

A large, stylized illustration of a gear. The gear is primarily orange and yellow, with a blue center. It is shown in a perspective view, appearing to be part of a larger mechanical system. The background features faint, light blue gear patterns.

IRI

RETIREMENT FACT BOOK - 2023

**A Guide to Concepts,
Solutions, Trends,
and Data in the
Retirement
Income
Industry**

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About the Insured Retirement Institute

The Insured Retirement Institute (IRI) is the leading association for the entire supply chain of insured retirement strategies, including life insurers, asset managers, broker-dealers, banks, marketing organizations, law firms, and solution providers. IRI members account for 90 percent of annuity assets in the U.S., include the foremost distributors of protected lifetime income solutions, and are represented by financial professionals serving millions of Americans. IRI champions retirement security for all through leadership in advocacy, awareness, research, and the advancement of digital solutions within a collaborative industry community. Learn more at www.irionline.org.

About the IRI Retirement Fact Book

Marking its twenty-second year in publication, the IRI Retirement Fact Book continues to be a reliable, trusted source for information regarding the insured retirement industry. Building on the redesign and renaming that commenced with the tenth edition in 2011, we strive to improve content each year, while keeping the focus on practical information that can help financial professionals better understand and serve their clients, including through the exploration and analysis of retirement topics beyond annuities. Readers will find practice management tips and information, the latest consumer and advisor research regarding retirement planning, current retirement market statistics, and much more. As IRI continues to grow to serve the diverse needs of the people and organizations that we are proud to represent, this publication will also evolve as a resource for the entire insured retirement industry and the consumers that invest in our strategies.



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Insured Retirement

The Retirement Landscape

Retirement for most American workers today bears little resemblance to the retirement of their parents and grandparents. Fifty years ago, a typical working life trajectory consisted of being employed by the same company for 30 or 40 years, fully retiring at age 65 with confidence that Social Security and a defined benefit pension plan would provide adequate income for as long as one might live — and perhaps with a gold watch to mark the time.

Retirement and pre-retirement have changed dramatically. The responsibility of providing for adequate income during retirement has shifted away from employers (traditional defined benefit pension plans) to individuals (defined contribution plans such as 401(k) plans). For more workers today, income beyond that provided by Social Security will have to come from savings or continuing to work well past age 65.

There are about 76 million baby boomers in the United States, approximately 50 million of whom are already age 65 or older. The United States is steadily moving into a period of potential crisis as the number of retirees increases significantly over the coming decades: 10,000 Americans will reach retirement age every day through at least 2030, when almost 73 million individuals, or 20 percent of the U.S. population, will be age 65 or older. At the same time, traditional retirement income sources have diminished, retirement is becoming more expensive, and many retirees and near-retirees are unprepared. And the United States is hardly alone; other developed countries are facing the same issues.

Figure 1-1 Retirement Expenses Increasing While Traditional Income Sources Diminish



However, these challenges are also opportunities. Financial services companies and insurers who offer solutions to help Americans save more for retirement, and create sustainable, lifetime income from their savings, are critical to helping Americans manage their needs and risks. Insured retirement solutions can help Americans prepare for retirement by providing for additional tax-advantaged savings opportunities, protection from market and other risks, and guaranteed income during retirement.

What Is Insured Retirement?

Retirement consists of many unknowns: How long will one live? How long will one's spouse live? Will he or she require expensive health care or long-term care? How will changes in equity markets and interest rates affect one's financial well-being? Will inflation be mild or significant?

Americans underestimate their life expectancy. The average life expectancy for a U.S. male is 76 years, and for a U.S. female it is 81, but that is life expectancy from birth. From age 60, a U.S. male can expect to live an average of 22 years, or to age 82, while the average 60-year-old female in the U.S. will live over 24 years, or to age 84. And this is just an average – some will die sooner but some will live much longer (World Health Organization, 2019). In fact, a 65-year-old male has a 62 percent chance of living to age 85, a 42 percent chance of making it to age 90, and more than one in five can expect to live to age 95. A female has a 72 percent chance of surviving to age 85, a 53 percent chance of reaching 90, and almost one in three will attain age 95. For a male/female couple age 65, there is an 89 percent chance one will make it to age 85, a 73 percent chance one will reach age 90, and in 45 percent of couples one person will survive to at least age 95 (American Academy of Actuaries and Society of Actuaries, Actuaries Longevity Illustrator, <http://www.longevityillustrator.org>). In most cases the surviving spouse will be female; there are more than three widows in the United States for every widower, and after the age of 80 the ratio of widows to widowers is 5 to 1 (US Census Bureau). The unfortunate reality is that women are especially vulnerable during retirement as they will likely live longer and may live as widows for years or even decades. Compounding the problem, due to a variety of factors such as lower earned income and time spent out of the workforce caring for children or other family members, they may also have saved less for retirement.

American workers, on average, plan to retire at age 66, but the average reported retirement age for Americans who are currently retired is 61 (Gallup, 2022). This gap between planned and actual retirement age is even more pronounced in various surveys. For example, a 2021 survey by the Employee Benefits Research Institute and Greenwald Research found that 26 percent of American workers expect to retire at 70 or older, or never, while only six percent of retirees reported actual retirement ages in this range. American workers should therefore expect, and plan for, a retirement lasting as long as their working years. Unfortunately, most do not plan for this possibility, and do not have a plan to ensure their retirement savings can generate sustainable lifetime income. Americans simply must have a plan that contemplates a longer retirement than they might have envisioned, because the longer a person lives the more all the other risks one may experience during retirement (such as an unfavorable sequence of returns, above average inflation, health care, and long-term care) are magnified.

There are many financial products and approaches that can provide retirement income. However, most of these products do not guarantee income for life, leading to the potential of one “running out” of money, possibly at an advanced age when options like returning to the workforce are not possible. The financial events in 2008 and 2009 and the economic uncertainty and market volatility resulting from COVID-19 in 2020, which continues to reverberate today, are examples illustrative of the perils of relying on non-guaranteed income during retirement.

For example, assume a 65-year-old retired in 2008 with a \$1 million nest egg. The retiree was planning to withdraw \$50,000 a year (5% of the nest egg) to supplement his or her Social Security and pension plan. However, assume the nest egg dropped in value to \$600,000 because of withdrawals and weak equity markets in 2008 and 2009. If the retiree withdrew another \$50,000, he or she would then be withdrawing 8.3 percent of the account value, a level that may not be sustainable. The retiree now has two choices: 1) continue to take out \$50,000 annually and face a greater probability of depleting the account value, or 2) scale back the amount of the annual withdrawals (and still face the risk of running out of money). True, returns on equities have been robust over the past decade plus, but during that time there have been periods of very high volatility and wild swings in equities markets. Did savers run to cash during the extreme market volatility in the spring of 2020 and miss out on the historically strong equity market gains since? There is strong evidence to suggest many did and that retirement savers don't truly understand diversification: the 2019 BlackRock Global Investor Pulse survey found that 57 percent of investors do not hold any stocks or bonds.

The Outdated “4%” Rule

The 4% rule, proposed by William Bengen in the 1994 paper “Determining Withdrawal Rates Using Historical Data,” was a guideline for determining a withdrawal rate that would theoretically provide sustainable income without depleting assets entirely over a 30-year retirement. Over the years, many have suggested using 4% as the amount that retirees can withdraw from their assets on an annual basis, adjusted for inflation, with a reasonable expectation that their assets will last for the rest of their life. However, an underlying assumption of the rule is an at least 50 percent allocation to stocks, and preferably 75 percent, with 25 to 50 percent allocated to bonds. Withdrawal rates can vary widely based on the portfolio assumption used and the desired probability of success. Wade Pfau, Ph.D., CFA, a professor at the American College in Bryn Mawr, PA, calculated “safe” withdrawal rates from volatile investment portfolios under a variety of spending and asset allocation scenarios. Figure 1-2 presents several spending strategies, and withdrawal percentages are based on varying levels of stock allocation, remaining wealth, and probability horizon (confidence that x% of wealth remains after y years).

Figure 1-2 Sustainable Spending Rates from an Investment Portfolio

Spending Strategy	Portfolio Allocation		
	Conservative (25% Stocks)	Moderate (50% Stocks)	Aggressive (75% Stocks)
Fixed Spending (No Growth)	2.77%	3.73%	4.88%
Spending with 2% Cost of Living Adjustment (COLA)	2.04%	2.88%	3.97%
Inflation (CPI-U) Adjusted Spending (the “4% rule”)	1.48%	2.40%	3.54%
Spending with 2% COLA and 5 Years of Buffer Asset	2.40%	3.56%	5.25%
CPI-U Adjusted Spending and 5 Years of Buffer Asset	1.69%	2.91%	4.60%
Guyton & Klinger Decision Rules (Variable Spending)	2.65%	4.03%	5.13%

Notes: The conservative couple uses a 25 percent stock allocation and seeks a 95 percent chance that real wealth will not fall below 20 percent of its initial level by year 35 of retirement. The moderate couple uses a 50 percent stock allocation and seeks a 90 percent chance that real wealth will not fall below 15 percent of its initial level by year 30 of retirement. The aggressive couple uses a 75 percent stock allocation and seeks an 80 percent chance that real wealth will not fall below 10 percent of its initial level by year 25 of retirement. Analysis assumes that withdrawals are made at the start of each year, retirees earn the underlying indexed market returns, and market return simulations are based on capital market assumptions starting from today’s level of interest rates. Source: Retirement Researcher (www.retirementresearcher.com).

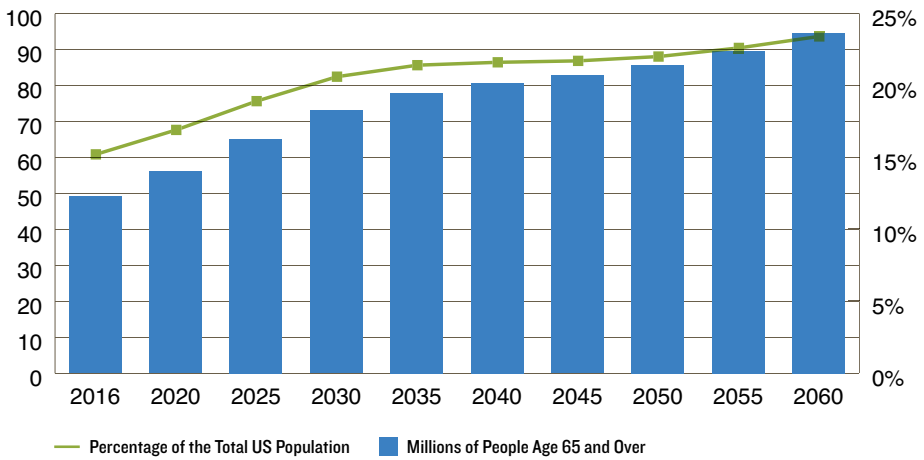
Systematic withdrawal strategies, whether a simple “x%” rule or based on a more sophisticated stochastic analysis of the probability that assets will not be depleted at various withdrawal rates, have two significant drawbacks: first, they are based on historic asset class returns, which may not repeat in the same sequence in the future, and secondly, they assume that the investor acts rationally, maintaining the asset allocation assumed in the models even during periods of significant negative returns, when in practice many consumers may weight more heavily toward cash and cash equivalents after a period of negative returns, and miss out on subsequent positive returns. **Insured retirement** refers to products and solutions that guarantee income and/or protection against principal loss and other risks regardless of market conditions. For example, annuities and pensions can guarantee lifetime income while long-term care insurance provides financial protection against long-term care costs.

An Aging Problem

In 2020 there were an estimated 54 million individuals age 65 or older in the United States, representing 16.3 percent of the total population (U.S. Census Bureau, “Table 1. Total U.S. Resident Population by Age, Sex, and Series: April 1, 2020”), as compared to 51 million and 15.2 percent of the population in 2017. These numbers are projected to increase steadily over the coming decade, with 73 million individuals age 65 or older by 2030, or 21 percent of the projected population. (U.S. Census Bureau 2017 National Population Projections Tables, *Projections of the Population by Sex and Age for the United States: 2017 to 2060*)

The increase in the number of retirees over the coming decades is expected to strain governmental retirement programs such as Social Security and Medicare, as there will be fewer workers supporting more retirees.

Figure 1-3 Age 65+ United States Population Growth



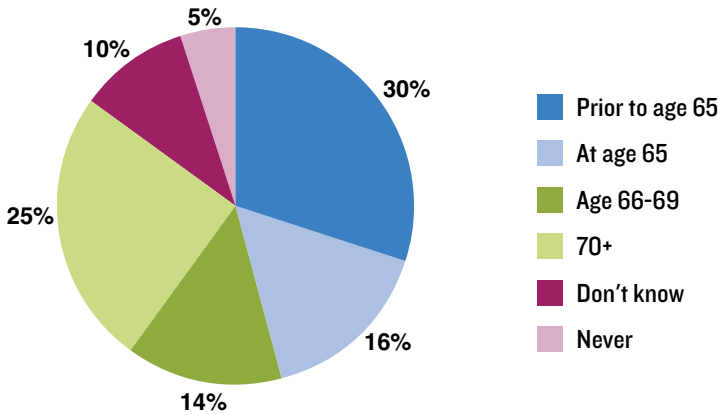
Source: U.S. Census Bureau

Two Financial Sides of Retirement

For all age groups, there are two sides to an individual's finances: expenses and income. However, there are significant differences between retirees and non-retirees. One major difference is that it is difficult for many retirees to increase their annual income amount if needed as they may lack adequate savings to do so, or be unable to re-enter the workforce due to their own health issues, or due to the health of a spouse or other family member.

While some people have a retirement date in mind, many Americans, particularly those in the Boomer generation, do not know when they will retire and among those that do many are planning to retire later. A 2021 IRI study, "The Retirement Readiness of Older Workers," found that despite minimal savings and lack of pensions, one-third of workers believe they will retire prior to age 65, and one-half at 65 or younger. This is especially concerning given most survey respondents were born in 1960 or later, so they do not reach full retirement age until age 66 at the earliest.

Figure 1-4 Older Workers' Anticipated Age of Retirement



Source: "Retirement Readiness of Older Workers," IRI 2021

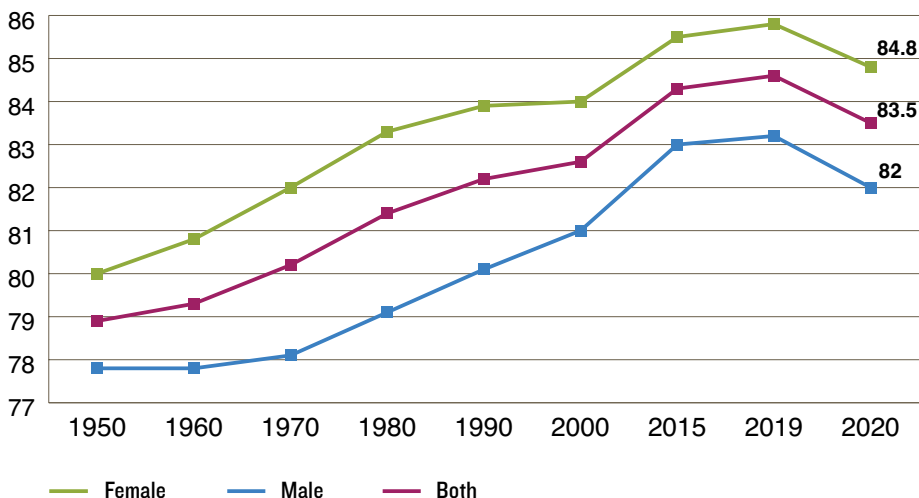
People retiring today face three fundamental problems: Retirement has become more expensive due to longevity and health care costs, the age to receive maximum Social Security benefits has increased, and fewer Americans are covered by traditional pension plans and retiree health insurance.

Is Retirement Getting More Expensive?

Life expectancy

As noted at the beginning of this chapter, average life expectancy has increase dramatically over the years. However, for the purposes of retirement planning, the more relevant statistic is not one's life expectancy at birth, which a century ago was heavily impacted by much higher rates of infant mortality, but one's life expectancy after retiring; in other words, the number of years one must rely on sources of income other than earned income. As average life expectancy has increased, so too has the life expectancy of a 65-year-old. In 1980, the average life expectancy for a 65-year-old male was 79.1 years. By 2019, this number had increased by over five years, to age 84.6. Life expectancy fell to age 83.5 in 2020, largely due to the pandemic, but absent a new pandemic or other systemic health emergency will rise again in the future. (NCHS, National Vital Statistics System, Mortality).

Figure 1-5 Life Expectancy at Age 65: 1950 – 2020



Source: U.S. Centers for Disease Control and Prevention

While an increase of four years may not seem dramatic over one's lifetime, it can have a significant impact on one's retirement security. Say a person has annual expenses of \$50,000 in retirement (ignore inflation for now). Expenses for a 65-year-old living 14 years in retirement would total \$700,000. Now, assume that a 65-year-old lives 19 years in retirement. Those additional four years increase expenses by \$200,000 for a total of \$900,000, an increase of 29 percent.

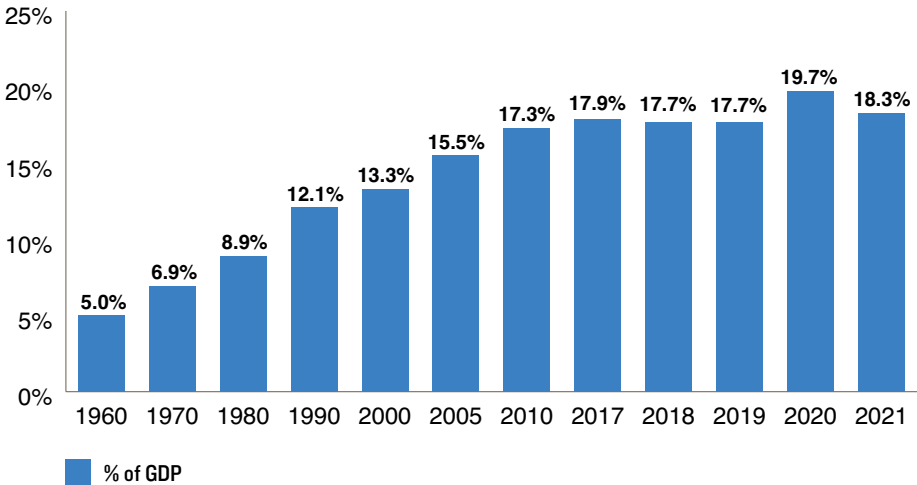
Let's now factor in inflation, assuming an annual rate of 3 percent, which despite current elevated inflation levels is approximately the long-term average rate of inflation. Under this scenario, a 65-year-old living 14 years to age 79 would need \$854,000 in income to meet his or her expenses. And by living an additional four years to age 83, he or she would have total retirement expenses of \$1,170,000, 37 percent higher. Recently inflation has accelerated far above the average of the past 40 years, compounding this problem even further and making it unlikely that "safe" investments such as Certificates of Deposit can enable 20 or 30 years of retirement spending without a significant erosion in purchasing power. At an annual inflation rate of 8 percent, the same 65-year-old would need a total of \$1,872,512, 60 percent more than at a 3 percent rate of inflation. It is also worth noting that an experimental index produced by the Bureau of Labor Statistics, the Consumer Price Index for Americans 62 years of age and older, or R-CPI-E, which measures inflation for a basket of goods more relevant to those who are retired, is generally significantly higher than headline inflation calculated using CPI-U.

Another note on life expectancy: it is an average of all demographic and geographical groups in the United States. Differences exist across different ethnic groups, states, and of course gender. As an example, the life expectancy of a white female at age 65 was 84.9 years in 2020 (the most recent year data based on ethnicity is available), almost six years longer than the life expectancy of a black male. ("United States Life Tables, 2020," U.S. Department of Health and Human Services).

Health care costs

Health care costs account for about 18 percent of the Gross Domestic Product (GDP), as shown in Figure 1-6. While health care costs as a percentage of GDP remained in a fairly tight range between 17 percent and 18 percent of GDP from 2010 to 2019, federal COVID-19 funding pushed this to almost 20 percent in 2020. The decline in COVID-19 funding brought costs down closer to recent norms in 2021, but they remain higher than pre-pandemic levels (Centers for Medicare & Medicaid Services, National Health Expenditures and Selected Economic Indicators). More sobering, the Congressional Budget Office (CBO) projects that total health care costs will reach 31 percent of GDP by 2035 and 46 percent by 2080 absent significant changes in policy.

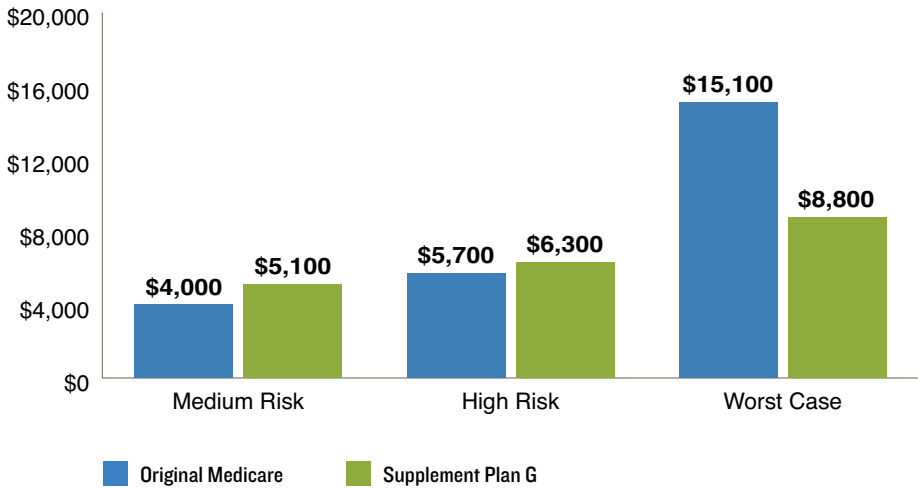
Figure 1-6 Health Care Costs as a Percentage of U.S. GDP



Source: U.S. Centers for Medicare and Medicaid Services

While Medicare provides medical insurance to most over age 65, it does not provide complete coverage. Retirees covered by Medicare will still have out-of-pocket (OOP) medical expenses, which include insurance premiums (for Medicare Advantage or supplemental plans), co-pays, and expenditures not covered by Medicare, such as dental care, eyeglasses, and hearing aids. OOP expenses may be highly variable depending on risk, i.e. the type and amount of medical care needed. Figure 1-7 shows the premiums and OOP medical costs for a 65-year-old woman at varying risk and Medicare coverage levels.

Figure 1-7 Average Premiums and Out-of-Pocket Medical Expenses (Female age 65)



Source: Mercer-Vanguard health care cost model, 2020

What does this total throughout one's lifetime? Based on life expectancy, a 65-year-old couple can expect to incur approximately \$315,000 in health care costs (in today's dollars) during retirement, not including costs for long-term care (Fidelity, 2022).

Long-term care is another significant component of health care costs in retirement, one which many mistakenly assume is always covered by Medicare — in fact, in IRI's 2019 Boomer study 50 percent of respondents believed long-term care would be covered by Medicare. People also tend to miscalculate their need for long-term care. Long-term care is a range of services and support to help people meet their personal care needs. Most long-term care is not medical care, but rather assistance with the basic tasks of everyday life, sometimes called Activities of Daily Living, or ADLs. The ADLs include bathing, dressing, eating, using the toilet, transference (as from bed to chair), and caring for incontinence. Seventy percent of people turning age 65 can expect to use some form of long-term care to help with these ADLs during their lives (U.S. Department of Health and Human Services). Long-term care services may be provided in a nursing home or through home health care. Medicare only pays for skilled services or rehabilitative care, not for non-skilled ADL assistance, which makes up most long-term care services. Non-skilled nursing home assistance with the ADLs may be paid by Medicaid, but generally only after an individual spends down his or her assets (within limits, and different limits apply for married couples).

