Bucket one is for safety and covers the income gap for immediate financial needs for 18 months to two years. Money for planned expenses sits in cash, not exposed

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to market risk or is held in CDs (certificates of deposit) or an annuity. The rest, an emergency rainy day fund, could go into a fixed annuity. The insurance company that issues the fixed annuities gives a little better interest rate than your bank. Plus, if structured accordingly, they can serve as a stream of protected income.

Bucket two covers year two to year 10. If you know your income gap is $2,000 a month, you could get an annuity to cover that. One option is an annuity with a guaranteed lifetime withdrawal benefit. You put money in today, but don't have to get immediate income. Instead, you pick when you want to activate the income. The longer you defer payouts, the higher the payouts become. For added flexibility, you could get two annuities. By activating one in say five years, and another one in say 10 years, you'd get more money than just putting everything in one annuity.

Further, it has a value if you die; you name your loved ones as beneficiaries.

Bajalia used this approach herself at age 55. She kept half of her savings in a brokerage account in the market, and used the other half to buy two deferred income annuities. "It gave me flexibility for life's unknowns," she says. "I expected to activate the two annuities at 65, but since I'm still working, I've deferred both for longer than expected." The same thing is happening to many of her baby boomer clients. They start businesses, or their employer calls them back to do contract work. In the meantime, the annuities are growing in value, leaving her even more protection for her older age.

Bucket three is the investment bucket. Some people don't need an annuity for income. They might have a sizable pension with a 100% survivor benefit. If they're risk averse, they might consider an annuity strictly as an accumulation vehicle in this long-term bucket to manage risk. If your investments grow over time, consider using some of the proceeds to buy more protected income. When Bajalia's investment bucket grew by $100,000, she used that $100,000 to buy a third annuity. By moving risk-based investments to protected guaranteed sources, adding to bucket two, she's gotten more protection as she ages, she says.

ANNUITIES ADD SECURITY TO YOUR PLAN

It's important for everyone to have a financial plan that protects their financial well-being. The plan informs how much to put in annuities, how much to invest, and what level of risk you take in your investment strategy. "Annuities can have a powerful role in planning," Bajalia says. But they work best as part of an overall financial plan that you lay out and reassess periodically to account for life changes.

Learn more at Resources.ProtectedIncome.org

Annuities are long-term investments designed for retirement purposes. The value of variable annuities is subject to market risk and will fluctuate. Product guarantees are subject to the claims-paying ability of the issuing insurance company. Earnings, when withdrawn, are subject to federal and/or state income tax, including a 10% tax penalty for withdrawals before age 59½. Some income guarantees offered with annuities take the form of optional riders and carry charges in addition to the fees and charges associated with annuity products.

There is no guarantee that any investment will achieve its objectives, generate positive returns, or avoid losses. Investments in annuity contracts may not be suitable for all investors.

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