10 Things You Should Know About Buying Annuities

1. What is an Annuity?

An annuity is a contract in which an insurance company makes a series of income payments at regular intervals in return for a premium or premiums you have paid. Annuities are often bought for future retirement income. An annuity can pay an income that can be guaranteed to last as long as you live. Your money grows tax deferred as long as you leave it in the annuity.

2. Examine Different Kinds of Annuities

There are varied features to annuities, which can occur in combination. They include:

- single or multiple premiums
- immediate or deferred, and
- fixed, equity indexed, or variable

For a *single premium* contract, you pay the insurance company only one payment.

For a *multiple premium* contract, you may make a series of payments.

With *an immediate annuity*, income payments start no later than one year after you pay the premium.

With a *deferred annuity*, income payments often start many years after the contract is issued. Deferred annuities have an accumulation period, which is the time between when the contract is issued and when income (annuitization) payments begin.

- **During the accumulation period of a *fixed deferred annuity***, your money, less any applicable charges, earns interest at rates set by the insurance company or in a way spelled out in the annuity contract.
- **During the payout period of a *fixed-deferred annuity***, the amount of each income payment to you is generally a set amount and will not change.
- **During the accumulation period of a *variable deferred annuity***, the insurance company puts your premiums, less any applicable charges, into a separate account. You decide how the company will invest the premiums, depending on how much risk you want to take.
- **During the payout period of a *variable annuity***, the amount of each income payment to you may be fixed (set at the beginning) or variable (changing with the value of the investments in the separate account).

3. Know How Interest Rates are Set

During the accumulation period, your money -- less any applicable charges -- earns interest at rates that may change from time to time. Usually, what these rates will be is entirely up to the insurance company.

The current rate is the rate the company decides to credit to your contract at a particular time. The company will guarantee it will not change rates for a certain time period. The minimum guaranteed interest rate is the lowest rate your annuity will earn. This rate is stated in the contract.

Some flexible premium annuity contracts apply different interest rates to each payment you make into the contract. Other annuity contracts may have two or more accumulated values that fund different benefit options. These accumulated values may earn different interest rates.

4. Know What Charges May be Subtracted from Your Fixed Deferred Annuity

Most annuities have charges related to the cost of selling or servicing it. These charges may be subtracted directly from the contract value. Ask your agent or insurance company to describe the charges that apply to your annuity. Some examples are:

- surrender charges on withdrawals
- contract fees
- premium taxes

5. Income Payment Options of Fixed Deferred Annuities

Companies may offer various income payment options. Establishing a payment stream based on the options below is called annuitization. You or another person that you name may choose the option.

- If you choose *Life Only*, the company pays income for your lifetime.
- *Life Annuity with Period Certain* pays income for as long as you live and guarantees to make payments for a set number of years even if you die.
- If you choose *Joint and Survivor*, the company pays income as long as either you or your beneficiary lives. In some annuity contracts, the company may pay a death benefit to your beneficiary if you die before the income payments start.

6. Tax Treatment of Annuities

Under current federal law, annuities receive special tax treatment. Income tax on annuities is deferred, which means you are not taxed on the interest your money earns while it stays in the annuity. Tax-deferred accumulation is not the same as tax-free accumulation. An advantage of tax deferral is that the tax bracket you are in when you receive annuity income payments may be lower than the one you are in during the accumulation period. You will also be earning interest on the amount you may otherwise have paid in taxes during the accumulation period. Most states' tax laws on annuities follow the federal law. You should consult a professional tax advisor to discuss your individual tax situation.

7. Take Advantage of the "Free Look" Provision

Many states have laws that give you a set number of days to look at the annuity contract after you buy it. If you decide during that time that you do not want the annuity, you can return the contract and get all your money back. This is often referred to as a free look or right to return period. The free look period should be prominently stated in your contract. Be sure to read your contract carefully during the free look period.

8. Is an Annuity Right for You?

You should think about what your goals are for the money you may put into the annuity. You need to think about how much risk you are willing to take with the money as well. Ask yourself: How much retirement income will you need in addition to what you will get from Social Security and other investments? Will you need that additional income only for yourself, or for yourself and others? How long can you afford to leave money in the annuity, and does the annuity let you get money when you need it?

9. Some Questions Your Agent Should be Able to Answer

A few questions that you should ask your agent are: What is the initial interest rate and how long is it guaranteed? What is the guaranteed minimum interest rate? Can I get a partial withdrawal without paying surrender or other charges? Is there a death benefit? What are the fees associated with the contract?

10. Review Your Contract Carefully

Before you decide to buy an annuity, you should review the contract. Terms and conditions of each annuity contract will vary. Ask the agent and company for an explanation of anything you do not understand. Do this before any free look period ends. Compare information for similar contracts from several companies. Comparing products may help you make a better decision. If you have a specific question or cannot get answers you need from the agent or company, contact the Maine Bureau of Insurance.

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