The cost of nursing home care is expensive. Nationally, average rates in 2021 for a private room were \$297 per day or \$108,405 annually, and for a semi-private room were \$94,900 (Genworth Cost of Care Survey 2021). See Chapter 3 for more detailed information regarding health care costs and planning for retiree health care.

Retirement Income Sources

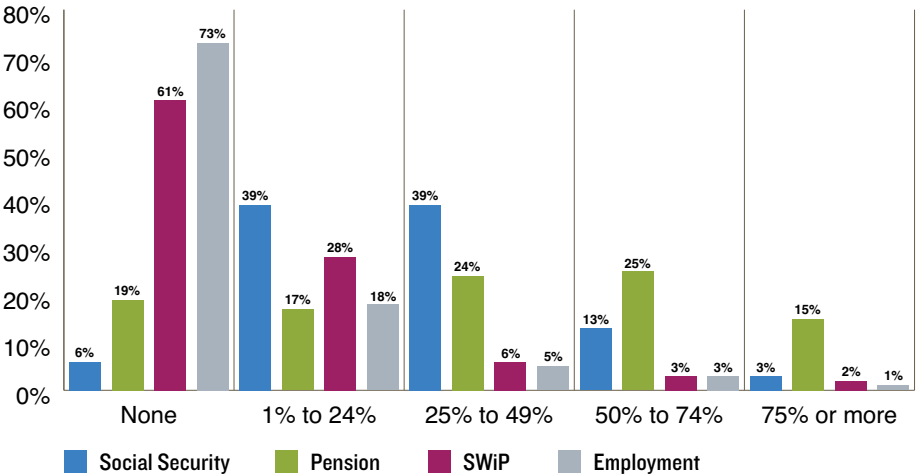
Many are familiar with the traditional three-legged stool of retirement income:

1. Employer-sponsored pension plans
2. Governmental plans, such as Social Security
3. Income from personal savings

Today, however, fewer Americans are covered by traditional pension plans, and the age to receive full Social Security benefits has increased. This requires Americans to take a more active role in preparing for their retirement.

Figure 1-8 shows income sources for Americans retired between five and 15 years, who retired with at least \$100,000 in investable assets. Social Security accounts for 50 percent of income, or more, for only 16 percent of these retirees, while pensions account for 50 percent or more of income for 40 percent. Employment and systematic withdrawals from savings are less significant than either (“Retirement, Income, and Risk,” IRI 2018).

Figure 1-8 Income Sources as a Percentage of Total Household Income



Source: “Retirement, Income, and Risk,” IRI 2018

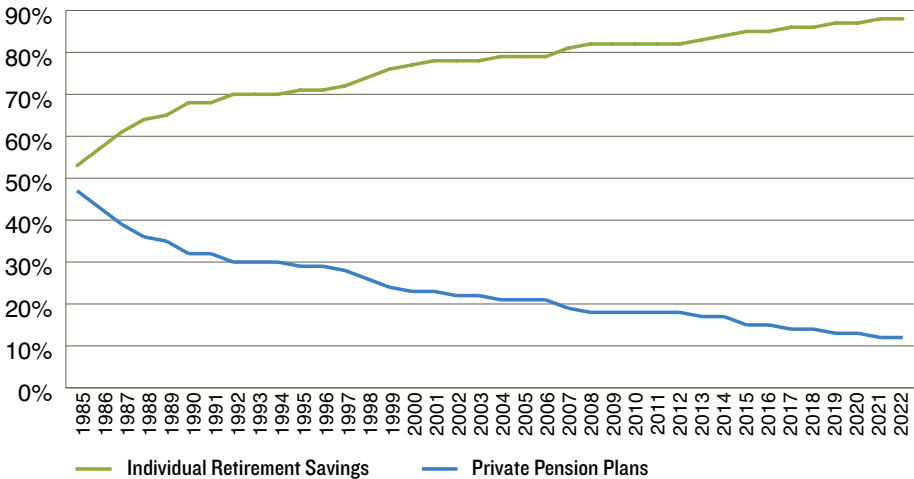
Pension Plans

The number of traditional pension plans has decreased significantly over the past several decades. In 1985, there were over 114,000 private pension plans insured by the Pension Benefit Guaranty Corporation. Today that number is about 25,000, covering 33 million people (Pension Benefit Guaranty Corporation, 2022).

While the number of private pension plans has decreased, many government employees are still covered by a traditional pension plan.

Figure 1-9 shows the decline of private pension plans since 1985 as a percentage of all retirement savings. In 1985, the split between individual retirement savings and private pension plans was nearly 50/50. However, the percentage allocated to individual plans (including annuities, IRAs, and employer-sponsored defined contribution plans such as 401(k), 403(b), and 457 plans) versus private pensions has increased steadily, reaching 88 percent in 2022 (Investment Company Institute, Q4 2022).

Figure 1-9 Percentage of Retirement Savings



Source: Investment Company Institute

Social Security

Historically, the age to receive full retirement benefits from Social Security was 65. However, due to concerns about the financial solvency of the Social Security system full retirement age has increased, varying by year of birth. For example, individuals born in 1955 can begin receiving full retirement benefits when they reach age 66 and 2 months, while those born in 1960 or later must wait until age 67 to receive their full retirement benefit. Individuals can still begin Social Security retirement benefits at age 62, but the annual amount they will receive will be reduced.

What is the impact on a retiree? Consider someone who was able to retire with full benefits at age 65 compared with someone born in 1960, who must wait until age 67 to begin receiving full Social Security retirement benefits. Assume that both individuals live to age 82, retiring at age 67 instead of age 65 means the retiree will receive 15 years of Social Security benefits as compared to 17 years.

Persons born in 1960 or later can receive 70% of the maximum benefit if they retire at age 62. If they begin receiving benefits after age 62, the percentage is increased every month until age 67. For example, those born in 1960 can receive 86.7% of the full benefit if they retire in the month they reach age 65.

Figure 1-10 Full Retirement Age and Reduction for Benefits Starting at Age 62

Birth year	Full retirement age	Amount benefit is reduced if retirement begins at age 62
1937 or earlier	65	20.00%
1938	65 and 2 months	20.83%
1939	65 and 4 months	21.67%
1940	65 and 6 months	22.50%
1941	65 and 8 months	23.33%
1942	65 and 10 months	24.17%
1943-1954	66	25.00%
1955	66 and 2 months	25.83%
1956	66 and 4 months	26.67%
1957	66 and 6 months	27.50%
1958	66 and 8 months	28.33%
1959	66 and 10 months	29.17%
1960 and later	67	30.00%

Source: Social Security Administration

Insured Retirement

The need for insured retirement products and solutions is arguably greater than ever as:

- Americans are living longer and health care costs continue to increase, and
- Fewer Americans are covered by traditional pension plans and the age to receive full Social Security benefits has increased.

There are many sources of retirement income, but the key question is if the source is guaranteed. For example, one can take systematic withdrawals from a mutual fund or stock portfolio, but the income cannot be guaranteed to last a lifetime. One can plan on returning to the workforce to earn additional income to mitigate the risk of running out of money, but health concerns may prohibit this.

There are a number of insured retirement products and solutions such as annuities, long-term care insurance, life insurance, and reverse mortgages. These products and solutions can help provide Americans with protection during their retirement and ensure guaranteed lifetime income.



Social Security

Introduction

The original intent of the creators of Social Security in post-Depression America was to provide a basic income stream that would offer some level of economic stability for those who were no longer able to work. As America prospered, Social Security became a welcome supplement to pensions and savings; however, since employers have steadily eliminated pensions over the past two decades, Social Security has become the greatest source of income for many retirees.

In 2023, approximately 55 million American workers and survivors of deceased workers aged 65 or older receive Social Security retirement benefits, and approximately 10.6 million disabled workers (including two million spouses and children of disabled workers) also collect benefits. According to the Social Security Administration, the number of Americans over age 65 will swell to 79 million by 2035, which is expected to put enormous strain on the Social Security Trust Fund.

Those who believe Social Security will provide a sustainable living income may be greatly disappointed, as Medicare premiums and reduced cost-of-living adjustments (COLAs) slowly erode monthly disbursements.

The Basics of Social Security

Social Security benefits are based on a beneficiary's Primary Insurance Amount (PIA). During employment years, workers contribute 6.2 percent of earnings into Social Security (up to \$142,800 per year in 2021), and employers match this amount. These funds are not held in personal accounts that individuals can access upon retirement; rather, the system pays it forward, with current contributions distributed to eligible beneficiaries. Any collected money that is not paid out in benefits goes into the Social Security Trust Fund.

Qualifying for Benefits

As more people work into their sixties and seventies, what will be the definition of “retired”? The government’s definition of “full retirement age” (FRA) — or when a citizen can collect their full retirement benefits — varies by year of birth:

Figure 2-1 Full Retirement Age

Year of Birth	Full Retirement Age
1937 or earlier	65
1938	65 and 2 months
1939	65 and 4 months
1940	65 and 6 months
1941	65 and 8 months
1942	65 and 10 months
1943-1954	66
1955	66 and 2 months
1956	66 and 4 months
1957	66 and 6 months
1958	66 and 8 months
1959	66 and 10 months
1960 and later	67

Source: Social Security Administration

For most soon-to-be retirees, FRA is between age 66 and 67, as 2017 marked the first year in which someone eligible to collect on their own Social Security benefit had an FRA greater than age 66. For those born after 1960, FRA is age 67. While one can begin drawing on Social Security at 62, the system is set up to encourage deferment, and penalties are levied against those who collect early.

Eligible beneficiaries who start collecting at age 62 will receive the minimum benefit. Waiting to start at FRA will return at least 33 percent more annually and waiting to claim until age 70 will yield 75 percent more income than at age 62. After age 70, no further age-based benefit increases are applied.

Using an example of someone who could earn \$1,000/month at age 62 (with an FRA of 66):

Collecting age	62	66	70
Monthly Benefit	\$1,000	\$1,333	\$1,760
Yearly Benefit	\$12,000	\$15,996	\$21,120

For those who have no income and/or can no longer work, claiming at a younger age may be the only option, but that is likely to result in a low standard of living. Those who have more financial flexibility may be wise to wait.

How to Determine Benefits

Because few give much thought to Social Security until it is time to collect, the general assumptions are that Social Security income automatically begins at retirement or when it is time to sign up for Medicare. According to a survey conducted by KRC Research (on behalf of MassMutual), more than seven in 10 Americans incorrectly believe that full Social Security retirement age is 65, when the age actually varies depending on birth year.

Retirement benefits are NOT automatic. Everyone must choose when to claim, and that choice affects the amount received.

The key factors in determining benefits are:

- Age in relation to FRA
- The age retiree (and spouse, if applicable) plan to claim
- Whether payments are based on an individual's or spouse's recorded earnings
- Change in marital status
- Wages earned after filing for benefits (if applicable)
- Life expectancy

Social Security was never meant to be an individual's only source of retirement income, as it only replaces about 40 percent of the average earner's wages. Also, Medicare Part B premiums are directly deducted from Social Security benefits; therefore, as premiums have risen and COLAs shrank (the Social Security COLA was 0 percent in 2015 and 0.3 percent in 2016, 2.0 percent in 2017, 2.8 percent in 2018, 1.6 percent in 2019 and 1.5 percent in 2020, all increases lower than the historical average of around 3 percent), more retirees saw a reduction in their monthly checks. However, the 2021 Social Security COLA was 5.9 percent effective January 2022 and 8.7 percent in 2022 (effective January 2023), reflecting the significant increase in the rate of inflation. This helps offset Medicare Part B premiums, but retirees were hardly better off as COLAs are of course driven by higher consumer prices. As of this writing, the nonpartisan Senior Citizens League estimates Social Security benefits may increase 2.7 percent in 2024, more in line with historic norms.

Filing Rules and Strategies

Social Security is structured to motivate people to defer claiming, and those who do will reap significantly higher monthly benefits during their retirement. The earliest an individual may choose (or due to health or other personal circumstances, have no choice but) to claim Social Security benefits is age 62. However, someone claiming at FRA (in this case, 66) would gain 33.3 percent more. If that same person delayed claiming until 70 years old, he/she would earn 76 percent more than when filing at 62.

Individuals

For Americans who have never been married, deciding when to claim is generally straightforward, but a couple of determining variables should be weighed: retirement income (including potential wages from a job), budgetary needs, and life expectancy.

As far as Social Security is concerned, there are three types of claimers: early, at FRA, and deferred. Here is a basic chart that compares how much an **average** 62-year-old would receive

based on the filing date with the payments that individual would receive by waiting until FRA or age 70, assuming the current average monthly benefit of \$1,700 and an annual COLA of 2.5 percent beginning in 2024. Figure 2-2 shows the break-even point for each strategy; that is, the death age that maximizes benefits in each claiming scenario. Intuitively, the later one begins to receive payments, the longer one must live to maximize total benefits.

Figure 2-2 Social Security Income Projections

Start Social Security At	Lifetime Social Security Income Depends on Claiming Date and Life Expectancy		
	62 (Earliest)	66 (FRA)	70 (Latest)
Initial Annual Income	\$14,969	\$19,951	\$26,516
Live to 70, Total Lifetime Income	\$149,007	\$104,871	\$26,516
Live to 80, Total Lifetime Income	\$358,443	\$357,766	\$331,014
Live to 90, Total Lifetime Income	\$626,539	\$681,492	\$720,796

Married Couples

For years, couples were able to increase their retirement income by taking advantage of several claiming strategies, which provided retirees with some control over when to file and how much they could receive. Unfortunately, recent legislative changes “simplified” the filing process by adjusting two income-generating strategies known as “File and Suspend” and “File Restricted.”

Here are the three remaining available spousal claiming strategies combinations:

1. Husband files for his own benefit, Wife files for her own benefit
2. Husband files restricted application*, Wife files for her own benefit
3. Husband files for his own benefit, Wife files restricted application*

*Restricted Application: Spouse A files for benefits at FRA based on Spouse B’s record, then Spouse A receives own benefits at FRA, plus accrued delayed credits. This strategy can only be utilized by individuals who achieved age 62 by January 1st, 2016.

Ex-Spousal Benefits

Divorcees who were married for longer than 10 years can receive benefits from an ex-spouse’s record (even if the ex-spouse has remarried) if

- the claimer is unmarried (unless remarriage took place at age 60 or later)
- the claimer is aged 62 or older
- the ex-spouse is entitled to Social Security retirement benefits; and,
- benefits based on claimer’s employment history are less than ex-spouse’s benefits.

Note: The claimer’s benefit as a divorced spouse is equal to one-half of an ex-spouse’s full retirement amount if the claimer files at FRA. Even if the ex-spouse has not applied for retirement benefits, but can qualify for them, the claimer can receive benefits on the ex-spouse’s record if they are divorced for more than two years.

Claiming Early

At first glance, it certainly seems much more cost effective to resist signing up for as long as possible. However, several personal factors can influence a decision, including

- having no other source of income
- experiencing an earnings reduction that renders current income insufficient
- becoming a widow or widower (survivor benefits can start any time between age 60 and full retirement age)
- learning of limited life expectancy (say from a diagnosed medical condition).

Life Expectancy

Let's examine life expectancy a little more closely. If everyone lived to 100, the obvious answer would be to wait as long as possible to file, because claimers would have time to recoup lost benefits. This is of course unrealistic (and such certainty around mortality would drastically change the benefit calculus in any case), so attempting to determine life expectancy becomes one of the most important variables in the decision-making process.

If life expectancy is in question, or there isn't an immediate need for retirement benefits before FRA, the choice of when to claim may hinge on what age will generate the largest lifetime income; therefore, it is important to try to calculate a break-even point, or the age when the total Social Security income from two claiming options becomes equivalent.

Here is a simple illustration of a hypothetical Social Security claimant:

Based on Mary's last 35 years of work, she is eligible to collect \$1,400 per month in Social Security after her FRA, which is age 66. Mary wants to know her break-even point if she chooses to file at age 62. For simplicity, COLA is ignored.

Earnings at FRA	Penalty for Taking Early	Advantage	Total Benefits between 62 + 66	Divide Benefits by Monthly Penalty	Divide by 12 (Months in Year)	Add to FRA	Break-Even Point
\$1400/month	-25% or \$350/month	+ 48 months of collecting	\$50,400	$\$50,400/350 = 144$	$144/12=12$	66+12	78

If Mary claims at 62 and dies before age 78, she will have maximized her possible Social Security income.

As indicated, life expectancy may be the greatest single variable in determining how much an individual will receive in total lifetime Social Security benefits.

It is also extremely important to consider surviving spouses when weighing claiming options. If a husband (with a higher PIA) who suffers from a heart condition has a life expectancy of 73, and his surviving spouse has a life expectancy of 89, it may make sense to delay filing so that the wife can earn more for a longer period of time.

Optimizing Benefits

Going forward, does it make sense for people to try to optimize Social Security benefits? Perhaps now more than ever.

With more retirees facing a reduction in lifetime benefits, individuals and couples need to analyze alternative income streams based on various filing dates and actuarially calculated life expectancy, and personalized longevity projections become even more critical in determining a break-even point and/or optimized claiming strategy. Income benefits earmarked for dependents may also play an important role in determining the right time to claim.

Additionally, retirees need to be aware of their net income after Medicare premiums and surcharges are deducted from monthly Social Security checks and, if applicable, available survivor benefits. It is important to note that survivor benefits may have a significant impact on the quality of life of the surviving spouse, as this income stream can be used to pay for rising health care costs or long-term care services.

Finally, when developing a successful investment strategy to fund retirement, income sources such as Social Security and pensions must be incorporated when determining how much savings will be required in a 401(k), IRA, Roth, and various insured retirement products.

Social Security and Medicare

The Medicare Modernization Act of 2003 initiated a policy change that ensured Medicare premiums would be deducted from Social Security disbursements. Unfortunately, this will ultimately result in health care expenses slowly eroding Social Security benefits and dramatically reducing future retirement income.

Affluent Americans are certainly not exempt from high health care costs. Although they may receive more in Social Security benefits, Medicare outlays will increase because of means tested surcharges. An affluent couple retiring today will likely see over half of their Social Security benefits consumed by medical expenses.

Social Security and Medicare Means Testing

Means testing for Medicare Parts B and D was officially introduced in 2007. This basically translates into “The more you make, the more you pay.” Retirees who cross income thresholds can see their Medicare Part B Premiums rise from 40 percent to over 200 percent.

Social Security is included in the calculation of total annual income, which can push retirees to draw income from other sources — and depending on what those sources are, past means-testing thresholds. This means that even more will be deducted from Social Security to pay for Part B premiums.

Means testing is discussed in greater detail in Chapter 3, *Retirement Health Care*.

Cost-of-Living Adjustments

Social Security cost-of-living adjustments (COLAs) were implemented in 1973 to ensure that benefits would keep pace with inflation. The annual calculations are based on the percentage increase in the Consumer Price Index for All Urban Consumers, or CPI-U.

Pre-COVID, Social Security COLAs were expected to rise by an average of 2.5 percent annually (after a 2.8 percent increase for 2018). And indeed, the 2020 COLA was as anemic as the prior several years. As noted above, the effective 2022 COLA of 5.9 percent and a whopping 8.7 percent effective in January 2023 were much more significant but will likely still fall short of the pace of rising health care inflation, which is expected to increase by over six percent for the foreseeable future. An anticipated increase of less than three percent in 2023 may be largely consumed by both increased cost for health care and general inflation. Projected health care inflation is likely to continue to outpace anticipated Social Security COLAs — and more retirees will face means testing in the future — so it remains likely that a large percentage of retirees will eventually see their Social Security income largely consumed by health care costs.

Social Security’s Role in Retirement Planning

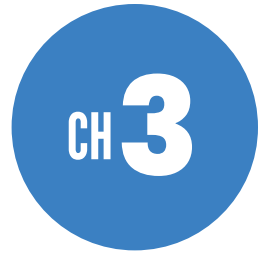
To be blunt, Social Security will simply not provide enough income for most Americans to survive in retirement. The program has evolved into a budgetary supplement that can potentially offset some retirement expenses, including a percentage of health care. As of 2022, the maximum Social Security Primary Insurance Amount (PIA) at full retirement age is \$3,345 per month, or \$40,140 per year. Using the example of a 65-year-old female in Chapter 1 (Figure 1-7), annual health care costs could range from 10 percent to 38 percent of that amount (not including potential income-based surcharges). After other household expenditures, such as housing, food, and transportation, little if any of that monthly check will be left over.

Conclusion

Deciding when to claim Social Security is personal and must be made in conjunction with other retirement planning strategies. A 62-year-old suffering from a chronic condition who can no longer work may be forced to file, while a healthy and financially stable 66-year-old may choose to wait.

Social Security’s most valuable feature is that lifetime monthly income is guaranteed — it can certainly be the cornerstone of a person’s retirement income portfolio. Combining Social Security benefits with stable investment products such as annuities and growth-oriented investments, such as mutual funds and stocks, can provide retirees with a measure of long-term financial stability as well as the potential to keep up with inflation.

Ultimately, in contrast to its often-perceived role in retirement budgets, Social Security must be viewed in the future as a complementary, not primary, source of retirement income that can help alleviate the growing burden of health care costs and supplement basic household needs.



Retirement Health Care

Because millions are entering the Medicare system every year, health and wealth in retirement are now inexorably linked. Americans will pay more for fewer benefits and will need to purchase supplemental coverage to fill in the gaps. Financial and health-related stability in retirement, a luxury enjoyed by most Americans since the passing of Medicare in 1965, will be replaced by the need for all consumers to place health care costs at the forefront of their retirement planning.

Health Care is a Significant Retirement Concern

Many people have little understanding of the long-term financial impact of health care costs. IRI's 2019 study on the Baby Boomer generation found that while 70 percent of Boomers who work with financial advisors have calculated a retirement savings goal, only half have considered health care expenses in those calculations. More than half also erroneously believe Medicare covers long-term care expenses. In the future, increasing premiums, expanded means testing, and Social Security Cost of Living Adjustments (COLAs) that may keep pace with general inflation, but not the accelerated inflation of health care, will exacerbate the problem.

There are four hard realities making rising health care costs the single greatest issue facing retirees:

1. Medicare is not free. Premiums, coverage gaps, co-pays, long-term care, and a host of other variables chip away at household budgets.
2. The double-edged sword of longevity means that Americans are living longer, but consequently are also more likely to outlive their retirement savings.
3. Health care inflation is increasing at more than twice the rate of Social Security COLAs.
4. The Affordable Care Act, through means testing (and other variables) had a significant long-term impact on Medicare costs.

Transitioning from Employer-sponsored Plans to Medicare

Research conducted by the California Health Care Foundation revealed that 56 percent of respondents were not aware of basic Medicare coverage options, and many Americans believe that Medicare will cover all or most of health care costs in retirement. In fact, original Medicare (Parts A and B) will only cover approximately 20 percent of total costs and retirees are responsible for 100 percent of costs for health coverage (Medicare Parts B, D and supplemental insurance) comparable to what many enjoyed under employer-sponsored plans (but were only responsible for 25 percent of premiums).

Parts of Medicare

A full analysis of the intricacies of Medicare is beyond the scope of this book, but it is useful to include a simple outline of its basic benefits.

The Difference Between Medicare and Medicaid

Medicare is an entitlement that everyone receives. To be eligible for Medicare a subscriber must be 65 years or older, a citizen for five years, or suffer from a qualified disability. Medicaid recipients must qualify based on their level of income, as Medicaid benefits are intended for those who cannot afford health care. Unusually, Medicare premiums were reduced in 2023 from 2022 rates due to lower than expected government spending on expensive drugs and other costs.

