

ARTICLE: “The Disadvantages of Fixed Index Annuities”

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<http://financecove.doodig.com/2010/07/29/the-disadvantages-of-fixed-index-annuities/>

The following comment was submitted to the blog author at www.financecove.doodig.com.

I am an independent market research analyst who specializes exclusively in the indexed annuity (IA) and indexed life markets. I have tracked the companies, products, marketing, and sales of these products for over a decade. I used to provide similar services for fixed and variable products, but I believe so strongly in the value proposition of indexed products that I started my own company focusing on IAs exclusively. I do not endorse any company or financial product, and millions look to us for accurate, unbiased information on the insurance market. In fact, we are the firm that regulators look to, and work with, when needing assistance with these products.

I am contacting you, as the author of a blog that was published at www.financecove.doodig.com, “The Disadvantages of Fixed Index Annuities.” This article had numerous inaccurate and misleading statements about indexed annuities in it. I am contacting you in response to these inaccuracies, to ensure that you and your readers have accurate, unbiased information on these products in the future.

Indexed annuities do not “mitigate the risks of fixed annuities.” Fixed annuities do not have any risks, so this statement is inaccurate.

In addition, you do not refer to purchasers of fixed or indexed annuities as “investors.” Only those who purchase variable annuities can be called “investors,” as these products place the purchaser’s principal and gains at risk due to market volatility. Stocks, bonds, and mutual funds are also investments. The Securities and Exchange Commission (SEC) is responsible for the regulation of such investment products. Fixed and indexed annuities, by contrast, are insurance products- similar to term life, universal life and whole life. Insurance products are regulated by the 50 state insurance commissioners of the United States. Insurance products do not put the client’s money at risk, they are “safe money products” which preserve principal and gains. Investments, by contrast, can put a client’s money at risk and are therefore appropriately classified as “risk money products;” they do not preserve principal.

You think that the limiting of interest on indexed annuities is a detriment when it is not. To ensure that you properly understand how indexed annuities are intended to work, I would like to

provide a brief overview. Because indexed annuities are a “safe money place,” they should be compared against other safe money places. Products like stocks, bonds, mutual funds, and variable annuities are “risk money places,” where the client is subjected to both the highs and the lows of the market (also referred to as “investments”). It is inappropriate to compare any safe money place, such as an indexed annuity, to risk money places and it is most certainly not appropriate to compare safe money places to the market index itself. Indexed annuities are not intended to perform comparably to stocks, bonds, or the S&P 500 because they provide a minimum guarantee where investments do not. Indexed annuities are priced to return about 1% - 2% greater interest than traditional fixed annuities are crediting. In exchange for this greater potential, the indexed annuity has a slightly lesser minimum guarantee. So, if fixed annuities are earning 5% today, indexed annuities sold today should earn 6% - 7% over the life of the contract. Some years, the indexed annuity may return a double-digit gain and other years it may return zero interest. However, what is most likely to happen is something in between. Were the indexed interest NOT limited, the insurer could not afford to offer a minimum guarantee on the product, and THAT is a variable annuity- not an indexed annuity. On the other hand, the client is guaranteed to never receive less than zero interest (a proposition that millions of Americans are wishing they had during that period of 03/08 to 03/09) and will receive a return of no less than 117% worst-case scenario on the average indexed annuity. In addition, it is absolutely irresponsible to say that indexed annuity “offer market-type returns.” Please refrain from such statements in the future.

Furthermore, caps are not any more “limiting” than participation rates or spreads over a long period of time. Regardless of whether the interest is limited by a cap, participation rate, or spread- all indexed annuities are priced to return about 1% - 2% greater interest than fixed annuities and certificates of deposit (CDs) are crediting. Ultimately, the index used, the crediting method utilized, and the choice of a cap or participation rate are irrelevant. All indexed annuities are priced to return 1% - 2% greater interest than traditional annuities are earning today, over the life of the policy (regardless of index, crediting method, and pricing lever). Indexed interest on indexed annuities sold today could be as much as 8.7% or even more. All of these different features (index, crediting method, pricing lever) merely give the marketing organizations that distribute these products an opportunity to promote why their product is "different" or "better" than their competitors' products, to the agent. They do not actually make any one product better than another. Yes, some designs will perform better than others in some years. However, over the life of the contract, they will be about even keel.

