THE BEST OF BOTH WORLDS
Guaranteed Income with Liquidity

By Kim O'Brien

The primary retirement challenge for baby boomers over recent decades has been accumulation. But now, the focus is becoming how to turn accumulated funds into a reliable income. The good news is that fixed and fixed indexed annuities have evolved to address both challenges well.

Fixed annuities have always provided a compelling value to consumers looking to safely build their retirement savings. Traditional fixed annuities credit an attractive fixed interest rate declared in advance and guaranteed by the issuing carrier. Fixed indexed annuities provide guaranteed safety of principal along with even greater interest-crediting potential than can be provided by a traditional fixed interest rate.

Now, with the baby boomers starting to retire, the consumer need for guaranteed retirement income is beginning to emerge. To meet this need, the fixed annuity industry has brought a new innovation to the market – a guaranteed lifetime income or withdrawal benefit.

Some carriers call it an "income benefit," and others call it a "withdrawal benefit." But no matter what you call it, an annuity with such a benefit provides all the usual advantages of a fixed annuity, plus an additional benefit – the option for a guaranteed lifetime cash flow to the purchaser.

That cash flow comes with two important assurances. The first assurance is liquidity: the purchaser retains access to the remaining annuity value at all times. The second assurance is longevity: even if the annual payments ultimately deplete the annuity's value, the issuing carrier is obligated to continue making the annual payments as long as the purchaser lives.

There is no other product that provides this wonderful combination of high interest crediting potential, guaranteed principal protection, guaranteed lifetime income, and access to remaining value.

How the Benefit Works

A guaranteed lifetime income or withdrawal benefit is typically optional on a fixed or fixed indexed annuity, and it is added to the annuity by a rider. Whereas the annuity has an accumulation value, the rider adds a second value, the income value.

The accumulation value works just as it always does on a fixed annuity. On a fixed annuity, the accumulation value is credited with an interest rate that is declared by the issuing carrier in advance. On a fixed indexed annuity, the purchaser has a choice of fixed and index-based interest crediting strategies. Each index-based strategy provides that in a period where the index increases, the annuity credits interest to the accumulation value. The more the index increases, generally the higher the interest credit. But in a period that the index declines, the annuity's value is completely protected and suffers no loss whatsoever.

The income value is completely separate from the accumulation value. It typically grows at a fixed rate of interest, and that rate is very attractive, often in the 5% – 8% range. Then, once the purchaser elects to start taking lifetime withdrawals, a payout factor is applied to the income value to determine the guaranteed annual withdrawal. If it just so happens that the accumulation value is higher than the income value at that point, then the accumulation value will be used in the payout calculation instead.

Now that we have calculated the amount of guaranteed withdrawal, the annuity purchaser may withdraw that amount from the annuity every year for life.

While taking these withdrawals, the purchaser is provided with two very valuable guarantees. First, although the annual withdrawals are deducted from the accumulation value, interest continues to be credited to the accumulation value, and the purchaser retains access to the remaining accumulation value at all times. Second, even if the annual withdrawals ultimately deplete the accumulation value, the issuing carrier is obligated to continue making the annual payments as long as the purchaser lives.

VALUE	ACCUMULATION VALUE	INCOME VALUE
HOW IT IS USED	It is the basis for most benefit calculations, including the value to be paid upon death, surrender, or maturity	It has one purpose – it is the value that is used to determine the lifetime payments that can be taken from the annuity
HOW IT GROWS	Interest is credited to this value using a choice of fixed and/or index-based methods	A separate fixed, guaranteed interest rate (usually in the 5% - 8% range) is credited to this value

The guaranteed lifetime income or withdrawal benefit rider adds a valuable benefit to the contract for anyone who is interested in a reliable retirement income. Therefore, the rider is not free. Some carriers build the rider into the annuity product, so the cost is reflected in a lower interest rate on the accumulation value, the income value, or both. Other carriers charge directly by deducting a fee from the accumulation value of the annuity, usually based on the income benefit base. On a fixed indexed annuity, this charge may cause the accumulation value to fall in years in which no indexed interest is credited. Rider charges normally continue until the accumulation value of the annuity is depleted or the rider is removed from the contract.

Fixed and fixed indexed annuities can be a great fit for people looking to grow their retirement savings safely with high interest crediting potential. In addition, fixed indexed annuities also provide benefits for people who are looking for guaranteed lifetime retirement income without giving up access to their money.