Medicare Components

- Medicare Part A—Free for most. Some may be required to pay premiums if neither they nor their spouses worked for 40 quarters. Medicare A is not all-inclusive; it covers most hospital care (but not all) and one wellness physical per year with no vitals or blood work.
 - Covered Services
 - Inpatient care
 - Skilled nursing facilities
 - Hospice care
 - Must enroll between October 15 and December 7
 - If eligible at age 65, subscriber has a seven-month period that begins three months before, includes the month of, and extends three months after 65th birthday
- Medicare Part B—Supplementary, but everyone enrolled must pay based on income.
 - Covered Services
 - Most other necessary medical services, such as doctor visits, physical therapy, medical equipment, etc.
 - Costs
 - 20 percent copay
 - In 2023, most first-time Medicare recipients are charged a monthly premium of \$164.90, a decrease of \$5.20 from 2022.
 - A small number of current enrollees pay slightly less due to a “hold harmless” provision that aligns premiums with the Social Security COLA
 - Premiums are deducted from Social Security
 - Individuals who make more than \$97,000, or a couple earning over \$194,000, may be subject to Part B surcharges
 - Additional penalties can be incurred for signing up late
- Medicare Part C—Formerly known as Medicare Plus Choice, now known as Medicare Advantage Plan.
 - Similar to HMO plans
 - Provides almost the same coverage as A and B at a lower cost, but some services require referrals and “in-network” restrictions can apply
 - Subscribers are responsible for 100 percent of the cost for out-of-network doctor visits
- Medicare Part D—Prescription drug coverage.
 - Covers most or all of six main prescription drug categories, but specific drug coverage and cost can vary and be quite complex
 - Premiums are based on terms and conditions set by private insurance companies
 - Everyone is eligible, but the open enrollment period lasts from November 15 to December 31. This is the only time when plans may be changed
 - Premiums can be impacted by income and state of residency

- Part D coverage gap (the “Donut Hole”)
 - Occurs when a person’s drug costs reach a set amount (\$4,660 in 2023)
 - The Donut Hole closed in for all drugs in 2020, so a subscriber entering the coverage gap is responsible for 25 percent of the cost of covered drugs.
 - When out-of-pocket costs for covered drugs reach \$7,400 in 2023, subscribers enter the Catastrophic Benefit Period, with significantly lower copays or coinsurance for the remainder of the year.
- Supplemental Insurance
 - Policies are purchased from private insurance companies
 - Covers copays, deductibles, and out-of-pocket expenses
 - Costs vary depending on the plan offered in each state

Prescription drug and supplemental insurance policies are regulated by the state, which approves carriers, policies that can be sold within its borders, and associated pricing. Therefore, retirees may discover significant price disparities for similar policies depending on where they choose to live.

State differences in retirement health care expenses highlight the problem of utilizing national averages when budgeting for future medical expenses. Instead, estimates of supplemental-plan costs should be based on a retiree’s planned state of residence.

Health Care Inflation

Estimates in the year-end summary from the Centers for Medicare and Medicaid (CMS) project that retirees will endure multiple years of health care inflation between 5 percent and 7 percent. Data from the Kaiser Family Foundation indicates the percentages of retiree household budgets spent on health care expenses is nearly three times higher than for working families (14 percent versus 5 percent), therefore inflation in health care costs will have a much greater impact on retirees than those still in the work force.

Long-Term Care

Medical advances in the latter half of the twentieth century have buoyed American life expectancy, but there is a downside to living longer, and that comes in the form of the potential need for long-term care (LTC). According to the Kaiser Family Foundation, in 2022 there were 15,183 Certified Nursing Facilities in the United States, with an average of 106.4 beds per facility (approximately 1.66 million beds), occupied by 1.2 million patients.

Types of Long-Term Care

Nursing Home Care is medically necessary and usually requires a residential stay. It is important to understand that Medicare covers required services such as physical therapy or post-surgery nursing, but it does not pay for custodial care, which provides help with the daily activities mentioned above. Medicare Part A may cover some costs in a sanctioned rehabilitation facility — under strict parameters and time constraints.

Assisted Living may or may not require inpatient treatment, but some care is necessary, such as redressing bandages. These are largely state-regulated, and are sometimes referred to as residential care, adult congregate care, or domiciliary care.

Home Health Care provides several medical-related services that can be administered in the home, such as injections, nutrition therapy, and wound care. Eligible patients must be under a doctor's supervision and require intermittent skilled nursing care, physical therapy, speech-language pathology services, or occupational therapy. The motivations behind acquiring care at home are lower costs, patient comfort, and maintaining independence.

According to the National Care Planning Council, the overall average stay in a nursing home is 835 days, and the average stay for those who have been discharged is 270 days. The 2021 Genworth Cost of Care Survey puts the daily cost of a semi-private room in a skilled nursing facility at \$260, or a total cost of \$70,200 to \$217,100 based on the average stay data. This is a potentially devastating expense for most retirees.

Long-Term Care Funding Options

Insurance

Long-term care insurance covers personal and custodial care in various settings, such as facilities, community organizations, or homes. The policies compensate recipients with a daily amount for services to assist with the Activities of Daily Living, which include eating, bathing, dressing, toileting, transferring (moving unassisted from bed to bath, for example), and continence. The cost of the policy depends on the contract owner's age when the policy is purchased, the maximum daily amount the policy will pay, the maximum number of times the policy will pay, the lifetime maximum amount the policy will pay, and any optional benefits chosen.

While long-term care insurance provides some relief for custodial care, coverage and premiums will vary so it is important to consult a financial professional for assistance in choosing the best option. Long-term care insurance premiums have seen high double digit percentage increases in recent years, driven by persistent low interest rates, increased longevity, and higher lapse rates.

Annuity

Annuities are also a viable funding option for LTC. There are a host of flexible annuities that can be used to either create a single-purpose plan targeting long-term care expenses, or a multi-purpose plan in which LTC is one expense among others. From an advisor perspective, a narrow focus is often more appealing to clients, but deciding which annuity suits a consumer is an exercise in balancing needs and resources holistically.

State-to-State Variance

The cost of long-term care varies greatly depending on state of residency. Prices fluctuate based on the availability and quality of care, economic factors, and population distribution. The cost of long-term care varies so greatly that choosing where to reside can have a tremendous financial impact on a fixed retirement budget. As noted in the Genworth study the median cost for a semi-private room in a nursing facility in Boston, Massachusetts is \$157,863, while in St. Louis, Missouri the cost is \$67,525.

Women and Long-Term Care

Women are especially vulnerable financially because they have longer life expectancies than men and are often left without enough savings after their spouses pass on. According to a “Women & Long-Term Care” fact sheet published by AARP:

- Over 70 percent of nursing home residents are women
- 70 percent of women 75 or older are widowed, divorced, or never married
- Women are around twice as likely as men to be living alone in their advanced years

A healthy 58-year-old woman living in Boston will have a life expectancy of 89 years and will have a 60% chance of requiring long-term care services at some point in her life.

- Average length of a future stay in a nursing home for this woman will be just over two years
- Average annual cost of nursing home care in the Boston area today is nearly \$158,000
- Estimated annual cost 30 years from now will be over \$500,000

If this 58-year-old woman is married to her 60-year-old husband, it is anticipated that she will live four years beyond her husband’s passing.

- His life expectancy will be approximately 87 years
- Average length of a future stay in a nursing home for a healthy 60-year-old male will be around 1.5 years
- Estimated annual cost 26 years from now will be over \$450,000

Medicare Means Testing

Since the passing of the Affordable Care and Medicare Modernization Acts, Parts B and D are now means tested. For subscribers, this means that higher incomes equal higher premiums. Medicare assesses surcharges by measuring *Modified Adjusted Gross Income (MAGI)*, which includes almost every potential source of income — including working in retirement, Social Security, pensions, required minimum distributions, earned interest, and capital gains.

When Modified Adjusted Gross Income (MAGI) surpasses \$97,000 for a single person and \$194,000 for a couple, surcharges are levied. There is also a two-year look-back period, which means that any income earned at age 63 can be counted when the subscriber signs up at 65. This rule can also become especially troublesome at age 72, when required minimum distributions (RMDs) must be taken, or when a spouse passes away, which may leave an income stream that could vault the lone survivor into a higher income bracket.

Crossing the first surcharge threshold increases Medicare Parts B and D by 35 percent, and surpassing the highest thresholds will inflate costs by more than 200 percent. The thresholds are not indexed to inflation and have been in place for several years.

The following is a breakdown of the current Medicare MAGI income brackets.

Figure 3-1 Medicare MAGI Income Brackets

Income Level (Individuals)	Income Level (Married, Filing Jointly)	Total % Increase
\$97,000 or less	Under \$194,000	0%
\$97,001 - \$123,000	\$194,001 - \$246,000	40%
\$123,001 - \$153,000	\$246,001 - \$306,000	100%
\$153,001 - \$183,000	\$306,001 - \$366,000	160%
\$183,001 - \$499,999	\$366,001 - \$749,999	220%
\$500,000 or more	\$750,000 or more	240%

Source: Medicare.gov

Lowering the income brackets appears to be an effort to extend the life of the Medicare trust fund, therefore it is unlikely that the trend of expanding means testing to include more middle class and affluent Medicare beneficiaries will end anytime soon.

Reducing MAGI through Investment Products

It is critical for future retirees to diversify their investments to include products that do not fall under MAGI; portfolio management can be especially important at age 72, when required RMDs must be taken, or when a spouse passes away, which may leave an income stream that could place the lone survivor into a higher income bracket.

Products including life insurance, non-qualified annuities, Roth IRAs and Roth 401(k)s, Health Savings Accounts (HSAs), longevity insurance, and even reverse mortgages can decrease MAGI and reduce Medicare Part B and D surcharges.

Income Replacement Ratios and Health Care

An income replacement ratio (IRR) is the percentage of pre-retirement income used to estimate how much investors will need to maintain their desired lifestyles throughout retirement. Income replacement ratios provide advisors with a streamlined, top-down approach to help assess retirement savings and income goals without having to calculate and project individual line-item expenses.

A basic assumption underpinning the use of IRRs is that evaluating pre-retirement income provides a solid foundation for calculating income needs during retirement since, for the most part, basic household expenses (housing, food, utilities) will continue after one stops working. The goal is for long-term IRR-based investments to produce sufficient income to last through retirement. While this may be effective to some degree, the truth is that retirees will have a significantly higher health care cost burden in retirement than when they were working — one that is not typically accounted for in IRR calculations.

A second assumption of IRRs is that overall expenses in retirement can be projected forward using an average inflation rate. While inflation rates of 2.5 percent to 3 percent are generally used in IRR calculations, health care costs are expected to rise at approximately 5 to 6 percent a year

for the foreseeable future. This can create a sizeable planning gap between calculated needed retirement savings and the impact health care costs will have on those savings in retirement. While IRRs can be an efficient strategy in the planning process, when applied to one of the most significant expenses in retirement — health care costs — the calculation may come up short.

While the gap may appear substantial, it is nonetheless manageable and can be closed through the implementation of slightly higher replacement ratios. This modification can motivate clients to make modest additional contributions to 401(k) plans, HSAs, Roth IRAs, annuities, or other products such as life insurance. With as little as \$100 in additional contributions per month (or even less), Americans can greatly strengthen their retirement savings and offset the potential gap from failing to factor health care into IRRs.

Conclusion

With medical care becoming more expensive and health care inflation expected to remain significantly above annual Social Security COLAs, health care will be among the most significant expenses for Americans in retirement.

To be prepared, retirees must understand the complexities of future health care expenses, develop strategies that can reduce the burden of these costs, and begin planning early. At a time when too few pre-retirees are saving at sufficient levels to achieve retirement security (even before health care is factored in), those who take action now, employ a knowledgeable advisor, and create a long-term plan to save for, manage, and reduce costs will be able to enjoy greater long-term financial security.

Annuities 101

What Is an Annuity?

Annuities have been around for centuries. In early Roman times, citizens would make a one-time payment to a contract known as an *annua* in exchange for income payments received once a year for the rest of their lives. Today, an annuity is an insurance agreement that comes in a number of different forms and can (1) help individuals accumulate money for retirement through tax-deferred savings, (2) provide them with monthly income that can be guaranteed to last for as long as they live, or (3) do both.

An annuity can be viewed as life insurance in reverse. Whereas life insurance protects a family's financial situation against the premature death of a breadwinner, an annuity protects an individual or a couple from running out of money at an advanced age. As with life insurance, annuity contracts are based on the principle of risk pooling; that is, the pooled funds of a large group are used to pay benefits to a relative few in any given year. The burden of not knowing how long one will live is shifted from the individual to the insurance company, which spreads the longevity risk among all annuitants, some of whom will die sooner than expected while others will live longer than expected. A good analogy is homeowner's insurance: the risk of fire is common to all homeowners, but during a given span of time only a few houses will burn down. For most people such an event would be financially devastating, so the risk is pooled using insurance.

Annuities can play a vital role in helping investors save for retirement and receive guaranteed lifetime income during retirement — effectively giving them the ability to create their own pensions. Unlike other investments, annuities provide a wide variety of benefit options that can protect against untimely death, provide principal guarantees, assure a specified amount of income when the contract is annuitized, guarantee withdrawals for life, or a combination of all of these.

What Role Can Annuities Play in a Comprehensive Retirement Plan?

Annuities are the only financial instruments available today, other than Social Security and employer-provided pensions, that can guarantee a lifetime stream of income during retirement. Along with giving retirees the peace of mind that comes from knowing they will not outlive their assets; annuities provide another important benefit — a way to increase current income.

Many of today's retirees are faced with the challenge of how to withdraw enough money from their portfolios to live comfortably during retirement without depleting their funds if they live a long life. Withdrawing money from an investment portfolio may not present a problem in the early years, but as retirees age, the risk of running out of money can increase dramatically. Allocating a portion of the portfolio to one or more annuities reduces this risk.

Annuity payments form an essential part of a comprehensive retirement plan along with Social Security and pension income. The amount of each annuity payment reflects the fact that some annuitants will not live as long as others. This "risk pooling" allows insurance companies to make annuity payments that are larger than would be possible through a systematic withdrawal plan, where an individual retiree periodically withdraws funds in amounts that give reasonable assurance that he or she will not run out of money. Thus, annuities can serve to both reduce the risk of running out of money in retirement and increase the amount of each income payment received.

Who Are the Parties to an Annuity Contract?

Most annuity contracts — and all commercial annuity contracts — are issued by life insurance companies. When the purchaser completes the application to buy an annuity, the contract owner, annuitant, and beneficiary are designated and identified as such in the contract.

Contract Owner

The owner of an annuity contract pays the premiums. He or she has certain rights under the contract, such as the right to make contributions, withdraw all or a portion of the contract value, or change the parties to the contract. The owner is usually an individual or couple but can also be a non-natural person such as a trust or a partnership. Special tax rules apply to annuities owned by non-natural persons.

Annuitant

The annuitant is the person upon whose life annuity payments are based. Often, the annuitant is also the contract owner, so payments continue as long as the owner/annuitant is alive. It is also possible for two people, such as an owner and spouse, to be designated as joint annuitants so that income can continue throughout either of their lives. This type of annuity is called a "joint and survivor annuity." While in most cases payments are made to the contract owner or annuitant, funds also can be paid to a third party referred to as a "payee."

Beneficiary

The beneficiary is the person designated under the contract to receive any payments that may be due upon the death of the contract owner or annuitant. Contingent beneficiaries, to whom payments are made in the event the primary beneficiary predeceases the owner or annuitant, may also be named in the contract.

Respective Rights of the Parties

Because annuity contracts can offer a great deal of flexibility in setting up income payments, the respective rights of the contract owner, annuitant, and beneficiary can vary. For example, under one insurer's contract, the owner may be entitled to receive annuity payments. Under another insurer's contract, the annuitant may be the party entitled to receive annuity payments.

What Types of Annuities Are Available?

A wide variety of annuities are available today, many designed to meet specific needs and help consumers achieve their retirement goals. With a deferred annuity, assets accumulate on a tax-deferred basis until distributions are made, usually during retirement; with an immediate annuity, the contract owner converts assets into income and starts receiving payments right away. Fixed annuities accumulate savings or distribute income at guaranteed rates and in guaranteed amounts; variable annuities accumulate savings or distribute income based on the performance of the underlying investment options chosen by the contract owner. Annuities can be part of an IRA, a qualified retirement plan such as a 401(k) or 403(b) (a "qualified" annuity) or may be purchased with after-tax dollars (a "non-qualified" annuity). The following is a more detailed look at various types of annuities.

Figure 4-1 Types of Annuities

	Deferred	Immediate
Variable (VA)	<ul style="list-style-type: none"> • Purchased either with a single premium or with periodic payments to help save for retirement; the contract owner determines the point at which accumulated principal and earnings are converted into a stream of income. • The contract value or income payments vary based on the investment performance of underlying subaccounts or a stated rate, if provided by the issuer. • Total sales of deferred VAs in 2022 were \$98.6 billion. 	<ul style="list-style-type: none"> • Purchased with a single lump sum; income payments begin within a short period — less than 13 months. • The income payments vary based on the investment performance of underlying subaccounts or a stated rate, if provided by the issuer. • Total sales of immediate VAs in 2022 were about \$0.1 billion.
Structured	<ul style="list-style-type: none"> • Structured annuities, also called Registered Index Linked Annuities (RILAs) use options on market indexes to provide purchases with upside potential and downside protection • RILAs carry investment risk, and are therefore a form of variable annuity • Total RILA sales in 2022 were \$36.4 billion (included in deferred VA total sales above) 	<ul style="list-style-type: none"> • There are no immediate versions of RILAs, but as a variable annuity they may be annuitized to create a fixed lifetime income stream
Fixed	<ul style="list-style-type: none"> • Purchased either with a single premium or with periodic payments to help save for retirement; the contract owner determines the point at which accumulated principal and earnings are converted into a stream of income. • Guarantees that the contract owner will earn a stated rate of interest during the accumulation phase of a deferred annuity and receive a defined amount of income on a regular schedule when the contract is annuitized. • Total sales of deferred fixed annuities in 2022 were \$192.2 billion. 	<ul style="list-style-type: none"> • Purchased with a single lump sum; income payments begin within a short period — less than 13 months. • The income payments are a pre-determined amount on a regular schedule. • Total sales of immediate fixed annuities in 2022 were \$10.3 billion. • Total sales of deferred income annuities (essentially “immediate” annuities with a five to 40 years waiting period before payments begin) in 2022 were \$1.0 billion.

Source: Morningstar, Inc.; Beacon Research

What Are the Differences Between Deferred and Immediate Annuities?

Deferred Annuities: A Way to Save Money for Retirement

Many people buy annuities because they want their money to grow tax-deferred while they are saving for retirement, and they want a guaranteed income stream once they retire. This type of annuity is called a deferred annuity. A deferred annuity contract has two phases — an accumulation or savings phase, and a payout or retirement income phase.

In the accumulation phase, the owner pays premiums (also referred to as purchase payments) into the contract to accumulate assets. Some contracts are purchased with a single payment and are called single premium contracts. Other contracts allow payments to be made at any time and are called flexible premium contracts. During the accumulation phase, the owner can surrender the contract or take one or more partial withdrawals.

In the payout phase, the owner (or other designated payee) receives income. When he or she wants payments to begin, the insurance company starts sending checks on a regular basis, typically monthly. The effective date of payments is called the annuity start date or the annuity commencement date. In certain circumstances, the insurance company will allow annuity payments to be commuted for a lump sum equal to their present value.

Immediate Annuities: When You Want to Receive Money Right Away

An immediate annuity (commonly known by the acronym SPIA, which stands for Single Premium Immediate Annuity, and may also be called a “payout” or “income” annuity) is purchased with a single premium and annuity payments begin right away (there is no accumulation period). If the owner chooses to receive monthly payments, payments usually begin at the end of the first month but may be scheduled to start any time within one year after purchase. An immediate annuity can be purchased using retirement savings, for example, from a 401(k) plan and/or personal savings, as a way to create guaranteed income payments during retirement. It can also be purchased using money from other sources, such as an inheritance or the sale of a business.

Annuity payments can be made over the lives of one or more individuals or for a specified number of years, e.g., for 10 or 15 years. Life annuity payments typically end when the annuitant dies, but various types of guarantees are widely available. For example, you can purchase a life annuity with 10 years of payments guaranteed. Under such an annuity, the payments will continue for the longer of 10 years or the annuitant’s life. In addition, insurers offer annuity payments that provide that if the annuitant dies before annuity payments equal to the premiums paid for the contract have been paid, the contract beneficiary will receive a lump sum equal to the difference between the sum of the annuity payments and the premiums paid (“cash refund”). As there are many payout options offered by issuing insurers, the owner should work with his or her financial advisor to assure that the payment feature meets his or her financial needs.

Data from the CANNEX annuity quoting platform shows about one-third of quote requests, a good proxy for sales, are for SPIA with cash refund, about 20 percent are for life-only payments, and the remaining approximately one-half are for life with periods certain of various durations, 10 years being the most common. More than 85 percent are for monthly payments.

Inflation-Protected Annuities

An inflation-protected annuity (IPA) is similar to an immediate annuity but payments are indexed to the rate of inflation. Initial payments will usually be smaller than they would be without the

inflation protection. Even at a moderate rate of 4 percent, inflation reduces the purchasing power of one dollar to fifty cents in approximately 15 years. IPAs guarantee a real rate of return at or above inflation. Very few life insurance companies offer true IPAs for sale in the United States (largely due to the difficulty of hedging the inflation risk). However, consumers can buy immediate annuity contracts available that provide pre-determined annual increases in the amount of annuity payments, e.g., 3 percent each year for the life of the contract. CANNEX data indicates more than 90 percent of quotes include no payment adjustment feature, i.e., no provision for increasing future monthly payments.

Structured Settlement Annuities

Structured settlement annuities are used to provide periodic payments to satisfy legal judgments. Structured settlement sales numbers are not included in the market data used in this publication.

What Are the Differences Between Fixed and Variable Annuities?

Fixed Annuities: Guaranteed Investment Performance

With a fixed annuity, the owner is guaranteed at least a minimum rate of investment return. The insurer declares a specific credited rate of return based on the investment performance of its general account assets. In the case of a deferred fixed annuity, the insurance company guarantees a minimum interest rate (also known as a minimum credited interest rate) on payments made by the owner during the accumulation phase. In many cases, an insurer will credit interest at a higher rate than the minimum for varying periods. This type of interest is often referred to as “excess interest.” The owner’s purchase payments are invested in the insurance company’s general account. When the annuity reaches the payout phase, the dollar amount of the annuity income payments is determined based on payment rates guaranteed at the time the deferred annuity was issued (or the insurer’s current payment rates, if higher) and are guaranteed for the selected payout duration, e.g., the owner’s life or a specified period of years.

Generally, fixed annuities involve less investment risk than variable annuities because they offer a guaranteed minimum rate of interest. The minimum rate is not affected by fluctuations in market interest rates or the company’s yearly profits. Some people like the security of knowing that their annuity payments will never vary or that they will receive at least a minimum amount of credited interest. Although they are less risky, fixed annuities generally offer less investment flexibility and less opportunity for growth than variable annuities.

Fixed Indexed Annuities: Market-Linked Interest Potential and Guaranteed Minimum Interest

A Fixed Indexed Annuity is a fixed annuity that typically provides the contract owner with an investment return that is a function of the change in the level of an index, such as the S&P 500, while guaranteeing no less than a stated fixed return on the investment. These products are designed for investors who want to partake in the benefits of a market-linked vehicle with a protected investment floor if there is a downturn in the benchmark index. Some indexed annuities also offer riders that guarantee income for life, even if the annuity value declines to zero.

Variable Annuities: Investment Performance Based on Portfolios Chosen by the Owner

With a variable annuity, contract owners may choose from a wide range of investment options called subaccounts, each of which generally invests in shares of a single underlying mutual

fund or, in some cases, in a “fund of funds (FOF),” which is a mutual fund that invests in several other mutual funds or in exchange-traded funds (ETFs). Variable annuity contract owners may direct the allocation of their contract value among subaccounts that correspond to a wide range of underlying mutual funds, such as equity funds, bond funds, funds that combine equities and bonds, actively managed funds, index funds, domestic funds, and international funds. Unlike mutual funds sold to the public, the mutual funds that underlie subaccounts are available only to investors in variable annuities, variable life insurance contracts, and in some cases, 401(k) plans, IRAs, and certain other investments permitted by applicable tax laws and regulations. Assets in a variable annuity can be transferred between subaccounts tax-free. As a result, investment decisions can be made based on an investor’s needs and strategy without worrying about the tax implications.