Although you are quick to point-out that indexed annuities are taxed at income tax rates, as opposed to capital gains rates, you fail to mention the many benefits of indexed annuities, which include (but are not limited to):

1. **No indexed annuity purchaser has lost a single dollar as a result of the market’s declines.** Can you say the same for variable annuities? Stocks? Bonds? Mutual funds? NO.
2. All indexed annuities return the premiums paid plus interest at the end of the annuity.

3. **Ability to defer taxes:** you are not taxed on annuity, until you start withdrawing income.
4. **Reduce tax burden:** accumulate your retirement funds now at a [35%] tax bracket, and take income at retirement within a [15%] tax bracket.
5. **Accumulate retirement income:** annuities allow you to accumulate additional interest, above the premium you pay in. Plus, you accumulate interest on your interest, and interest on the money you would have paid in taxes. (Frequently referred to as “triple compounding.”)
6. **Provide a death benefit to heirs:** all fixed and indexed annuities pay the full account value to the designated beneficiaries upon death.
7. **Access money when you need it:** fixed annuities allow annual penalty-free withdrawals of the account value, typically at 10% of the annuity’s value (although some indexed annuities permit as much as 20% of the value to be taken without penalty). In addition, 9 out of 10 fixed and indexed annuities permit access to the annuity’s value without penalty, in the event of triggers such as nursing home confinement, terminal illness, disability, and even unemployment.
8. **Get a boost on your retirement:** many fixed and indexed annuities provide an up-front premium bonus, which can provide an instant boost on your annuity’s value. This can increase the annuity’s value in addition to helping with the accumulation on the contract.
9. **Guaranteed lifetime income:** an annuity is the ONLY product that can guarantee income that one cannot outlive.

Verifying how little research you have done on indexed annuities, there is no such thing as a “fund manager” in this market. Only mutual funds have “fund managers.” Please do some research on the products you write about in the future, prior to publishing your content.

Furthermore, there are no fees on indexed annuities. The only “cost” to the consumer is a commitment of time.

Indexed annuities do not have “significant” penalties. There are indexed annuities with surrender charges as short as three years and the average first-year penalty (which declines thereafter) on indexed annuities is a mere 10.61%. Every indexed annuity allows 10% of the annuity’s value to be withdrawn without penalties on an annual basis; some allow as much as 50% to be withdrawn in a single year! Plus, 9 out of 10 indexed annuities provide a waiver of the surrender charges, should the annuitant need access to their money in events such as nursing home confinement, terminal illness, disability, and even unemployment. Consider the fact that these products pay the full account value to the beneficiary upon death, and I think that you’ll see that consumers have tremendous ability to “get their money when they need it” with indexed annuities. Certainly, all annuities are considered long-term investments. However, indexed annuities are some of the most liquid retirement income products available today!

You should note that “annual reset” is not a crediting method. It is an indicator of when the next index measurement begins on most indexed annuities (annually).

While it is true that insurance companies reserve the right to change the caps, participation rates, and asset fees on indexed annuities in years two plus, it does not mean that insurance companies do. I can name numerous companies that have never reduced their renewal rates on their indexed annuities. However, this provision is no different than that of a fixed annuity, where the insurance company has the discretion to change the credited rates in years two plus. Not to mention the fact that variable annuities have the ability to increase fees if necessary in years two plus. All fixed and indexed annuities are subject to minimum rates, as approved by the state insurance divisions that approve the products for sale in their respective states. Insurance companies are smart to protect themselves by filing products that have the ability to change rates annually, in the event of a volatile market. I personally feel much more confident that the companies offering these products today will be able to make good on their claims-paying ability, considering such flexibility in the event of unforeseen circumstances.

It truly illuminates how little you know about the indexed annuity market when you talk about “high water mark” indexed crediting methods. There are only eight products left on the market that use this crediting method. In addition, this method does not necessarily result in the purchaser “not [receiving] the accrued interest during the period if the [indexed annuity] were surrendered before the term ends.”

I would advise that if you readers truly want to “weigh the disadvantages against the benefits” of indexed annuities, that they go to my website, and not yours. It appears that you do not know enough about these products to be writing about them. However, should you have a desire to write about these products in the future, I am more than happy to assist you in your understanding of these products or aid you in fact-checking. Please do not hesitate to contact us, should there be a need.

Thank you.

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