As with mutual funds, the investment returns of variable annuity subaccounts fluctuate. During the accumulation phase, the contract value varies based on the performance of the underlying subaccounts. During the payout phase of a deferred variable annuity (and throughout the entire life of an immediate variable annuity), the dollar amount of the annuity payments may also fluctuate if variable annuitization is chosen, again based on how the portfolio performs. Fixed annuitization generally produces equal payments over the time period selected (life only or life in combination with a minimum payment period).

Unlike mutual funds, annuities offer a wide variety of guarantees to protect a contract owner’s investment. Death benefits provide principal protection in the event a contract owner dies during a market downturn. Living benefit features protect against investment and/or longevity risk by providing guarantees that cover income, accumulation, and withdrawals for either a fixed number of years or for life.

In addition to variable investment options or subaccounts, many variable annuities offer a fixed account or fixed investment option. This means that during the accumulation phase of a deferred variable annuity, the owner can allocate payments not only to one or more variable investment options, but to a fixed interest option as well. The money allocated to the fixed option goes into the insurance company’s general account. A minimum rate of interest is typically guaranteed for a period of one or more years.

Registered Index Linked Annuities (RILAs) are a relatively recent innovation. RILAs generally do not offer subaccounts (although some include a money market subaccount); rather, purchase payments are invested in the insurer’s general account, and a portion is used to purchase options on one or more market indexes selected by the purchaser. The use of options provides some upside potential to contract owners in years when the index(es) perform well, and limit downside risk during years when returns are negative.

During the payout phase of some contracts, only fixed annuity income payments are offered. Other contracts provide fixed and/or variable payouts. Providing both types of payouts allows contract owners to take on the added risk associated with variable investment options while accumulating assets, and to manage their level of risk during retirement by choosing to have the rate of return guaranteed for at least some portion of their income payments.

What Are the Differences Between Qualified and Non-Qualified Annuities?

Qualified Plans versus Non-Qualified Plans

Annuities can be used in tax-qualified retirement plans, such as IRAs, pension or profit sharing plans, 401(k) plans, 403(b) plans, and certain governmental plans. These annuities are called qualified annuities and are typically funded with pretax dollars. (Some qualified annuities are purchased with after-tax dollars for use with Roth accounts, under which the annuity payments and other withdrawals are tax-free if certain tax rules are satisfied.) Annuities that are not used in qualified plans are called non-qualified annuities and are purchased by members of the general public with after-tax dollars.

The first variable annuity in America was designed and developed for a qualified retirement program offered by TIAA-CREF (now called TIAA) in 1952. As such, the variable annuity was available only as an investment within a tax-qualified plan until 1960, when the first publicly available variable annuity outside a qualified plan was developed and brought to market by the Variable Annuity Life Insurance Company (VALIC).

An annuity used in a qualified plan can provide contract owners with the same insurance benefits offered by non-qualified annuities, such as guaranteed death benefits, guaranteed living benefits, and guaranteed income payments for life. It does not, however, provide any additional tax-deferred treatment of earnings — tax deferral is provided by the qualified plan itself. (Other tax aspects of qualified and non-qualified annuities are discussed in Chapter 14: *Regulation and Taxation of Annuities*.)

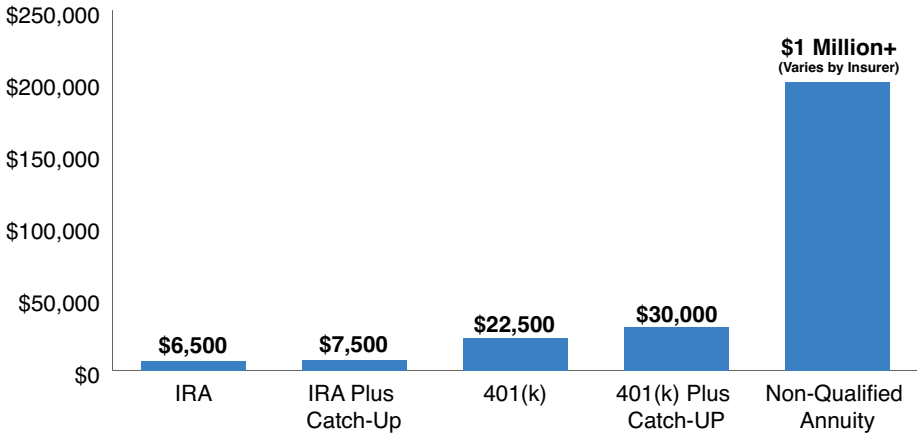
Figure 4-2 Qualified and Non-Qualified Annuities

	Qualified	Non-Qualified
Variable	<ul style="list-style-type: none"> • Purchased through retirement plans or IRAs using pre-tax dollars, up to specified limits. • The contract value or income payments vary based on the investment performance of underlying subaccounts. • Total sales of qualified variable annuities in 2022 were \$69.1 billion. 	<ul style="list-style-type: none"> • Purchased by members of the general public using after-tax dollars. • The contract value or income payments vary based on the investment performance of underlying subaccounts. • Total sales of non-qualified variable annuities in 2022 were \$29.6 billion.
Fixed	<ul style="list-style-type: none"> • Purchased through retirement plans or IRAs using pre-tax dollars, up to specified limits. • Guarantees that the contract owner will earn a stated rate of interest during the accumulation phase of a deferred annuity, and receive a defined amount of income on a regular schedule when the contract is annuitized. • Total sales of qualified fixed annuities in 2022 were \$111.9 billion. 	<ul style="list-style-type: none"> • Purchased by members of the general public using after-tax dollars. • Guarantees that the contract owner will earn a stated rate of interest during the accumulation phase of a deferred annuity, and receive a defined amount of income on a regular schedule when the contract is annuitized. • Total sales of non-qualified fixed annuities in 2022 were \$91.6 billion.
Total	<ul style="list-style-type: none"> • Total sales of qualified annuities in 2022 were \$181.0 billion. 	<ul style="list-style-type: none"> • Total sales of non-qualified annuities in 2022 were \$121.2 billion.

Source: Morningstar, Inc.; Beacon Research

Annuities used within qualified plans are subject to annual contribution limits (Figure 4-3 shows the limits for 2023). The government does not, however, limit the total annual amount of premium payments to non-qualified annuities. Insurance companies may impose maximum premium limits that are typically very high and do not affect most contract owners. Because of this feature, many people view non-qualified annuities as valuable personal retirement accounts to which they can contribute as much as they need for retirement.

Figure 4-3 Retirement Savings Plan Contribution Limits – 2023



Source: Internal Revenue Service – Publication 590, Individual Retirement Arrangements

Are Annuities Sold Outside of the Retail Market?

In addition to the annuities described above that are sold through the retail market, several annuities are sold through institutional or private markets. This includes group annuities as well as lesser-utilized annuity products such as private annuities, private placement annuities, and charitable gift annuities. While most of the remainder of the IRI Retirement Fact Book concentrates on individually sold annuities, a brief mention of these additional types of annuities is included for informational purposes.

Group Annuities

Group annuities are typically used as a retirement income plan for employees. Unlike annuities sold in the retail market, group annuity contracts are generally owned by the employer, and employees are participants. Certain individual annuities used in 403(b) plans may also be referred to as “group annuities,” but these are actually individually owned contracts purchased in a group setting and contributed to via payroll deduction, for example in the case of a retirement plan for employees of a university or hospital. Group annuities are covered in more detail in Chapter 12: *Tax-Qualified Retirement Plans*.

Private Annuities

In the United States, all commercial annuities are issued exclusively by insurance companies. A “private” annuity is not issued by an insurance company. Rather, it involves the transfer of property (such as real estate) from an individual or a revocable living trust in exchange for an unsecured promise by the transferee (an individual or a non-insurance entity, such as a trust) to make a periodic stream of fixed payments. The tax treatment of private annuities is complex and differs from the tax treatment of commercial annuities.

Private Placement Annuities

Private placement annuities are variable annuity contracts that are not registered under federal or state securities laws. They are available exclusively to investors who meet certain minimum net worth and income levels under such laws. The types of investment options available under private placement annuity contracts often include hedge funds, commodities, managed accounts, and other kinds of private equity offerings.

Charitable Gift Annuities

With a charitable gift annuity, a donor transfers cash or property (including appreciated property) to a charitable organization in exchange for income payments for life or joint lives, with no guarantee period. The federal tax law imposes specific requirements on the relationship of the amount donated and the value of the promised annuity stream. The charity can fund its payment obligations using its own assets, or it can fund them by purchasing a commercial annuity.

What Fees and Expenses Are Associated With Annuities?

What Fees and Expenses are Associated with Fixed Annuities?

A fixed annuity typically does not impose direct expense charges on the contract owner, other than surrender charges (charges for cancellation of the contract during its early years) for deferred fixed annuities. The spread, or difference between what the issuing company expects to earn and what it commits to pay out is intended to cover the insurer's expenses.

What Fees and Expenses are Associated with Variable Annuities?

A variable annuity, on the other hand, involves direct expenses in the form of insurance charges and indirect expenses in the form of management and other fees and expenses associated with the underlying mutual funds in which the variable annuity subaccounts invest.

Insurance, Administrative, and Distribution Charges

The fees and charges commonly associated with variable annuities include mortality and expense risk charges (M&E fees), administrative charges, and distribution charges.

In most contracts, the M&E fee pays for three important insurance guarantees:

- The ability to choose a payout option that provides an income that cannot be outlived at rates set forth in the contract at the time of purchase
- When available, a death benefit to protect beneficiaries
- The promise that the annual insurance charges will not increase

The administrative and distribution charges pay for all of the services involved in the maintenance of variable annuity contracts, such as the preparation of contract statements and mailings and other customer services. Some variable annuities also impose an annual contract fee that is similar to the annual account maintenance fee imposed by many IRAs. This fee generally ranges between \$30 and \$40 per year. Most insurers waive this fee for contracts with an accumulation or contract value of at least a certain amount, e.g. \$25,000.

Mutual Fund Fees and Expenses

Underlying mutual funds incur investment management fees and operating expenses, and in many cases, distribution charges known as “12b-1 fees,” which are named after the SEC rule that governs them. Investment management fees for the mutual funds that underlie the subaccount investment options in variable annuities are, on average, lower than those charged for publicly offered mutual funds. These lower fees have the effect of offsetting, to some extent, the insurance charges. See Chapter 9: Focus on Accumulation with Income Flexibility, for illustrations show how projected accumulation values can vary between variable annuity and mutual fund portfolios.

Surrender Fees

If a contract owner decides to cancel a deferred annuity during the early years of the contract, surrender charges may apply. These charges, if applicable, generally begin in a range from 5 percent to 7 percent of the amount invested and decline to zero over a period of time, such as five to seven years. Surrender charges are structured differently for different annuity products. (See the following section, How Are Variable Annuity Sales Charges Structured?)

Unbundled Fees

Some variable annuity contracts permit purchasers to select from a menu of optional product features, each of which usually has an associated charge. This unbundling approach gives customers the ability to select and pay for only those features they want. Optional features, referred to as riders, include, for example, enhanced guaranteed death benefits and guaranteed minimum living benefits. These riders typically have a separate, additional fee. See Chapter 8: Planning for Future Income, for data on these optional contract rider fees.

Premium Tax

States may impose premium taxes on variable annuity purchases. Currently California, Maine, Nevada, South Dakota, West Virginia, and Wyoming tax life insurance and annuity premiums, and only California and West Virginia tax qualified purchases. Tax rates range from 0.5 percent (California on qualified monies) to 3.5 percent (Nevada on non-qualified). Florida assesses a 1 percent tax on both qualified and non-qualified monies, but it is typically absorbed by the issuing insurance company.

How Are Variable Annuity Sales Charges Structured?

B-Share Variable Annuities

Most variable annuity contracts are B-share products. They are offered with no initial sales charge, but cancellation of the contract during its early years may trigger a withdrawal charge known as a surrender charge. These charges typically range from 5 percent to 7 percent of premium in the first policy year, and subsequently decline to zero, generally after five to seven years (known as the surrender charge period). Some annuity contracts impose surrender charges only during the initial surrender charge period that begins after the contract is purchased, while others associate a new surrender charge period with each subsequent premium payment.

Surrender charges underscore the long-term nature of the annuity product. As long as contract owners remain committed to accumulating money for retirement through their variable annuity, they generally will not incur these charges. In addition to surrender charges, B-share contracts have annual M&E and administration fees. B-shares accounted for over 80 percent of variable annuity sales in 2022.

A number of insurers have begun to offer other types of charge structures to meet different investor needs. The following are the most common.

A-Share Variable Annuities

Like A-share mutual funds, A-share variable annuities have up-front sales charges instead of surrender charges. Sales charges are calculated as a percentage of each premium payment.

A-share variable annuities offer breakpoint pricing, which means up-front sales charges decrease depending on the cumulative amount of purchase payments that have been made. In addition, assets that a contract owner has in other products in the company's product line may be recognized in the cumulative payment amount used to determine the breakpoint pricing. A-share contracts often have lower ongoing M&E annual fees than annuities with surrender charges. A-shares accounted for less than one percent of total VA sales in 2022.

C-Share or No-Surrender-Charge Variable Annuities

C-share, or no-surrender-charge variable annuities, offer full liquidity to owners at any time, without any up-front or surrender charges (although tax penalties may apply to withdrawals before age 59½). There are, however, ongoing M&E and administrative fees. C-shares made up about two percent of total VA sales in 2022.

I-share or Fee-Based Variable Annuities

I-share, or fee-based variable annuities, are intended for investors who favor paying one fee to have their investment portfolio managed by a registered investment advisor or fee-only advisor, (for example, a wrap-fee advisory program). Typically, the sale of an I-share does not result in a sales commission for an advisor from the issuing insurance company. However, the advisor assesses fees for the services, including the I-share contract, which is agreed upon by the client. Consequently, M&E annual fees are generally less than other share-classes due to the absence of commissions. I-shares have no surrender charges and may provide optional living benefit guarantees for an additional fee. I-share sales are a larger percentage of the VA market than they were several years ago; sales of I-shares have grown as overall VA sales have dropped, so I-shares are about eight percent of the VA market today versus three percent 10 years ago.

L-Share Variable Annuities

L-share variable annuities have no up-front sales charges. They typically have relatively short surrender charge periods, such as three or four years, but may have higher ongoing M&E and administrative charges than other share classes. It is becoming more common for L-shares to be structured as a B-share with an optional "buy down," which reduces the duration of surrender charges for an additional fee. This "liquidity rider" expires when the shortened surrender charge period is over, as does its fee. L-shares once accounted for almost one-third of the market but have almost disappeared from the VA landscape due to suitability concerns and represented less than 1 percent of total VA sales in 2022, with almost all this likely coming from additional purchase payments to existing contracts rather than new sales.

O-share Variable Annuities

O-shares are intended to merge the advantageous M&E and surrender charges of A-share and B-share variable annuities, respectively. Unlike A-shares, O-shares do not impose up-front sales charges, while, typically, possessing surrender charge periods akin to B-shares. Instead, M&E charges are assessed against both the account value and the premium, with the premium-based charges progressively declining throughout the surrender period, and ending after the surrender period. These features result in expenses similar to an A-share once the contract is free of surrender charges. The design of O-shares encourages investors to think of variable annuities as a long-term investment by rewarding longer holding periods with lower fees. O-shares were less than three percent of sales in 2022.

X-Share (Bonus) Variable Annuities

X-Share variable annuity contracts credit an additional amount or bonus to the contract value, which is calculated as a percentage of purchase payments added to the contract at or subsequent to contract issue. Bonus amounts generally range from 1 percent to 6 percent. For example, with a 3 percent bonus feature, a contract owner paying \$10,000 in premiums would have \$300 credited immediately to the balance. This category does not include contracts that credit additional amounts to the contract value after a designated period, sometimes referred to as “persistence bonuses.” Variable annuities with bonus credits may have higher ongoing expense charges and longer surrender periods than variable annuities without bonus credits. Some contracts allow the insurer to re-capture all or part of the bonus if the contract is surrendered within the first few years. Bonus contracts are difficult for companies to offer in a low interest rate environment, and there are far fewer available than there once were. There are only a few X-shares available for new purchase, and the class accounted for about one percent of total sales in 2022; as with L-shares, most if not all of these sales represent additional premiums paid into older X-share variable annuities.

What Are Guaranteed Minimum Death Benefits?

If a contract owner dies in the accumulation phase, a deferred annuity contract will, at a minimum, pay the accumulation value to a named beneficiary. Sometimes the contract may be continued by the beneficiary, with the beneficiary as the new owner. The contractual payout of this benefit varies by policy and can be payable as a lump-sum payment or as periodic annuity payments. (Fees associated with death benefits are discussed in Chapter 8: Planning for Future Income. The tax treatment of death benefits is discussed in Chapter 14: *Regulation and Taxation of Annuities*.)

Most, but not all, variable annuity contracts provide a standard Guaranteed Minimum Death Benefit (GMDB) during the accumulation period equal to the greater of (a) the contract value at death or (b) premium payments minus any prior withdrawals. The “return of premium” (ROP) GMDB gives contract owners the confidence to invest in the stock market, important in keeping up with market inflation, as well as the security of knowing their families will be protected against financial loss in the event death occurs as a time when the account value has incurred losses due to negative market returns.

The value and importance of the death benefit is periodically highlighted during major market corrections, such as the COVID-19 precipitated selloff in equity markets in March 2020; the financial crisis in 2008; or the technology stock led market downturn between 2001 and 2003. While markets inevitably recover and historically go on to reach new highs (as they certainly did in 2021!), the beneficiaries of variable annuity contracts owned by those who die during or

immediately after a huge selloff are protected. During each of these major market corrections, variable annuity beneficiaries received death benefits worth significantly more than the value of the annuities, protecting annuity value for beneficiaries. For a VA contract owner dying in a “trough” of financial market returns, the preservation of assets for heirs afforded by a GMDB, even a standard ROP, can be quite significant: estimates of unhedged GMDB exposure at the height of the 2008-2009 financial crisis were as high as \$15 billion, meaning \$15 billion of death benefit liability in excess of variable annuity account value. A similar circumstance occurred at the onset of the pandemic; contract owners who died in the early months when the market dropped precipitously before recovering were protected from those losses. Beyond ROP there are also several types of enhanced GMDBs that provide additional growth and/or protection of account value. The different types of enhanced GMDBs are described below, some of which have additional associated charges.

Contract Anniversary Value or Ratchet

Some life insurance companies offer death benefits that step up or increase based on pre-determined criteria. Called contract anniversary value or ratchet, these enhanced GMDBs are equal to the greater of (a) the contract value at death, (b) premium payments minus prior withdrawals, or (c) the contract value on a specified prior date. The specified date could be a prior contract anniversary date, such as the date at the end of every seven-year period, every anniversary date, or even more often. A ratchet GMDB locks in the contract’s gains on each of the dates specified.

Initial Purchase Payment With Interest or Rising Floor

Some insurers offer a rising floor GMDB that is equal to the greater of (a) the contract value at death or (b) premium payments minus prior withdrawals, increased annually at a specified rate of interest. In some cases, a ratchet and a rising floor may be available within the same contract. Some contracts offer a choice of a ratchet or a rising floor. Though they have become less common and more expensive in recent years due to low interest rates, they are still available.

Enhanced Earnings Benefits

Not all variable annuity death benefits are associated with protection against falling markets. Many variable annuity contracts offer enhanced earnings benefits (EEB) that provide a separate death benefit to help offset federal and state income taxes payable upon death on any gains in the contract. With this feature, beneficiaries receive not only the base death benefit amount, but also an additional amount that is usually equal to a percentage of the contract’s earnings at death, e.g., 40 percent.

What Are the Different Types of Guaranteed Minimum Living Benefits?

Prior to 1997, principal protection under variable annuity contracts was offered only in the case of death. In 1997 the first Guaranteed Minimum Income benefit was issued by Equitable, which offered contract holders the opportunity to generate annuity income from the greater of the account value or a guaranteed minimum amount based on the premium, after a multi-year waiting period. In subsequent years insurers developed other “living protection” against investment and/or longevity risk in variable annuity contracts by guaranteeing minimum accumulation values or withdrawal amounts. Some type of living benefit rider is offered on about two-thirds of “open” (i.e., available for new purchases) variable annuity contracts.

Various types of guaranteed minimum living benefit (GMLB) riders are described below. Besides offering these in new contracts, some companies allow them to be added to existing contracts. Guaranteed living benefits are usually offered as riders to variable annuity contracts for an optional charge. (Fees associated with guaranteed living benefits are discussed in Chapter 8: *Planning for Future Income*.)

Guaranteed Minimum Income Benefit

A guaranteed minimum income benefit (GMIB) rider is designed to provide the investor with a base amount of lifetime income when they retire regardless of how the investments have performed. It guarantees that if the owner decides to annuitize the contract (for life, life plus a certain period, or the lives of two people), payments are based on the greater of the contract value, or the amount invested credited with simple or compound “interest” at a rate of 1 percent to 3 percent. The “interest” creates a notional balance upon which annuity payments can be calculated; it does not represent account or cash value. An investor must annuitize to receive this benefit and there is typically a 10-year holding period before it can be exercised. Age limits may also apply.

Guaranteed Minimum Accumulation Benefit

A guaranteed minimum accumulation benefit (GMAB) rider guarantees that an owner’s contract value will be at least equal to a certain minimum percentage (usually 100 percent) of the amount invested after a specified number of years (typically 10 years), regardless of actual investment performance.

Guaranteed Minimum Withdrawal Benefit

First introduced in 2002 by The Hartford, a guaranteed minimum withdrawal benefit (GMWB) rider guarantees that a certain percentage (usually 4 percent to 6 percent) of the amount invested can be withdrawn annually until the entire amount is recovered, regardless of market performance. Reducing withdrawals in one year generally does not allow for increased withdrawals in subsequent years. However, if a contract owner defers withdrawals and the account value grows and is “locked in” at certain points as the new “benefit base,” the subsequent withdrawal amounts allowed may be larger.

If the underlying investments perform well, there will be an excess amount in the policy at the end of the withdrawal period. If they perform poorly and the account value is depleted before the end of the withdrawal period, the investor can continue to make withdrawals until the full amount of the original investment is recovered.

If the investor decides to terminate the contract before the end of the withdrawal period, he or she will receive the cash surrender value of the contract.

Guaranteed Lifetime Withdrawal Benefit

Another type of GMWB rider that guarantees withdrawals for life was introduced in 2004. The guaranteed lifetime withdrawal benefit (GLWB) guarantees that a certain percentage (typically 3 percent to 5 percent, often based on age) of the amount invested can be withdrawn each year for as long as the contract holder lives. This percentage may vary depending on the person’s age when withdrawals begin, whether the payment is guaranteed to continue for the life of one (single life) or two (joint life) individuals, and in some of the newest structures based on the level of an external benchmark such as the 10-year Treasury Constant Maturity Rate. More recently issued benefits may also include other levers that help the insurance company manage the risk of guaranteeing lifetime income on a variable annuity, such as a reduction in the withdrawal percentage rate if the account value is exhausted while income payments are still being made.

In many GMLBs, “step-up” features periodically, e.g., annually or every five years, lock in higher guaranteed withdrawals if investments do well. “Roll-up” features, conversely, increase the amount that may be withdrawn (by increasing the “benefit base” used to calculate withdrawals) during the deferral period, i.e., prior to the commencement of withdrawals. Allocation to a balanced or volatility managed fund, adherence to an asset allocation program, or a minimum allocation to a fixed or fixed income subaccount is often required when electing a GMLB. The liability risk to the insurer may also be managed through dynamic rebalancing, which shifts allocation toward more conservative investment options when equity returns are negative and/or market volatility increases.

In-Plan Lifetime Income Benefit

The standalone lifetime income benefit (SALB) was introduced in 2008. While the SALB did not get much traction in the individual market, the framework has evolved into a defined contribution plan option that embeds a lifetime income benefit into a target-date fund. Since this is not an annuity per se, under current law it is eligible as a Qualified Default Investment Alternative (QDIA), which participants can be auto-enrolled in with the option to opt out if they so choose. This provides in-plan income protection similar to that provided by GLWB on an individually purchased annuity, enabling retirement savers to create their own pensions within workplace plans. Combined with the SECURE Act and SECURE 2.0, which helped alleviate fiduciary concerns by providing a safe harbor for plan sponsors, strong growth is expected in this area in the coming years (see Chapter 14: Regulation and Taxation of Annuities, for more information about the SECURE Act).

Long-Term Care Protection

Some annuity contracts have features designed to address aging Americans’ concerns about long-term care (LTC). Many contracts permit owners to withdraw money from their contracts for long-term care needs without incurring surrender charges. Surrender charges may be waived if, for example, a contract owner has been confined to a nursing home for a minimum period or has suffered a critical illness. Some variable annuity contracts provide GLWB features that double the income payment during a qualified long-term care event, for example admission to a long-term care facility or the inability to perform the Activities of Daily Living (ADLs). Additional benefits may also be offered, such as eldercare resources, referral and consultation services, and discounted long-term care services from a specified group of providers. Hybrid annuity/long-term care products can provide valuable protection against the impact of long-term costs to consumers for whom traditional long-term care may be unaffordable, or unobtainable due to pre-existing conditions.

With the enactment of the Pension Protection Act of 2006, new hybrid products that combine annuities with LTC were introduced. Beginning in 2010, tax-free distribution status was given to both annuity assets and LTC rider benefits used for a qualified LTC purpose. Under prior law, withdrawals taken from the annuity to pay the LTC premiums were taxable and subject to a 10 percent penalty prior to age 59½.

How Is the Value of a Deferred Annuity Determined?

The accumulation period begins when the initial purchase (or premium) payment is made by the contract owner and the contract is issued by the life insurance company. Gifts, an inheritance, or any other source of income can be used to initiate or add to a contract. Typically, insurance companies have minimum requirements for initial and additional premium amounts. However, sometimes a life insurance company will permit a smaller minimum initial payment, for example,

\$1,000, if the purchaser agrees to pay premiums on a regular basis, e.g., through automatic payroll deduction. Insurers may also have lower minimum premium requirements for annuities in qualified retirement plans such as 403(b) or 401(k) plans. As is true for all qualified plans, contributions to annuities used to fund qualified plans must come from earned income.

How Is the Value of a Variable Annuity Measured?

The value of a contract owner's variable annuity is equal to the sum of the contract owner's account values in all the variable investment options or subaccounts plus the value of any amounts allocated to available fixed account options, if any.

Unit Values

Each subaccount has a unit value, which is similar to the net asset value (NAV) of a mutual fund. The unit value measures the numerical worth of the assets in a subaccount, per unit of the subaccount owned. The unit value increases or decreases, respectively, with the positive or negative investment performance of the underlying mutual fund in which the subaccount invests and is reduced by insurance charges and the fees and expenses of the underlying mutual fund. Unit values vary among the subaccount options inside a variable annuity. A contract owner's account value allocated to a particular subaccount is equal to the number of units of the subaccount owned multiplied by the current unit value.

Unit values apply to variable annuities in both the accumulation phase and the payout phase. Although the specific unit values differ between the accumulation and payout phases, the concept is the same. During the payout phase, contract owners are entitled to receive a determined number of units of benefit, which translate into an income payment amount based on the unit value at the time of payment. The unit value and resultant income payment may increase or decrease due to investment performance.

Variable Investment Options

Variable annuities offer investment choices called subaccounts, a selection of funds similar to publicly sold mutual funds, often managed by the same fund managers (most variable annuities also offer a fixed account, effectively an embedded fixed annuity, within the variable contract). The value of the subaccounts will fluctuate over time, and the variable annuity's return will be based on the investment performance of those subaccounts.

A variable annuity contract will generally permit the owner to choose from a range of subaccounts with different asset classes and strategies. The choices may include equity funds, bond funds, balanced funds, money market funds, and specialty funds such as international and sector funds.

The subaccounts are often managed by a variety of investment advisors, who may or may not be affiliated with the insurance company. Most of the largest mutual fund companies, and many smaller shops, offer subaccounts that serve as investment options or provide professional fund management services for variable annuities.

Variable Annuity Portfolio Allocation

Variable annuities offer investors a wide variety of funds to choose from to match their risk tolerance and views of the market. There are different types of asset allocation programs available to help variable annuity purchasers analyze their risk tolerance and decide on a specific mix of funds. Choosing the right mix can be a complex process.

Portfolio Rebalancing

Once a contract owner has decided on the investment mix best suited for his or her needs, premium payments are allocated in accordance with those percentages. However, as time goes by, market performance may alter the percentage of the variable annuity's contract value held in certain subaccounts (e.g., equity exposure may be significantly higher after a period of strong stock market returns). Many variable annuity issuers offer programs that automatically maintain a pre-determined investment diversification based on the specific needs of each investor. These programs, referred to as portfolio rebalancing programs, periodically reallocate variable annuity contract assets among fixed and variable investment options to reflect the proportions originally selected.

Dollar Cost Averaging

Contract owners who are wary of investing when the market is at a peak can take advantage of dollar cost averaging programs offered under many variable annuity contracts. An owner may choose to allocate a substantial portion of his or her premium payments to a particular stock fund. If the allocation is made all at once, it is possible that a single purchase price could be locked in when asset values of the stock fund are relatively high. With dollar cost averaging, the premium is systematically transferred (typically from the variable annuity's fixed account option or a money market option) to one or more stock, bond, or balanced funds over a specified period of time, with the goal of investing at lower, as well as higher, prices. While dollar cost averaging does not ensure a profit or protect against a loss, it can be an effective investment technique.

Importance of Tax Deferral to Portfolio Allocation

The benefits of tax deferral are vital to rebalancing programs and dollar cost averaging. In a taxable account, such as a stand-alone mutual fund, each time an investor sells a stock, mutual fund, or other investment, and replaces it with another in order to reallocate assets, the investor can be required to pay short- or long-term capital gains tax on any investment growth. With a variable annuity, an owner can rebalance between funds as desired without being taxed, thereby maximizing investment potential.

Transfers

While variable annuity contract owners may transfer money, tax free, from one investment option to another during the accumulation period, certain restrictions typically apply. Owners may be restricted to the number and amount of transfer payments allowed in any given year from a fixed account contained inside a variable annuity contract. Another restriction may also limit the number of transfers made among the variable investment options within a specified period of time. Transfers in excess of such limits may be subject to nominal administration charges or alternative transfer request methods, such as a requirement to send such requests via U.S. Mail versus online or telephonic instruction.

How Is the Value of a Fixed Annuity Measured?

Fixed annuities offer a rate of return that is determined by the insurance company for a set period of time, subject to a specified minimum. When the applicable period is over, the company may offer a new rate for the next period, which can be for a different length of time. Fixed annuities generally specify a minimum credited interest rate for the lifetime of the contract.

There are several types of deferred fixed annuities available, each with its own method of crediting interest.

- *Book value deferred* products earn a fixed rate for a guaranteed period. The surrender value is based on the annuity's purchase value plus credited interest, net of any charges.
- *Market value adjusted (MVA)* annuities are similar to book value deferred annuities, but the surrender value is subject to a market value adjustment based on interest rate changes.
- *Fixed indexed annuities (FIA)* guarantee that a certain rate of interest will be credited to premiums paid but also provide additional credited amounts based on the performance of a specified market index (such as the S&P 500).

Individual fixed indexed annuity contracts have additional interest crediting provisions. These include:

- *Crediting method* — the method used to measure the change in the underlying index, e.g., point-to-point or annual reset.
- *Participation rate* — the percentage of the calculated index gain credited to the contract owner as interest. This can be guaranteed or eligible for reset.
- *Spread/Margin* — the percentage by which the gross index gain is reduced before being credited to the contract owner as interest.
- *Cap* — the maximum index-based interest credited to the contract owner. This can be guaranteed or eligible for reset.
- *Volatility Controlled Indexes* — custom indexes intended to mute the effect of ups and downs in the markets they track; may be used instead of, or in conjunction with, participation rates, caps, and spreads.

What Happens to the Annuity Value if the Contract is Surrendered?

Deferred annuity contracts permit the contract owner to surrender the annuity contract during the accumulation period and receive a cash payment from the insurance company. This amount is called the cash value or cash surrender value of the contract. It equals the sum of premiums paid plus any earnings, minus prior withdrawals and charges deducted. The owner may take partial withdrawals or fully surrender the contract during the accumulation phase. Penalties for early withdrawal may be incurred and federal income taxes will apply to any gain in the contract value. The amount paid to the contract owner on surrender may be subject to surrender charges, which generally range from 5 percent to 7 percent. Some deferred annuity contracts impose surrender charges only for an initial period after the contract is purchased; others start a new surrender charge period for each individual premium paid. Surrender charges usually decline to zero over a period of time, such as five or seven years.

A partial surrender is the withdrawal of an amount less than the entire cash surrender value of the contract. Partial surrenders can also be taken as a pre-scheduled series of payments under a systematic withdrawal plan. Many contracts permit annual withdrawals of an amount, such as 10 percent of the contract value, free of a surrender charge. Tax penalties may apply, however, in the event such withdrawals occur prior to the contract owner reaching age 59½.

How Are Annuities Used to Generate Retirement Income?

While much of the focus on annuities in recent years has been on their value as a savings vehicle for retirement, their value as a source of lifetime income during retirement is equally important. Traditional sources of guaranteed retirement income are diminishing at the same time retirees are living longer, more active lives. This places the burden on individuals to both carefully save for retirement and wisely manage their investments during retirement, so their money lasts as long as they live. How retirees decide to receive income from their annuities once they retire can play an important role in achieving this outcome.

What Are the Various Options for Receiving Retirement Income?

Once a person is ready to retire, annuities offer a number of retirement income options. The contract owner can choose to receive all the assets from the annuity at once, opt for a series of withdrawals of his or her choosing until all the assets are exhausted, or decide to exercise the annuitization features of the contract.

The following information pertains to non-qualified annuities that are purchased with after-tax dollars. While the payout options available are the same for annuities purchased as part of qualified retirement plans, as discussed in the last section of this chapter the tax consequences are different.

Lump-Sum Option

When a contract owner elects a lump-sum distribution, the annuity is surrendered and all assets are withdrawn from the contract. Taxes will be due on earnings in the year the money is received, and tax penalties may apply to withdrawals before age 59½. With this option, individuals are still faced with the need to generate a guaranteed stream of income.

Systematic Withdrawal Plan

With a systematic withdrawal plan, the assets are left in the annuity and the contract owner receives distributions at regular intervals until the assets have been exhausted or the contract owner elects to suspend the operation of the plan. All earnings on the investment are considered to be distributed before any return of principal and are taxable at ordinary income tax rates. Assets remaining in the annuity continue to grow tax deferred until withdrawn.

The principal advantages of a systematic withdrawal plan are the flexibility provided to the contract owner and the ability to maintain full ownership of the assets. The principal disadvantage is that the contract owner retains the risks associated with both uncertain longevity and investment fluctuations, particularly the exposure to adverse market performance during the early stages of retirement.

If a specified dollar amount is withdrawn each period, whether adjusted for inflation or not, the contract owner assumes the full risk of market cycles. The very principles that recommend dollar cost averaging as a successful strategy for entering the market work against the contract owner in a liquidation strategy. Withdrawal of a fixed dollar amount means that a higher percentage of assets will be liquidated in a down market than in an up market. This can be a very dangerous strategy, even if long-term investment performance meets anticipated targets, since the withdrawal of assets in earlier years can prevent the overall portfolio from achieving the projected return.

The withdrawal of a specified percentage of assets rather than a specified dollar amount may help reduce this risk. Many people plan their retirement income based on an average rate of return on their investments (such as 8 percent). If they happen to retire during a time of far lower (or even negative) returns, however, the specified percentage of assets they withdraw may not provide sufficient income to maintain their desired lifestyle. To help reduce the impact of market fluctuations on retirement income, it is important for retirees to have a variety of diversified investments in their portfolios, including annuities, which can help create a guaranteed source of income that will last as long as they live.

Guaranteed Withdrawals

Contract owners electing a guaranteed minimum withdrawal benefit (GMWB) rider can choose to receive the value of their investment through annual withdrawals (up to a set percentage) at least until the entire amount invested is completely recovered. Contract owners electing a guaranteed lifetime withdrawal benefit (GLWB) can choose to withdraw a percentage of their contract value each year for as long as they live, even if the account value is exhausted. Distributions are deemed to represent investment earnings until total payments equal the account value in excess of total purchase payments and are taxable at ordinary income tax rates, after which time payments are deemed return of principal and are not taxed. Payments made by the insurance company after the account value is reduced to zero are deemed ordinary income and taxed as such.

Contract owners electing these benefits have greater control over their assets but may receive lower monthly payments than if they annuitize. While some GLWBs are beginning to tailor the percentage withdrawal to the age of the contract owner, it is only through annuitization that an investor can maximize the benefit of mortality risk pooling.

Annuitization

Annuitization involves turning the contract owner's accumulated assets into a stream of income based on the amount of the contract, the annuitant's age, payout choices, etc. The insurance company guarantees that it will provide payments for the life of the annuitant(s). With a deferred annuity, money is saved and invested during the accumulation period, and then annuity payments are received during the income period (e.g., during retirement). With an immediate annuity, payments begin immediately or within one year after the annuity is purchased. Payments can be either fixed or variable and guaranteed for one person's life, for the lives of two people, and/or for a specified period. Payments may also be structured with a cash refund feature, which provides for a payment to beneficiaries of an amount equal to the difference between the annuitized amount and the total payments made prior to the annuitant's death, should death occur before payments at least equal the amount annuitized.

Deferred Income Annuities

With a deferred income annuity (sometimes called longevity insurance), a retiree can purchase a contract at one point in time, for example, at age 65, but defer payments until a later time, for example, at age 85. Individuals not living until the commencement age will not receive benefits;

and individuals who do live to the required age and beyond, will receive income payments. Because these products usually have no death or living benefits, and not all contract owners will live long enough to collect income, insurance companies can maximize insurance leveraging (risk pooling) and thus make larger income payments to retirees still living. Recent innovations include optional death benefit and joint and survivor payments, but the trade-off is a higher premium or smaller monthly payments. The issuance of new regulations from the U.S. Treasury in June 2014, the “Qualified Longevity Insurance Contract” rules, provided clarity around the use of these products in qualified plans by establishing a deferred income annuity purchase amount limit of the greater of 25 percent of account value or \$125,000 and created provisions for the addition of a death benefit and the ability to reverse an excess purchase payment in order to avoid tax penalties. The SECURE 2.0 Act removed the 25 percent limitation and increased the QLAC purchase limit to \$200,000 for 2023.

What Are the Benefits of Annuitization?

By exercising the annuitization option of a deferred annuity (or by purchasing an immediate annuity), the contract owner can transfer the longevity risk to the insurance company and, if a fixed annuity is chosen, the investment risk as well.

As mentioned earlier, annuities are the only financial instruments available today, other than Social Security and pensions, that can guarantee a lifetime stream of income during retirement. Annuitizing a portion of retirement savings provides retirees with an effective hedge against outliving their assets. And because annuity owners are part of a mortality pool, the annuity payments received are larger than they could generate by saving on their own and systematically withdrawing funds in amounts that give them a reasonable assurance of not running out of money.

As part of a comprehensive retirement portfolio, annuities both reduce the risk of running out of money if a person lives a long life and increase the amount of each income payment received.

What Types of Annuity Payout Options Are Typically Available at Annuitization?

One of the first choices contract owners may have to make once they decide to annuitize is whether to receive fixed or variable payments. Owners of deferred fixed annuities can elect only a fixed payout option. Owners of deferred variable annuities, however, can sometimes choose either fixed or variable payouts. Once a selection is made, it is usually irreversible. With fixed payments, the insurance company sets a given amount it will pay (typically monthly) for the term of the contract. With variable payments, the amount of each payment is not guaranteed but changes with the performance of the underlying portfolio selected by the contract owner. Fluctuations in these payments can sometimes be reduced by opting for level payments (which hold payments level for a certain period of time) or stabilization guarantees (which provide a floor below which payments will not fall).

Life Annuities

A life annuity provides an income stream guaranteed to last as long as the annuitant lives. Under a straight or pure life annuity, annuity payments stop when the annuitant dies. A joint and survivor annuity (often selected by spouses) provides income for as long as either of the two annuitants is alive, although the amount of each payment will be less than if the payment were based on a

single life. Payments can stay the same or decrease after the death of the first annuitant. Under a joint and two-thirds annuity, each payment made after the death of the first annuitant is two-thirds of the amount paid while both annuitants were alive. This can be an effective strategy, as it results in a higher payment when both annuitants are alive and expenses will likely be lower for one person than for two.

As discussed previously, a valuable feature of an annuity is the fact that it can generate higher income payments than an individual systematic withdrawal plan and continue payments for as long as a person lives. But what about the investor who does not live long enough to receive many payments? There are a number of options for mitigating this risk. Each, however, results in a lower basic periodic payment.

Period Certain Annuities

With a period certain annuity, payments are guaranteed to continue for a specified time, for example, 10 years, no matter how long the annuitant lives. If the annuitant dies before the period has expired, payments continue to the designated beneficiaries for the remainder of the period. Period certain annuity payments typically are available for periods from five to 30 years. This option, however, offers no protection against longevity risk as payments are only made for the fixed period selected.

Life Annuities With a Period Certain

Life annuities with a period certain option guarantee payments for the life of the annuitant, but also guarantee that these payments will continue for a set period of time if the annuitant dies before the period has expired. Payments continue to the designated beneficiaries until the guarantee period has ended.

Cash Refund Annuities

With a pure life annuity, payments stop when the annuitant dies. In the most extreme case, an annuitant could die after one payment is made. Some annuitants prefer to hedge against this possibility by setting up a life annuity with some form of refund feature. As indicated earlier, adding such provisions results in a lower payment than would otherwise be the case.

There are two types of refund annuities now being offered that pay a refund to the beneficiary if the annuitant dies before the total of the annuity payments received equals the premiums paid for the annuity.

- *A cash refund annuity* provides for a lump sum refund of the premium minus the annuity payments already made at the time of the annuitant's death.
- *An installment refund annuity* provides that payments will continue in installments until the amount received is equal to the premiums paid.

Risk Tolerance vs. Longevity

In deciding what type of annuity payment option to choose and how much to commit to it, individuals must determine their risk tolerance with respect to their possible longevity, as well as the relative importance to them of receiving lifetime income versus leaving money to their heirs. All else equal, individuals who live beyond average life expectancy will generally realize higher income but lower estate values when using annuities versus other approaches.

How Are Variable Annuity Payment Amounts Determined?

The amount of each payment received from a fixed annuity is calculated at the time of annuitization and does not change during the life of the contract. The amount of each variable payment, on the other hand, fluctuates based on the investments chosen. Since the investment return of the portfolio cannot be determined in advance, some assumptions must be made in order to calculate the amount of the initial payment under the contract. This is accomplished by selecting an assumed interest rate, or AIR. After the initial payment, each subsequent payment is determined by adjusting the previous payment up or down based on the actual performance of the underlying portfolio for the period of time in question. If the portfolio earns more than the AIR, the subsequent payment will increase. If the portfolio earns less, the payment will decrease. If it earns the same amount, the payment will stay the same.

Some contracts set the AIR, but most allow the contract owner to choose from a range (usually 3 percent to 6 percent), the outside limits of which are set by state regulations. Selecting a low AIR will cause payments to increase faster with higher positive returns, or decline more slowly with low or negative returns, than if a higher AIR were selected. However, the initial income payment will be less than if the higher AIR were selected.

Level Annuity Payments

Some variable annuity contracts provide payment streams that can be adjusted at periodic intervals of up to 12 months, rather than monthly, to provide the annuitant with an element of certainty. This allows the annuitant to plan on a given level of payments for the period in question. When the periodic adjustments are made, however, they are likely to be more substantial than if the adjustments had been calculated more frequently.

Payment Stabilization Guarantees

Other variable annuity contracts offer payments supported by “floors.” These floors guarantee that subsequent payments will never be less than a given percentage of the original payment e.g., 85 percent or 100 percent, regardless of the performance of the underlying portfolio. Some provisions, limit the investment choices underlying the annuity, providing the insurance company with the opportunity to hedge its guarantee with derivative instruments. These floors provide contract owners with a safety net that may make them more comfortable with having their annuity payments subject to the variability of stock market performance. If a contract owner chooses this feature, however, payment amounts will be lower than if no floor were elected.

Liquidity Options

Historically, once an annuity contract was annuitized the stream of payments could not be altered. Some insurance companies now offer life annuities that allow annuitants who have also selected a period certain option to receive an advance of a given percentage of income payments, subject to certain restrictions that vary by company. These partial commutations, as they are called, reduce the remaining annuity payments. Some companies also allow the liquidation of the entire annuity, converting the value of the future stream of income into a lump-sum payment. If this option is exercised, all future payments cease.

How Are Annuity Payments Taxed?

If an annuity (fixed or variable) was purchased with non-qualified or after-tax dollars, a portion of each payment is considered to be a tax-free return of principal. The remainder of the payment is subject to taxation to the extent it represents earnings. Current federal income tax law specifies that the taxable portion of annuitized payments is taxable at ordinary income tax rates.

To determine the amount of each fixed annuity payment that qualifies as a tax-free return of principal, the insurance company makes an underlying calculation based on a formula known as the “exclusion ratio.” For variable annuities, since the amount of each future payment is unknown, a different calculation is performed to determine the exclusion amount.

If an annuity was purchased with qualified or pre-tax dollars using funds from a 403(b), a 401(k), or an IRA (other than a Roth or an after-tax IRA), the full amount of each distribution is taxable at ordinary income tax rates, even the amount attributable to principal.

Qualified assets, once they have been annuitized, are not subject to the required minimum distribution rules of the Internal Revenue Code since the insurance company is deemed to have already made the appropriate calculation for a lifetime distribution of the underlying assets. (See Chapter 14: *Regulation and Taxation of Annuities*, for more details on taxation.)

How Are Annuities Used in Estate Planning?

A variable annuity, while not designed as an estate planning tool, does offer some benefits in this area. An annuity avoids probate, provides flexibility when passing on assets to heirs, and can potentially increase the likelihood of leaving a larger estate in some circumstances.

Variable Annuities Avoid Probate — A variable annuity is a contract between an owner and an insurance company. The contract requires that a beneficiary be named. When a contract owner dies, there is a payout directly to the beneficiary. As a result, the annuity assets do not go through the probate process.

Probate, or the distribution of a deceased’s assets via the court system, can be costly and time consuming. There are attorney fees, court costs, and administrative expenses, and the process slows the distribution of proceeds. Plus, probate proceedings are a matter of public record. Assets held in a variable annuity bypass this process and go directly to the beneficiary.

Variable annuity proceeds will be subject to probate only if the estate is named as beneficiary, when no beneficiary is named, or when a death benefit is disclaimed by the beneficiary and no contingent beneficiary is named.

The Restricted Beneficiary Option Offers Advantages — Naming a restricted beneficiary is a unique option available to an annuity owner. This enables the owner to direct the amount, frequency, and timing of the distributions. Choosing the restricted beneficiary option provides the added benefit of continued tax-deferral over the life expectancy of the beneficiary. The individuals named as beneficiaries get payouts over a period of time, during which the proceeds grow tax deferred and compound over time, potentially providing many times more from the investment than a lump-sum payout. An individual must be directly named as beneficiary to take advantage of this treatment. It is necessary to complete paperwork instructing the insurer how

to distribute the death benefit proceeds.

A Single Premium Immediate Annuity as an Estate-Building Tool — Here is an example of an annuity product that can, under some circumstances, increase the value of an estate. A single premium immediate annuity (SPIA) is usually not considered to be a vehicle that can help preserve or increase the size of an estate. Indeed, many people have the false belief that a SPIA always reduces the size of the estate. However, for those retirees who need to make regular withdrawals from their assets, a portfolio that uses a SPIA is more likely to leave a larger estate than a portfolio without it. Consider an example. Most retirees, especially as they age, place at least half of their money in fixed investments, usually bonds or certificates of deposit. Regular income is often taken from these fixed investments. As of July 2023, the average 10-year High Quality Market (HQM) Corporate Bond Spot Rate was 5.14 percent, about 40 basis points higher than at the same time last year. For a retiree to withdraw \$1,000 a month (\$12,000 per year) from high quality corporate bonds, that person would have to invest approximately \$235,000, versus almost \$500,000 before rates began to rise in 2021, illustrating the tremendous impact interest rates have on income streams during retirement. In 10 years, the retiree would still have the \$235,000 investment “at par,” or the redemption value of the bonds. However, the actual value of the bond holdings would be lower if rates had risen and higher if they had fallen.

However, rising rates benefit retirees using annuities for income as well. A 70-year-old male could elect to receive the same \$1,000 monthly income from a SPIA with a 10-year certain period for a premium of about \$145,000. Imagine this hypothetical retiree has the same \$235,000 to invest for retirement income. He can use \$145,000 for the SPIA purchase while investing the remaining \$90,000 in a side fund for long-term growth. After 10 years, assuming an annual return from a balanced portfolio of approximately 9.7 percent per year, the side fund would grow to the same \$235,000. The side fund also has the potential to grow significantly larger if returns are higher, as would certainly be possible based on the long-term average return of a diversified investment portfolios. Additionally, options such as Registered Index Linked Annuities (RILAs) enable participation in market growth with some protection against potential extreme market loss events discussed earlier. According to the Center for Research in Security Prices, the historic average annual return of a 60 percent stock, 40 percent bond portfolio from 1961 through June 30, 2021 was about 10 percent, which would grow the hypothetical side fund in this example to over \$240,000. In addition, the retiree continues receiving the \$1,000 monthly payment from the annuity for life, while the bond holder would get no further income after the bonds mature and may have to reinvest the proceeds at a lower interest rate (though the value of the bonds would likely have risen in this scenario, providing a partial offset). A 70-year-old male has an 80 percent chance of living 10 years, a 63 percent chance of living 15 years, and four in 10 70-year-olds can expect to reach at least age 90, which means that most people who buy a SPIA at age 70 will be alive at age 80 and are likely to have more money and more income with a SPIA and a side fund than if they relied solely on bonds for income.

A Variable Annuity Offers a Death Benefit — Most variable annuities offer a death benefit, which guarantees that if the annuity owner dies at a time when the market value is less than the money they put into it because of market declines, the beneficiaries will get the original purchase amount, minus any withdrawals that may have made. In some cases, the beneficiaries can receive more than was invested via an enhanced death benefit, which steps up the death benefit payout based on positive performance of the investments, or a fixed percentage increase annually in the promised death benefit payout. A beneficiary must often recognize income and pay taxes on the earnings portion of the death benefit payout. The earnings enhancement death benefit can help offset a higher tax bill.

Overall, annuities are not designed as estate-planning tools. But these products do help a person protect his or her financial security and can often lead to a larger estate if an annuity is invested in a retirement portfolio.

How Are Annuity Products Developed and Sold?

In the United States, commercial annuities are issued by insurance companies. When new fixed and variable products are developed, they must be filed with the state's insurance department. Before these products can be sold, each state where they will be available must provide written approval.

Because variable annuities are considered securities as well as insurance products, when a new variable annuity is developed, a registration statement must be filed with the Securities and Exchange Commission (SEC). This statement includes a prospectus that discloses, among other things, the fees and charges associated with the annuity contract; a description of the various benefits, rights, and privileges afforded under the contract; any changes that can be made to the contract; and the risks and tax consequences associated with investing in the contract. The prospectus, which is updated annually, is a vital source of information for all contract holders and should be read thoroughly.

Insurance Company Ratings

Annuity guarantees are subject to the claims-paying ability of the issuing insurance company. It is therefore important to consider the financial soundness of a company before making a purchase. Companies are rated by one or more of the following independent industry analysts: AM Best Company, Standard & Poor's, Fitch Ratings, and Moody's Investors Services. The ratings do not apply to the underlying mutual funds, which are subject to market risk and will fluctuate with changes in market conditions. Ratings can differ somewhat among the analysts, so it is useful to check the ratings from at least two analysts.

Who Can Sell Annuities?

People who sell variable annuities need training in both securities and insurance. This training can be obtained from many sources. Some distributors provide in-house training to their registered representatives; others utilize training provided by insurance company wholesalers and independent third-party educators.

Fixed annuity sellers receive much of the same instruction as those selling variable annuities but do not need the securities training.

To legally sell annuities, individuals must first obtain a state insurance license from the state in which their office is located. A non-resident license must be obtained for all states in which out-of-state clients reside.

Since variable annuities are considered securities under federal securities laws, individuals who wish to sell them must, in addition to having an insurance license, be associated with a broker-dealer, be federally registered as a representative, and pass a Series 6 exam, or the more comprehensive Series 7 exam. In some jurisdictions, a state securities license is also required.

Where Can Annuities Be Purchased?

Some insurance companies sell their products only through a dedicated sales force (captive agents); others use agents who represent many companies and have no primary relationship (independent agents). But annuities can also be purchased from a variety of different sources, some of which may sell both fixed and variable annuities while others may market only one type.

Variable annuities can be purchased through several distribution channels, such as independent FINRA firms, wire houses, regional investment firms, captive agents, and banks. Fixed annuities are sold through these same distribution channels, yet sales are dominated by independent agents and banks. The difference in the percent of sales by distribution channel for fixed and variable annuities may be explained, at least in part, by the fact that purchasers of fixed annuities tend to be more conservative with their investments than those who buy variable annuities.

How Are Variable Annuity Commissions Determined?

Broker-dealer firms may be paid a commission by insurance companies when they sell variable annuity contracts. The amount of compensation depends upon the issuing insurer, the relationship the broker-dealer has with the insurer, the types of annuities sold, the amount of money invested in the annuity, and the way commissions are paid. Commissions can be paid in full at the time the annuity is sold, as a level commission over the life of the contract or some other period, or as a smaller amount at the time of the sale with a trail commission paid each year thereafter for a period. Both fixed and variable annuities may also be sold within managed, fee-based accounts, where the account is charged an ongoing annual fee and there is no commission paid on the sale of the annuity.

Registered sales representatives are, in turn, paid a commission when they sell an annuity contract. Commissions paid to representatives are generally less than the full amount paid to the broker-dealer and may or may not be on the same basis. Also, certain management personnel, such as branch managers, may be paid for sales made by representatives over whom they have supervisory responsibility.

In addition to commissions, the broker-dealer may receive other forms of compensation from insurance companies, such as lodging, travel, and meals at insurance company-sponsored meetings. Some broker-dealers also receive monetary and other support to conduct client and educational seminars.

Insurance companies recoup the commissions and other compensation they pay through the various fees, charges, and deductions within the annuity contract, including any sales load that may be imposed, but no one charge is specifically earmarked to pay commissions.



State of the Industry

Overview

2022 was a year of records and shifts in annuities markets, and developments that will continue to impact the annuity product mix and the preferences and perceptions of both advisors and consumers. Variable annuity sales continued to hover at historic lows, while fixed and fixed indexed annuities reached new highs. Registered index-linked annuities remained strong, and anecdotal evidence indicates strong interest in in-plan annuities, spurred on by SECURE and SECURE 2.0. Additionally, Contingent Deferred Annuities (CDAs) appear to be back on the radar, though it is not yet clear how extensively these will proliferate.

This chapter focuses on three fundamental areas of importance to IRI members:

- Annuity marketplace data and trends
- Trends in annuity product development
- Operations and technology advances and milestones

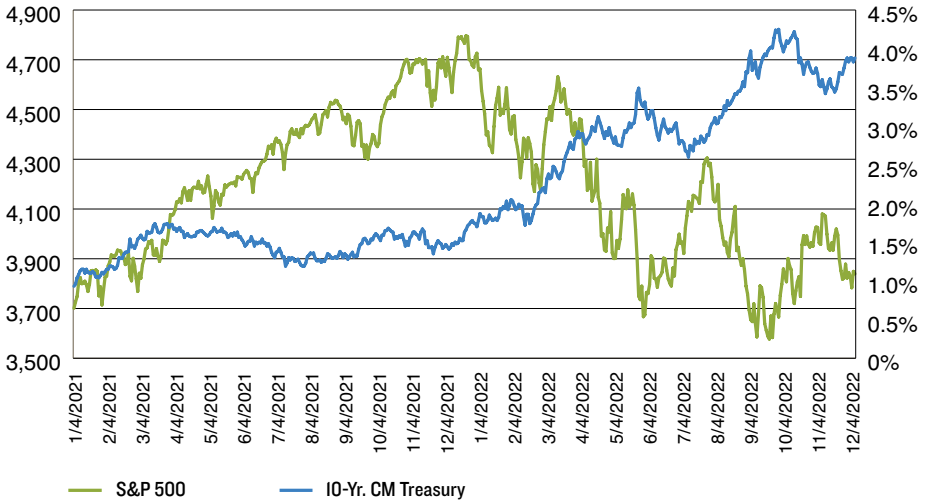
Legislative and advocacy issues and updates are covered in Chapter 14, “*Regulation and Taxation of Annuities*.”

Market Environment

From a financial markets perspective, 2022 was quite the opposite of 2021, and indeed the opposite of most years throughout the previous decade. The post-financial crisis “new normal” of mostly rising equity prices and persistently low interest rates was replaced in 2022 with significantly higher stock market volatility and falling equities prices, and rising interest rates. Figure 5-1 shows a mostly steadily rising stock market in 2021 and low, flat interest rates. In 2022 the stock market rose and fell at a dizzying pace, while the 10-year treasury reached four percent for the first time in years.

Figure 5-1 S&P 500 and 10-Year Constant Maturity Treasury

January 2021 – December 2022



Source: FRED® Economic Data

These market dynamics contributed to a tremendous increase in annuity sales as investors piled into fixed annuities offering higher crediting rates, fixed indexed annuities (FIAs) with higher participation rates and caps, and registered index-linked annuities (RILAs) with more generous participation in their indexes.

Annuity Markets in 2022

Overall sales of annuities set a new record in 2022, rising 28 percent to \$302.1 billion from 2021 sales of sales of \$236.6 billion. Fixed annuities and fixed indexed annuities (FIAs) comprised most of the growth, with sales up 79 percent over 2021. Growth in sales of registered index-linked annuities (RILAs) flattened a bit, growing eight percent year-over-year, while variable annuities offering guaranteed lifetime income benefits (VA-GLIB) fell by 33 percent after rebounding from pandemic lows in 2021. Also notable was the 61 percent increase in income annuity sales as rising rates drove purchases in that category. Figures 5-2 through 5-5 and the accompanying data tables on the following pages show the evolution of annuity sales and market share over the past decade on both a broad product type (fixed versus variable) basis and through the more detailed lens of specific product type.

Figure 5-2a Historic Annuity Sales by Variable Versus Fixed

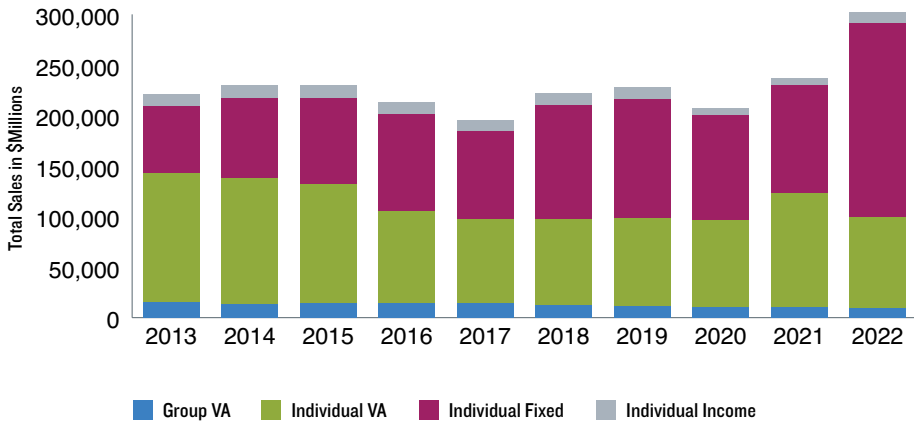


Figure 5-2b Data Table: Historic Annuity Sales in \$Millions

Broad Type	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Group VA	15,190	13,819	14,217	14,544	13,862	12,223	11,549	10,324	10,474	9,585
Individual VA	127,414	124,426	117,457	90,742	83,111	84,826	86,825	85,513	112,018	89,067
Individual Fixed	67,053	78,509	85,867	95,695	87,386	113,611	117,564	104,346	107,105	192,171
Individual Income	11,030	13,021	12,523	12,317	10,459	11,412	11,916	7,399	7,024	11,279
Annual Totals	220,687	229,775	230,064	213,299	194,818	222,071	227,855	207,582	236,621	302,102

Sources: Morningstar, Inc. and Beacon Annuity Solutions

Figure 5-3a Historic Market Share by Variable Versus Fixed

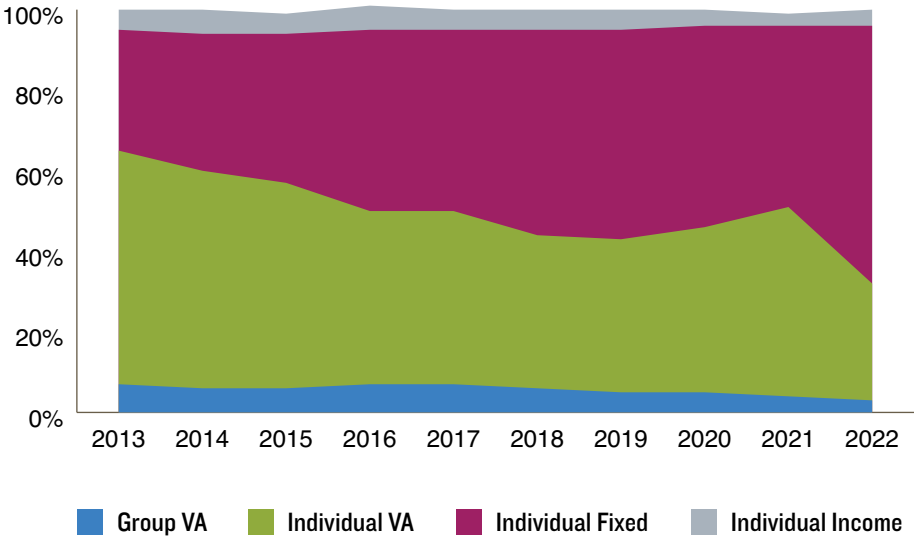


Figure 5-3b Data Table: Historic Annuity Market Share

Product Type	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Group VA	7%	6%	6%	7%	7%	6%	5%	5%	4%	3%
Individual VA	58%	54%	51%	43%	43%	38%	38%	41%	47%	29%
Individual Fixed	30%	34%	37%	45%	45%	51%	52%	50%	45%	64%
Individual Income	5%	6%	5%	6%	5%	5%	5%	4%	3%	4%

Sources: Morningstar, Inc. and Beacon Annuity Solutions

Figure 5-4a Historic Annuity Sales by Product Type

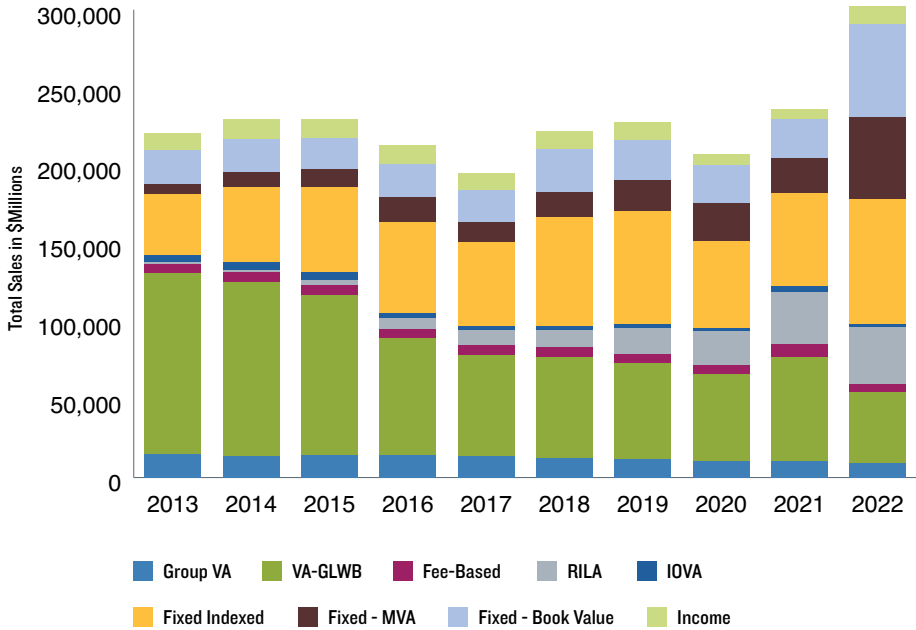


Figure 5-4b Data Table: Historic Annuity Sales in \$Millions

Product Type	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Group VA	15,190	13,819	14,217	14,544	13,862	12,223	11,549	10,324	10,474	9,585
VA-GLWB	115,681	111,551	102,744	74,992	64,292	65,319	61,958	56,246	66,846	44,889
Fee-Based	5,800	5,900	6,000	5,300	6,800	5,920	5,404	5,209	7,923	5,423
RILA	1,783	1,776	3,746	7,382	9,200	11,074	17,292	21,901	33,566	36,353
IOVA	4,151	5,199	4,996	3,067	2,818	2,512	2,171	2,157	3,683	2,401
Fixed Indexed	38,710	47,958	54,603	58,756	54,276	69,882	72,466	55,407	60,249	79,651
Fixed-MVA	6,716	9,778	11,058	16,025	12,371	15,838	19,859	24,467	22,387	52,968
Fixed-Book Value	21,627	20,772	20,206	20,914	20,739	27,890	25,239	24,472	24,469	59,552
Income	11,030	13,021	12,523	12,317	10,459	11,412	11,916	7,399	7,024	11,279
Annual Totals	220,687	229,775	230,064	213,299	194,818	222,071	227,855	207,582	236,621	302,102

Sources: Morningstar, Inc. and Beacon Annuity Solutions

Figure 5-5a Historic Market Share by Product Type

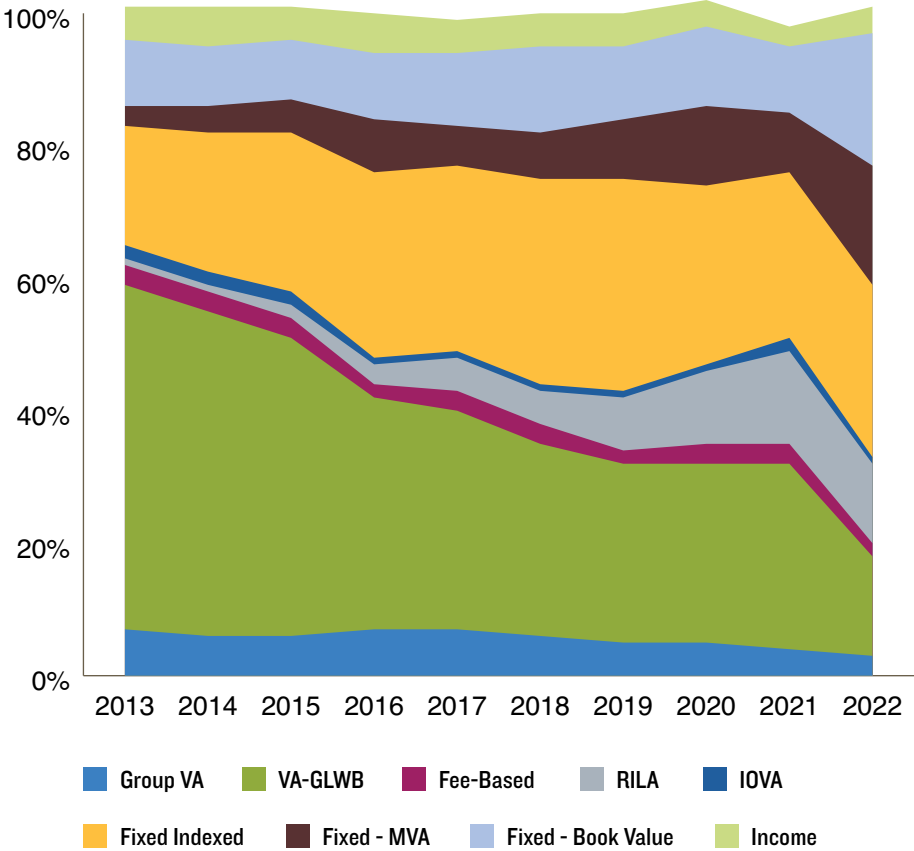


Figure 5-5b Data Table: Historic Annuity Market Share

Product Type	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Group VA	7%	6%	6%	7%	7%	6%	5%	5%	4%	3%
VA-GLWB	52%	49%	45%	35%	33%	29%	27%	27%	28%	15%
Fee-Based	3%	3%	3%	2%	3%	3%	2%	3%	3%	2%
RILA	1%	1%	2%	3%	5%	5%	8%	11%	14%	12%
IOVA	2%	2%	2%	1%	1%	1%	1%	1%	2%	1%
Fixed Indexed	18%	21%	24%	28%	28%	31%	32%	27%	25%	26%
Fixed - MVA	3%	4%	5%	8%	6%	7%	9%	12%	9%	18%
Fixed - Book Value	10%	9%	9%	10%	11%	13%	11%	12%	10%	20%
Income	5%	6%	5%	6%	5%	5%	5%	4%	3%	4%

Sources: Morningstar, Inc. and Beacon Annuity Solutions

As noted at the beginning of this section, sales growth in RILA products flattened somewhat in 2022 as rising rates and significant spreads between crediting rates on bank Certificates of Deposit (CDs) and fixed annuities powered sales of the latter, and volatile equities markets may have dampened RILA sales. However, RILAs continue to grow both in sales and market entrants, setting up for continued growth in 2023 and beyond. Figure 5-6 and the accompanying data table show sales and market share for RILA products and variable annuities ex-RILA for the five-year period ending 12/31/2022. The line shows RILA sales as a percentage of the total variable annuity market.

Figure 5-6a Sales and Market Share Growth of Registered Index-Linked Annuities (RILAs) Versus Total Variable Annuity



Figure 5-6b Data Table: Historic RILA and Variable Annuity ex-RILA Sales in \$Millions

Product Type	2017	2018	2019	2020	2021	2022
RILA	9,200	11,074	17,292	21,901	33,566	36,353
VA ex-RILA	87,773	85,974	81,082	73,936	88,926	62,299
RILA as % of total VA sales	9.5%	11.4%	17.6%	22.9%	27.4%	36.9%

Sources: Morningstar, Inc. and Beacon Annuity Solutions

Alongside the growth in sales of RILA products, assets under management in Defined Outcome subaccounts have also increased substantially in recent quarters. Similar to RILAs, Defined Outcome subaccounts offer exposure to a market index such as the S&P 500®, with caps and buffers that define participation in the growth of the index and limit principal loss. Since Defined Outcome solutions are subaccounts within variable annuities that typically also offer a range of

other asset categories, they are not captured separately in sales data reporting. Figure 5-7 and the accompanying data table show the growth in assets under management in Defined Outcome subaccounts from the second quarter of 2021 through the third quarter of 2022, the latest quarter for which data was available at the time of publication. Note that the AUM totals in Figure 5-7 are not included in the asset reporting that forms the basis of Figure 5-8..

Figure 5-7 Defined Outcome Assets Under Management (AUM) 2Q 2021 - 4Q 2022

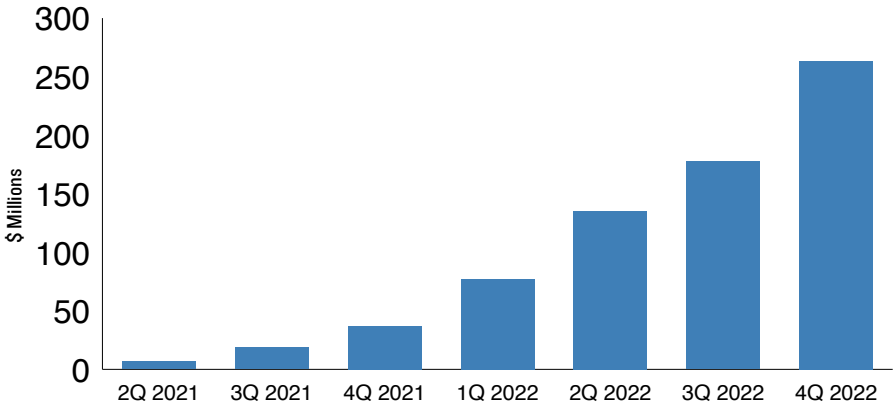


Figure 5-7b Data Table: Historic Defined Outcome AUM in \$Millions

Product Type	2Q 2021	3Q 2021	4Q 2021	1Q 2022	2Q 2022	3Q 2022	4Q 2022
Defined Outcome Subaccounts	6.8	18.6	37.2	77.3	135.4	177.5	263.6

Source: Soleares Research LLC

Assets under management in annuities fell 10.2 percent in 2022, as rising rates hit valuations and a nearly 20 percent drop in the S&P 500 took a toll on all categories. Bond funds were hit particularly hard, with the amount under management cut in half from 2021 due to the combination of negative performance and outflows. Allocation funds, hit by both stock and bond losses, fared the worst, falling 24 percent from year-end 2021 and ending 19% lower than five years ago. Figure 5-8 and the accompanying data table show annuity asset growth over the past decade in the broad categories of variable annuity subaccounts and in fixed annuities. Percentage growth at five-year increments is shown in the data table to illustrate slower growth in variable annuity assets in the second five years despite tremendous market gains. This is due to a number of factors, including lower variable annuity sales volume, increasing net outflows, the shift in assets to allocation funds, and assets accumulating in RILAs and not reflected in overall variable annuity assets under management.

Figure 5-8a 10 Year Chart of Fixed and Variable AUM

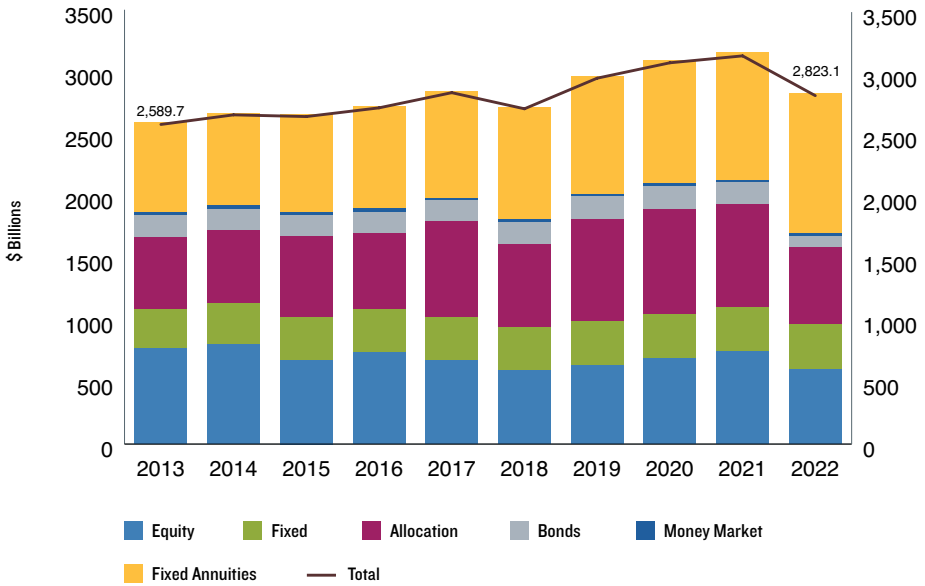


Figure 5-8b Data Table: Historic AUM in \$Billions

Product Type	2013	2014	2015	2016	2017	5-year Growth	2018	2019	2020	2021	2022	5-year Growth
Equity	769.6	799.8	677.4	740.5	676.0	9.0%	590.6	635.3	689.9	746.8	604.3	-11.0%
Fixed	321.8	334.6	344.6	343.7	341.6	8.0%	346.7	352.7	357.3	358.6	360.0	5.0%
Allocation	576.5	586.1	652.9	613.2	775.1	60.0%	676.8	827.8	843.8	823.2	625.1	-19.0%
Bonds	171.6	172.3	166.8	174.7	171.2	-9.0%	173.2	178.7	186.3	178.2	86.3	-50.0%
Money Market	29.0	27.6	29.9	24.6	21.8	-31.0%	27.0	23.5	28.5	23.6	24.7	13.0%
Fixed Annuities	721.2	747.1	782.0	827.5	861.5	25.0%	902.3	946.6	983.5	1,030.9	1,122.7	22.0%
Total	2,589.7	2,667.5	2,653.6	2,724.2	2,847.2	16.8%	2,716.6	2,964.6	3,089.3	3,161.3	2,823.1	10.5%

Sources: Morningstar, Inc., Beacon Annuity Solutions, and LIMRA

Product Development

As in the past several years, spread products (fixed, FIA, and RILA) comprised the bulk of product issuance in 2022. Fixed and FIA accounted for nearly two-thirds of new products, and on the variable side most new products were investment oriented variable annuities (IOVAs). The breakdowns in Figure 5-9 identify a variable annuity with an account value only death benefit, whether as the default or as an option, and no living benefits as an IOVA. While this is an imperfect definition as virtually any variable annuity with optional benefits can be sold as an IOVA, it serves to help categorize activity in variable annuity product development by separating variable annuity products offering lifetime income benefits from those oriented toward tax deferred investing. There was also a slight uptick in new variable annuity products offering GLIBs, with 11 new products in 2022 versus seven the previous year. Figure 5-9 shows annuity issuance by type since 2013. As noted in this chapter’s introduction, a few CDAs were also filed in 2022. Data is not yet available from independent information sources but will be included in future Fact Books if they become a significant part of the overall annuities market.

Figure 5-9a New Annuity Issuance 2013 – 2022

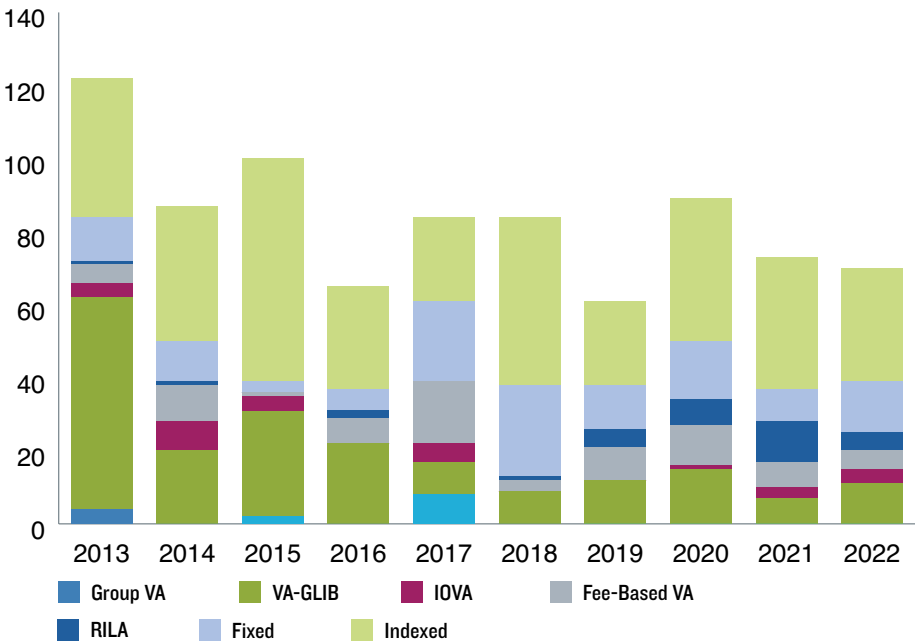


Figure 5-9b Data Table: New Annuity Issuance 2013 – 2022

Product Type	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Group VA	4	0	2	0	8	0	0	0	0	0
VA-GLIB	58	20	29	22	9	9	12	15	7	11
IOVA	4	8	4	0	5	0	0	1	3	4
Fee-Based VA	5	10	1	7	17	3	9	11	7	5
RILA	1	1	0	2	0	1	5	7	11	5
Fixed	12	11	3	6	22	25	12	16	9	14
Indexed	38	37	61	28	23	46	23	39	36	31

Sources: Morningstar, Inc. and Beacon Annuity Solutions

Operations & Technology

Renewed Strategic Vision and Priorities

In early 2023, IRI's reviewed and adjusted its strategic vision and priorities for Operations & Technology. IRI has developed four strategic pillars to drive forward with a purpose:

1. Financial professional experience, encompassing the voice of the entire market
2. Adoption of eSolutions
3. Process and regulation
4. Data enablement

With these four pillars, IRI has honed its strategic vision and priorities with desired outcomes that will remove friction from the process of selling and servicing an annuity.

Creating a Better Financial Professional Experience

The IRI Board of Directors unanimously approved the creation of the Annuity Data Enablement initiative, a new industry-wide senior level task force. The two targeted outcomes are to increase the net new number of financial professionals who sell and manage annuities and are delighted with the results (increasing addressable markets such as independent, advisory, and wealth management); and providing a digital-first model eliminating the critical friction points from the financial professional experience.

Financial Professional eSignature Survey

In support of the mission to improve the financial professional experience, the eSolutions & Adoption Working Group will conduct a member-sponsored survey that will determine core reasons and circumstances causing financial professionals to resist using eSignature for annuity transactions and identify potential improvements to tools and processes that will increase adoption of eSignature.

Bridging the Gap Between Operations & Technology and Compliance

The Secure 2.0 Act marked a historic next step in bolstering retirement security for millions of Americans. IRI's Operations & Technology Process and Regulation Working Group, Framework & Conformity Task Force, and the Secure 2.0 Implementation Task Force are collecting member

input on potential technical needs resulting from Secure 2.0. A full list of provisions and resources is available through IRI's Secure 2.0 Overview. This collaborative effort marks a continuation of the push to bridge the gap between compliance and operations.

Creating Efficiency in the Carrier to Carrier Transfer and Exchange Process

The Framework & Conformity Task Force and the Paperless Transfer/Exchange Task Force are collaborating with the DTCC, ACORD, Ebix, and iPipeline to create a more accurate and efficient environment for processing replacement business. Members are meeting to align data requirements derived from ACORD's 951e Form in DTCC's APP file.

All fields from the 951e Form will be captured in the DTCC App file which will enable the DTCC to digitize carrier-to-carrier digital replacement data. DTCC's proposed carrier-to-carrier replacement solution will leverage this data and relay it through JSON messages between the receiving and ceding carriers. The removal of paper-based exchanges will eliminate not-in-good-order (NIGO) errors that result from missing paperwork, handwritten forms, and delivery black holes.



Annuity Innovations

Equity markets took a bit of a beating in 2022, falling 19.4 percent after tremendous post-pandemic surges, and the overall economic environment remains in a state of flux and is difficult to read, with both positive and negative readings such as strong jobs reports but worrisome inflation trends. Supply chain disruptions, massive increases in government spending and geopolitical issues such as the impact of the war in Ukraine on oil and gas prices have together driven inflation to a 40-year high. Interest rates continued to rise but inflation does not yet appear to be under control, portending further Federal Reserve action. This puts immense pressure on Americans, and especially retirees on fixed incomes who struggle to maintain their standards of living amid rising costs. At the same time, volatility in equities has increased dramatically. Investors seek yield and safety, which has increased interest in annuity products, and particularly those products offering comparatively high yields and/or safety of principal.

The annuity industry has adapted well to these conditions, with two bright spots being the continued development and growth of fixed indexed annuities and registered index-linked annuities (RILAs). In fact, variable annuity sales growth in 2022 continued to be mostly attributable to RILAs, and fixed indexed annuities continued to sell well in the overall annuity landscape. With principal guarantees and limits on upside potential through participation rates, caps, and spreads, the fixed indexed annuity has much more in common with fixed income products than with equity products, and in fact should be viewed as a component of the fixed income portion of an investment portfolio. Importantly, however, especially in a historically low rate environment, it does not carry interest rate risk — the risk of principal loss due to rising rates. The value of a corporate bond, for example, drops when interest rates rise; if interest rates rise suddenly and significantly, depending on the duration of a bond portfolio the effect on market value can be devastating. But, absent a market value adjustment feature, the value of a fixed indexed annuity does not change when interest rates rise; in fact, rising rates tend to increase participation rates, caps, and spreads, thereby increasing the potential for excess interest to be credited based on indexed returns. RILAs can play a similar role for investors, albeit with some risk of principal loss in exchange for a greater degree of upside potential.

Fixed Indexed Annuities

Fixed indexed annuity (FIA) sales represent a substantial portion of the overall fixed annuity business. FIA sales were \$79.7 billion in 2022, a 32 percent increase from 2021 sales of \$60.2 billion. FIAs are designed to guarantee that principal is returned at the end of the surrender charge period while crediting both a guaranteed rate of interest (usually ranging from one to three percent) and potentially additional interest based on the change in the price of one or more broad market indexes such as the S&P 500. In order to secure that guarantee and provide the

opportunity for index-based gains, the insurance company issuing the product allocates a portion of the premium to bonds and a portion to the purchase of options on the index(es). The lower prevailing interest rates, the greater the percentage of premium that must go to the bond piece that secures the principal. This leaves less for the “options budget,” or that piece of the premium that can be used to obtain the market exposure from which the interest crediting is derived. This is the upside potential of fixed indexed annuities and is often expressed in terms of the interest rate cap or spread, which define the potential share of the index return the product will credit. In a year like 2008, a typical fixed indexed annuity may have returned 1 percent versus the -38 percent return of the S&P 500; conversely, in a year like 2019, when the change in the S&P 500 index was 28.9 percent, the return on a fixed indexed product would be greater than the 1 percent guaranteed rate but would be much lower due to the cap and/or participation rate. Many FIAs are “uncapped” in the sense that there is no explicit cap or spread on the return of the index; however, “uncapped” products either use custom indices that blend an index with a volatility control component (e.g., cash) to mute the gains and losses of the index, or there is a requirement to allocate a percentage of premium to a fixed account, so the interest credited will be less than the percentage change in the underlying index(es).

Registered Index-Linked Annuities (RILAs)

RILAs are registered products — some are filed as all other registered variable annuities using SEC Form N-4, while others are filed using SEC Form S-1 or S-3 (simplified SEC registration forms used to make an offering of securities). In either case, RILAs are considered securities as there is a risk of loss of principal, but they resemble both variable and fixed indexed annuities in their characteristics. The Registered Index Linked Annuities (RILA) Act., which was signed into law in December 2022, requires the SEC to modernize its filing requirements to allow RILAs to be filed without the need for extraneous and unnecessary information required on forms that were not specifically designed for them. Sales of RILA sales rose 75% in 2021, reaching \$38.4 billion in sales versus \$22.0 billion in 2020. While still dwarfed by \$61.5 billion in sales of variable annuities with lifetime income benefits in 2021, RILAs are growing rapidly in market share. The impetus for the development of RILAs is the recognition that not all investors need 100 percent principal protection and are willing to trade some downside protection for a higher potential return. The premise behind RILAs is shared risk. Whereas a fixed indexed annuity guarantees full return of principal and a variable annuity (absent a death or living benefit) provides no guarantee of principal, the RILA provides a defined level of protection against investment loss. In exchange for giving up complete protection of principal, the contract holder is afforded greater upside potential than that provided by fixed indexed annuities, though typically less than the potential upside of a variable annuity.

There are two concepts insurance companies employ to share risk in RILAs, the “buffer” approach and the “loss limit,” or “floor” approach, and issuing companies may offer one or the other, or both.

The buffer approach is one in which the issuing company agrees to absorb losses up to a certain limit — (for example the first 10 percent or 20 percent) over a specified time period for a given investment option. In exchange for this buffer, the investor enjoys a higher cap than in a fixed indexed annuity. However, beyond the “buffer” the contract owner is theoretically exposed to unlimited downside risk. The loss limit approach takes the buffer concept and turns it upside down. With the loss limit, the contract owner absorbs losses up to a defined point (for example the first 10 percent or 20 percent) and the issuing company protects the contract owner from losses beyond the limit. Essentially, the contract owner decides between protecting against

market volatility versus protecting against major market corrections. Most recently, Fixed Indexed-Linked Annuities, or FILAs, have come to market that behave more like fixed indexed annuities, offering 100% principal protection.

Defined Outcome Subaccounts

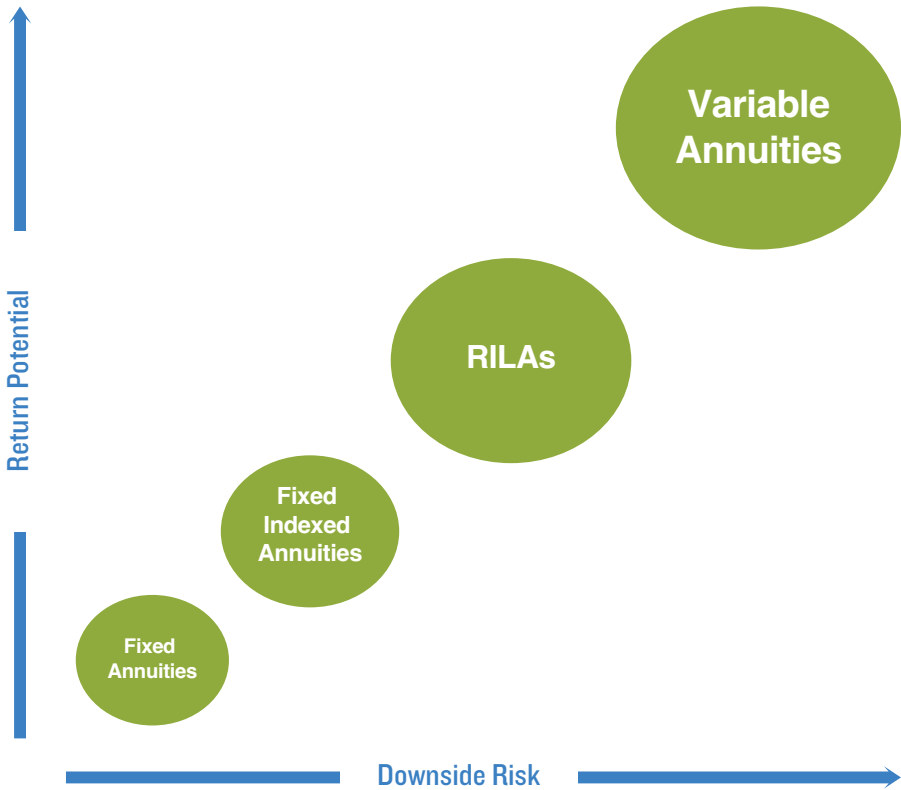
Defined outcome subaccounts are a cousin of RILAs and function a bit more like buffered exchange-traded funds (“buffered ETFs”). Buffered ETFs offer investors the ability to invest in highly liquid ETFs with stated downside and upside limits, allowing for the ability to move in and out of “vintages” as market conditions change. Offering a similar structure within a variable annuity provides investors with a similar structure, but with the added benefit of tax deferred investing, and access to a large menu of traditional subaccounts to permit construction of a complete portfolio. The first defined outcome subaccounts were introduced in late 2021, only offered by a few companies but expected to proliferate rapidly given the interest in protected investing. New in this year’s Fact Book, Figure 5-8 in Chapter 5 shows the growth of assets under management in defined outcome subaccounts.

Volatility Controlled Indexes for Fixed and Variable Annuities

“Volatility overlays,” or the use of options to mitigate market risk, are increasingly used in the asset allocation funds often required when electing lifetime income benefits in variable annuities. Similarly, volatility managed indexes, synthetic indexes which embed options strategies in order to dampen volatility, are increasingly used as the benchmark index in fixed indexed annuities, particularly “uncapped” fixed indexed annuities.

These synthetic indexes are generally created and managed by mixing a base index — such as the S&P 500 — with a cash component. Given that cash has little or no volatility, it offsets the volatility inherent in securities markets. Functionally it is not much different from allocating a portion of premium to cash and a portion to the index crediting “bucket.” The resulting synthetic index is less expensive to hedge, and fewer options purchases are necessary to achieve the target level of exposure. Low rates dramatically increase the proportion of fixed indexed annuity premium that must be allocated to securing the principal guarantees, leaving less for the upside potential offered by the options purchased on the index(es). The result is a very small options budget that then must be stretched for maximum opportunity. Applying that budget to a relatively stable volatility-controlled index means fewer options need to be purchased (as there is inherently less risk), and in some cases upside potential can be uncapped (though a margin, spread, or participation rate may still apply). However, while the index-based return may be uncapped, it is important to bear in mind that the synthetic index has a lower potential return than the “base” index due to the cash component. A risk/reward chart for annuities, where “risk” is defined as the opportunity cost of the tradeoff between guaranteed, but generally lower, investment return and safety of principal, and “reward” is the higher potential returns of the equities markets, would look something like Figure 6-1. On this type of chart, fixed indexed annuities (volatility managed or not) appear northeast of products like CDs and fixed annuities due to the tradeoff between guaranteed and potential return, and RILAs and variable annuities without guarantees are even further northeast due to their potential for at least some degree of principal loss but also higher potential returns.

Figure 6-1 Return Potential versus Downside Risk



Given the black box nature of many of these synthetic risk-controlled indices, they are less actively managed as they are programmed to meet given volatility targets. This programming is the result of a target volatility that is identified in the index objective, and the resulting algorithm that is built to “manage” to that level of target volatility.

Within variable annuity contracts, the volatility control is embedded in the allocation funds used in conjunction with lifetime income benefits. A typical overlay will have anywhere from 5 percent to 30 percent of the fund’s assets allocated to the buying and selling of options on major market indexes. The options are intended to offset losses in the remainder of the portfolio, smoothing out returns. Because volatility is dampened, it is less expensive to hedge the risk that income benefit liabilities will become greater than the assets supporting them. The use of volatility managed funds shifts some of the investment risk back to the contract owner.

“Investment Oriented” Variable Annuities

Variable annuity companies grappling with managing the risk of guarantees have in recent years begun developing and marketing variable annuities with no guarantees, known as “investment oriented” variable annuities, or IOVAs. As the name suggests, these products are focused on the investment options and strategies offered through the product. Alternatives-based and outcome-oriented strategies provide advisor and investor with pre-cooked portfolio approaches designed to achieve certain goals, such as diversification through the use of non-correlated asset classes (i.e., an alternatives based strategy), or perhaps strategies designed to defend against inflation or rising interest rates. Combined with tax deferral, which complements strategies that may involve the use of tax inefficient funds and/or frequent portfolio rebalancing, these products can complement an overall accumulation strategy. IOVA sales are difficult to track as it is not defined as a specific product type in databases that track sales by product; e.g., an IOVA may offer a death or living benefit, but if most sales do not include those benefits this is opaque in the data, as sales are not broken out by benefit elections. Sales of “pure” IOVA products (commission-based products offering goals-based portfolios with no death or living benefits) have fallen to \$2.4 billion from a peak of \$5.1 billion in 2014.

Fee-Based Annuities

Fee-based annuities are less an innovation than a proliferation; in the wake of the efforts by the Department of Labor to enact the ultimately vacated fiduciary rule, annuity issuers brought a flood of new fee-based variable annuities to market. Fee-based variable annuities carry low fees and no surrender charges, and do not pay compensation to the selling advisor or agent. These products were intended for use in so-called “wrap fee” programs, where the investor pays an annualized percentage of assets for the management of the entire portfolio. As the sales and management of annuities generally require the advisor to expend considerably more time and effort than is the case when working with mutual funds, including maintaining additional licensing and continuing education and satisfying more regulatory requirements through additional state forms, many advisors seek to use other financial products and approaches such as bond ladders when they cannot receive higher compensation through commissions. This has constrained growth in annuity sales, especially in third party channels. Annuity commissions are often, and unfairly, the target of criticism in the annuity space, when in fact they are generally only modestly higher than the compensation paid on actively managed mutual funds. Sales of fee-based annuities may grow significantly in the future as a result of accelerated transaction modernization efforts driven by the exigencies of COVID-19, such as universal adoption of e-Signature and e-Delivery.

Deferred Income Annuities

Deferred Income Annuities (DIAs) trace their roots to Longevity Insurance, a product that first appeared in the market in the early 2000s. Longevity Insurance was a restrictive product that was designed to start making payments 5, 10, or even 20+ years after purchase, provided the annuitant was still alive at that point. So, a 65-year-old would purchase the product and payments would commence at age 80 or 85. Because payments would not begin for 20 or 25 years, and then only if the annuitant was alive to receive them, the product was relatively low cost for the amount of payment guaranteed. However, limited or no recourse in the event the

financial needs of the purchaser changed meant the product did not resonate with consumers. The DIA is similar in structure to Longevity Insurance, i.e., lifetime annuity payments commence only if the annuitant reaches an advanced age, but it may offer a death benefit option and/or liquidity provisions such as the flexibility to change the income start date or a one-time cash withdrawal feature. DIAs can work well in a holistic financial plan as they create a finite time period over which other income sources are tapped. Some of the newest DIA products are even participating, that is they can receive dividends from the issuing company, further enhancing their payout potential. In June of 2014 the Department of the Treasury issued a rule for Qualified Longevity Annuity Contracts (QLACs). The rule allowed the greater of 25 percent or \$125,000 of qualified assets (IRA, 401(k), etc.) to be allocated to the purchase of a QLAC and excluded from calculations of Required Minimum Distribution (RMD) amounts; for 2023, as a provisions of SECURE 2.0, the limit has increased to \$200,000 and the 25 percent provision has been dropped. Additionally, the rule permits the reversal of QLAC purchases that inadvertently exceed the investment limit, and the inclusion of a death benefit feature. While the QLAC rule has not led to explosive growth in DIA sales, it has sparked development of products designed to work with the rule. Sales of DIA products have been relatively flat for the past few years after a peak of \$2.6 billion in 2016, to only \$1 billion in 2022, roughly equivalent to the past several years. The new and much higher investment limit and removal of the percentage of qualified assets component should help increase sales in the future.

Contingent Deferred Annuities

A contingent deferred annuity (CDA) is a financial product that provides a stream of income payments to an individual, typically in retirement and in a similar manner as a variable annuity with a guaranteed lifetime withdrawal benefit, but with a unique twist. In a traditional variable annuity, subaccounts are integrated into the annuity product and selected by the owner, or pre-determined by the insurance company to manage the risk of the withdrawal benefit. In a CDA, the portfolio is created by an asset manager in alignment with the risk and cost of the withdrawal benefit, which exists as a contract between the portfolio owner and the insurance company (or companies) providing the benefit. The insurance company will continue payments even if the portfolio is reduced to zero, provided the portfolio allocation is maintained in accordance with the insurance company's parameters and withdrawals do not exceed a prescribed annual amount. CDAs first hit the market in the early to mid-2000s and largely disappeared in the wake of the 2008 financial crisis but have recently started to see interest again as variable annuity sales have fallen and rates have risen (higher rates help support the risk management aspect of CDAs). Sales numbers are not yet available for these products as most are still quite new, but increasing numbers of retirees and near-retirees should support sales growth.



Generating (Almost) Immediate Income

Annuities offer several options for providing immediate (or almost immediate) income when retirement begins or afterward. Fixed immediate income annuities are most frequently utilized for this purpose. These products generate payments of a guaranteed amount on a regular schedule. Variable immediate income annuities also pay out on a regular schedule, but the amounts fluctuate based on the investment performance of underlying subaccounts. Immediate annuity payments may last for a lifetime or a specified duration. Several deferred fixed indexed annuities offer guaranteed lifetime withdrawal benefits (GLWBs) that can be utilized after a brief waiting period. These contracts generally are purchased with a single contribution (not a series), using before- or after-tax funds. Owners of non-qualified deferred annuities also can roll their contracts into an immediate or indexed annuity as a tax-free exchange. Or they may choose to annuitize their contracts, turning the accumulated assets into a stream of income. (If purchased some time ago when interest rates were higher, these contracts may offer guaranteed payouts higher than those attainable with new money.)

All these options can provide lifetime income for one or two people, thereby transferring longevity risk to the insurance company. The company manages this risk by pooling longevity over many individuals. Premiums paid by those who die earlier than expected represent gains for the remaining individuals in the pool and provide a higher yield or credit to survivors than could be achieved through individual investments outside of the pool. Annuities are akin to Social Security in this regard, albeit on a much smaller scale. This survivor or mortality credit increases significantly with age/shorter life expectancy.

Growth Trends

Sales of fixed and variable immediate income annuities and deferred income annuities were above \$10 billion annually from 2013 through 2019, reaching a peak of \$13 billion in 2014. In 2021 sales declined to \$7.0 billion from \$7.4 billion in 2021 and \$11.9 billion in 2019, but with higher rates sales rebounded to \$11.3 billion in 2022. Income annuities of all types have always served a more limited market as the prospect of not having access to the principal investment can be unpalatable to consumers (see Chapter 15: *Data Section* for historic deferred and immediate annuity sales data).

However, future growth is still expected for several reasons in addition to demographic trends. Lifetime payouts are relatively attractive in the current low interest rate environment due to

survivorship credits and will be considerably more attractive when interest rates rise. Income annuities have been endorsed by the U.S. Government General Accountability Office, the federal government has been encouraging employer sponsors of defined contribution retirement savings plans (such as 401(k)s) to offer them as options for retiring employees, and the U.S. Treasury issued rules specific to the use of Qualified Longevity Annuity Contracts (QLACs) in qualified plans in June 2014. The maximum investment, initially set at the greater of 25 percent of the qualified plan (IRA or 401(k)) balance or \$125,000, was raised to \$130,000 in 2018, to \$135,000 in 2020 and maintained at \$135,000 for 2021, then raised again to \$145,000 for 2022. In 2023, as part of the SECURE 2.0 Act, the limit is increased to \$200,000 and the percentage of assets limitation is removed. Sales of QLACs have been anemic, but their popularity may rise with the significant increase in the investment limit.

Finally, carriers are adding liquidity and inflation-protection features to existing products — or introducing new ones with these features — to overcome the objections many advisors and consumers have had to fixed immediate lifetime income annuities in the past. “Participating contracts,” which hold the potential for income to increase through dividend payments from the issuing company, are also relatively new to the market and may help make the product more palatable. In contrast, term-certain (non-lifetime) payments have been declining in popularity. This is probably due to increasing demand for guaranteed lifetime income as well as the low interest rate environment — because the payments are not life-contingent, there are no survivorship credits to boost payouts.

Variable immediate income annuity sales are quite small relative to sales of deferred variable annuities, generally accounting for less than 3 percent of sales. Variable and indexed annuity GLWBs are rarely utilized for immediate income and this is not expected to change much in the future, mainly because relatively few products offer this option and payments are generally smaller than they would be after a longer waiting period.

Though partial annuitization is possible, it is not a popular option and it is still the case that deferred annuities are rarely annuitized. A relatively recent development is the traditional fixed annuity with GLWB, which has seen very little proliferation to date, but which may grow with rising rates. Little in the way of sales or product data is available yet, but this is a product that may do quite well since it is a simpler and more conservative, yet flexible, alternative to variable and fixed indexed annuities with GLWB.

Product Details

Single Premium Immediate Annuities (SPIAs): These immediate income annuity products are purchased with a single premium. Regularly scheduled payments (usually monthly) of a guaranteed amount begin within 12 months. Term-certain or period-certain annuities provide a stream of payments for a specified time (generally five to 30 years). The amount of these payments is a function of the premium size, the specified period, and prevailing interest rates. Lifetime income payment size is a function of all these factors plus the life expectancy of the covered individual (the annuitant). The shorter the life expectancy, the larger the payment. Medically underwritten income annuities take serious illness as well as age into account in calculating the payout amount.

For any given age, the largest lifetime payouts generally are made by a straight or pure life annuity. These payments stop when the individual annuitant dies, and this enables the maximum survivorship credit.

A joint and survivor annuity (often chosen by couples) provides income if either of the two annuitants is living. The payment is usually less than it would be if based on a single life because joint life expectancy is longer. Depending on expected income needs, payments can stay the same or decrease after the first death.

Many are uncomfortable with the possibility that they may not recover some of their premium if they do not live long enough. This is not a concern with term-certain products because payments are not based on the owner's lifetime. There are two basic options to address this issue; both ensure full recovery of premiums (i.e., the amount invested) but will result in smaller payments. Life annuities with a period certain will provide guaranteed payments for the life of the annuitant or a specified period, whichever is longer. Refund annuities provide a lump sum equal to the premium minus payments already received (cash refund) or continue making payments until the total amount received equals the premium (installment refund). In all these cases, payments are made to designated beneficiaries after the annuitant's death.

It was once the case that fixed immediate income annuity payments provided an irrevocable stream of equal payments for the specified period or the annuitant's lifetime. Insurance companies have responded to market preferences for more flexibility in several ways. Liquidity options include an advance of a given percentage or number of payments, which may be very helpful when there are unexpected or one-time expenses. Some carriers will liquidate (commute) the entire annuity, converting the present value of the future stream of payments into a lump sum. Some lifetime income annuities can be structured to provide larger payments early and smaller payments later (perhaps to pay for travel early in retirement), or to provide smaller payments early and larger payments later (to cover increased medical or assisted living costs). These flexible options generally result in smaller payments than those available with a pure life annuity.

Those concerned that inflation may erode the value of their income annuity payments can find contracts that provide pre-determined annual increases in the payment amount. A few carriers offer true inflation protection, but this is rare because inflation is difficult to hedge. When an increase payment option is elected, payments in the early years will usually be smaller than they would be with level payments.

Immediate Variable Annuities (IVAs): Immediate Variable Annuities are fundamentally the same as their fixed cousins in terms of payment options, liquidity features, etc. However, unlike fixed immediate annuities the payment amount can fluctuate based on the value of the investments to which the investment in the contract is allocated. Payments are initially determined using the concept of an "assumed interest rate," or AIR. A higher AIR means a higher initial payment, but also a higher probability that future adjustments will reduce the payment amount. For example, if an AIR of 3 percent is selected and the return on the underlying investments (net of fees) is greater than 3 percent, the payment will rise, but if less than 3 percent the payment will fall. All else equal, a higher AIR means a higher initial payment, but also a greater probability that future adjustments will reduce the payment amount. The payment may adjust every month or may lock in for periods of a year. In any event, when the payment is eligible for adjustment the return of the portfolio of investments is compared to the AIR — if lower, the payment is reduced; if equal, the payment remains the same; and if higher, the payment may increase. There are other variations, of course — the payment amount may lock for longer periods and/or there may be liquidity provisions that allow for periodic windows during which additional income may be taken, but in general the greater the liquidity the smaller the initial payment and subsequent adjustments.

Generating Income Now

Fixed or variable immediate income annuities and some indexed annuity GLWBs can be used to provide income that's needed now. GLWBs on variable annuities may also be purchased to provide income that begins immediately, but as these are more typically used for accumulation followed by future income, they will be covered in detail in Chapter 8: *Planning for Future Income*. Any of these options can be effective for providing enough guaranteed income to cover basic living expenses in combination with other sources of guaranteed lifetime income such as pensions and Social Security; the choice as to which is optimal is an individual one and depends on each consumer's goals, risk tolerance, bequeathing motivations, health status, and other factors.

Term-certain fixed immediate annuities can be used to bridge the gap between actual retirement age and age 70, when Social Security payments are considerably larger. They also can be used as part of a laddering strategy, providing income while other assets grow, or until interest rates are higher.

When a retiree is trying to live on interest from certificates of deposit or bonds, a fixed immediate annuity or indexed annuity GLWB can provide considerably more income and free up assets to be invested more aggressively. Having some assets in higher risk/reward investments generally will help reduce inflation risk.

As part of the provisions of SECURE 2.0, qualified retirement savings are subject to the Required Minimum Distribution (RMD) rule at age 73 for those who turn 72 on or after January 1, 2023. The RMD age will change again in 2033, to age 75. But many retirees want to spend more money when they are younger and still be able to travel or be active in other ways. If some of these funds are used to purchase a SPIA, or a variable or indexed annuity with GLWB, income well in excess of RMDs can be generated when it will contribute most to quality of life. Unneeded income can be invested or can fund life or long-term care insurance.

Considerations

Single Premium Immediate Annuities: These products generally generate the largest guaranteed payments of the three kinds of annuities providing immediate income. They are relatively simple and easy to understand. The cost of liquidity and other options is reflected in quoted payouts, so it is easier to see the tradeoffs and make informed decisions. If purchased with after-tax funds, payouts also receive favorable tax treatment. But there is no possibility of asset growth, as well as less control, flexibility, and liquidity.

Immediate Variable Annuities: Immediate variable annuities offer the potential for income payments to grow as a result of positive market returns, as opposed to fixed immediate annuities where the payment remains the same and its real value is eroded by inflation over time. Due to the natural rate of inflation it is almost a certainty that, over time and barring the onset of a deflationary environment, the purchasing power of payments from a fixed immediate annuity will drop as the real value of the payments becomes lower than the nominal value. Unfortunately it is also far from a certainty that payments from an IVA will increase over time; adverse return sequencing (where negative performance is experienced in early years and positive performance later on) can cause payments to remain flat or drop below the initial level, especially when a high AIR is used to calculate the initial payment (because a higher AIR results in a higher payment, fewer invested dollars are left to grow if returns are negative in early years).

Fixed Indexed Annuity Guaranteed Lifetime Withdrawal Benefits (FIA GLWBs): Owners maintain control of the annuity's cash value, which can be partly or fully liquidated at any time. However, withdrawals will reduce the account value and those larger than the guaranteed amount will reduce the benefit base as well. Surrender charges also may apply. Account value growth is possible, especially during periods of strong returns on the underlying market index(es). GLWB payments may be stopped (e.g., if unneeded and/or to allow the account value to grow) and restarted at the owner's option. On the other hand, guaranteed income payments usually will be smaller, and they will be taxed as ordinary income to the extent they exceed the cost basis of the contract or represent settlement payments made if the account value goes to zero. Fixed indexed annuity crediting methods and GLWBs can also be complex and difficult to explain or understand.



Planning for Future Income

There are several insurance-based products that are structured to provide for a period of accumulation, during which the total amount invested may grow due to investment earnings and/or additional contributions, followed by distributions that can provide lifetime retirement income. Broadly speaking, these products fall into one of the following four categories:

1. Fixed Indexed Annuities with Guaranteed Lifetime Withdrawal Benefits (GLWBs)
2. Fixed Annuities with GLWB
3. Variable Annuities with GLWB or GMIB
4. Deferred Income Annuities (DIA)

Investors planning for retirement use these products to help create predictable future income, i.e., income that will be at least some minimum level when they reach their planned retirement age. While some of the products covered in this chapter may also be employed to generate immediate income, this chapter will focus on product aspects that are geared toward growth over a fixed time period followed by lifetime guaranteed income.

Fixed Annuities with GLWB or GMIB

Any deferred annuity product can be annuitized, but it is also true that a deferred annuity can be exchanged for an immediate annuity when income is desired, allowing the contract owner to shop for the best payout. Therefore, this chapter focuses on generating income from deferred annuities using GLWB features.

Traditional Fixed Annuities with an add-on GLWB currently make up a relatively small percentage of total annuity sales. It may seem surprising that an insurance product with a guaranteed minimum rate of return would also offer an income guarantee, but such a guarantee can be an important part of managing longevity risk in an overall income strategy.

Fixed Indexed Annuities with GLWB

FIA GLWBs provide lifetime guaranteed withdrawals, limited to a maximum annual amount to enable the payment of ongoing income. Withdrawal amounts are calculated as a stated percentage of a shadow account (generally 2 percent to 5 percent, though rates as high as 5 percent are typically available only if withdrawals begin at age 70 or later), known variously as the benefit base, income base, or income account. Often confused with the accumulated/cash value of the fixed indexed annuity, it exists for no other purpose than to provide the basis for guaranteed withdrawals. Initially equal to the amount invested in the contract, the benefit base for most GLWBs grows by a guaranteed annual percentage — often called the rollup rate — during a period of years that ends when guaranteed lifetime withdrawals begin. Of course, there isn't time for the benefit base to grow in this way when lifetime withdrawals are taken soon after the contract is purchased. For this reason, GLWBs designed for almost immediate withdrawals usually offer a larger benefit base bonus and a lower rollup rate. But as mentioned, these very early guaranteed payments are almost always significantly smaller than those available after five or 10 years.

Guaranteed payments covering two lifetimes are generally lower than those which only cover a single lifetime but can incorporate any of these risk management features as well. Some GLWBs will also increase payments by a guaranteed percentage if the owner is unable to perform two or more activities of daily living as a form of long-term care insurance. This may be particularly valuable for those who are unable to obtain affordable underwritten long-term care insurance.

Most GLWBs are available as optional riders for an annual fee. Fees range from 0.35 percent to 1.60 percent, the wide range is a function of varying withdrawal percentages, step-up features, and asset allocation restrictions. In most cases, the annuity's cash value will be reduced in years when the credited interest is less than the fee, but a few contracts guarantee that rider charges will never exceed credited interest. There are some no-fee GLWBs, but credited interest may well be lower (e.g., smaller cap/participation rates) to cover the cost of providing the GLWB.

Variable Annuities with GLWB or GMIB

Variable annuities are often purchased for their guaranteed income features, an evolution from the historic sales drivers of tax deferral and death benefits. In fact, variable annuities with either GLWBs or GMIBs continue to capture more sales than any other VA product category. Additional fees for GLWB features average 1.36 percent, and GMIB fees average 0.94 percent (2022 Morningstar, Inc.). Tax deferral and death benefits are still valuable features, but with the top selling products consistently offering, and being sold with, either GLWB or GMIB benefits and two-thirds of sales reported in qualified plans (i.e., sales where the tax deferral is a function of the plan, not the product), death benefits and tax deferral have become secondary considerations in most sales situations — though some anecdotal evidence is beginning to indicate that death benefits are becoming more important and integral to the sale of variable annuities as the baby boom generation ages.

In the years since the financial crisis of 2008, it has become more common to see features embedded in lifetime withdrawal benefits that serve to help the issuer manage the risk of guaranteeing payments for the contract owner’s lifetime, such as:

- Withdrawal percentages pegged to an external benchmark, such as the 10 Year Constant Maturity Treasury (CMT) Rate.
- Withdrawal percentages based on the age at which withdrawals begin, with percentages significantly lower when payments start at younger ages.
- Withdrawal percentages that are reduced if the account value is completely exhausted and the contract moves into a “settlement phase,” where payments continue to be made while the contract owner(s) are still living, but the account value is zero.

A closer examination of the mechanisms used in these benefits that provide investors with guaranteed income and growth potential will serve to illustrate both their potential importance to retirees needing guaranteed income, and how they are constrained to ensure issuers can manage the considerable risk of guaranteeing income drawn from a portfolio of investments that can potentially experience substantial market losses.

First Things First: How Do GLWB and GMIB Provide Guaranteed Income?

Both the GLWB and GMIB guarantee a minimum payment from a notional amount (the “benefit base”) that is used to calculate either a guaranteed lifetime withdrawal benefit (GLWB) or a life or life contingent annuity payment (GMIB)¹. The benefit base is generally initially equal to the amount invested, but it is not an actual dollar amount; it is a notional amount against which the annual withdrawal percentage or annuity payment factor is applied. The GLWB payment is a withdrawal from the contract value, calculated as a percentage of the benefit base (about 4 percent on average); if the account value is fully depleted, the contract moves into a “settlement phase,” where the insurance company continues to make payments for the life or lives of the contract owner(s). The GMIB payment is calculated as an amount per \$1,000 of benefit base and paid as a life or life contingent annuity. There are some critical differences between these approaches.

Figure 8-1 Differences Between Lifetime Income Benefit Types

Benefit Type	Income Payments by	Income Payments Begin	Cash Value After Income Payments Begin	Income May Increase After Payments Begin	Benefit Base May Increase After Payments Begin
GLWB	Withdrawal	Now or Later	Yes, unless/ until account depletion	Yes	Yes
GMIB	Annuitization	Later	No ²	No ³	No

In a GLWB the investor retains ownership of the contract value, so long as there is contract value, and therefore the potential for positive market performance to increase the contract value and subsequently the benefit base and annual income amount through a “step-up” of the benefit base (see below). With a GMIB the investor no longer owns the contract value when the contract

is annuitized (typically no earlier than after a minimum 10-year waiting period) and its value transferred to the general account of the issuer, but may realize higher income payments due to mortality risk pooling. In a large annuitized group, some percentage of payees is statistically assumed to die earlier, creating a “mortality credit” that is distributed among the surviving payees to support their annuity payments.

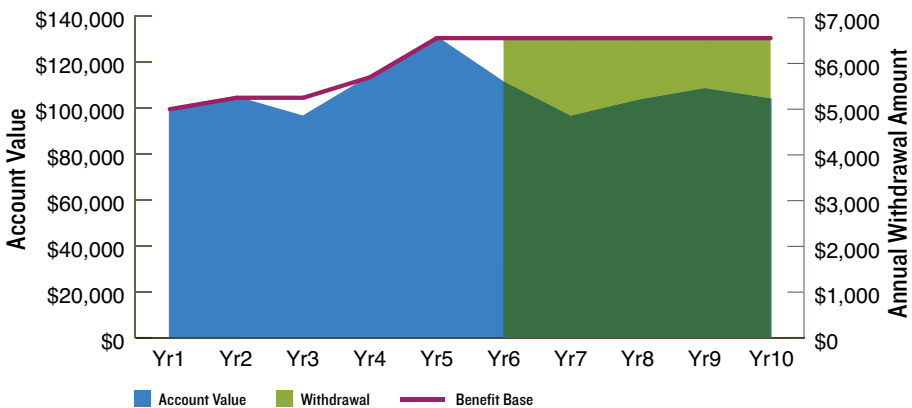
The Mechanics of GLWB

As noted above, the benefit base is generally initially equal to the amount invested, and this is true in both GLWB and GMIB benefits. However, the benefit base may increase before income payments begin in both GLWB and GMIB structures, and after income payments begin with GLWB. Broadly speaking, there are three ways the benefit base may increase after the initial investment: through a step-up feature (also called maximum anniversary value); a deferral bonus (also known as a rising floor); or a combination of the two.

Step-Up Features

So named because it “steps up” the benefit base to a higher value, this feature increases the benefit base to equal the current account value. Put another way, it is an increase in the notional value against which the withdrawal percentage is applied. Such adjustments are usually done annually, but may be more frequent, and most compare the contract anniversary account value to the current benefit base and increase the benefit base if the current account value is higher. Some benefits may use the highest quarterly, monthly, or even daily value reached during the preceding contract year, which affords more opportunity to capture market upturns. Figure 8-2 illustrates a step-up feature, assuming withdrawals begin in the fifth contract year.

Figure 8-2 GLWB with Step-Up



Source: Insured Retirement Institute

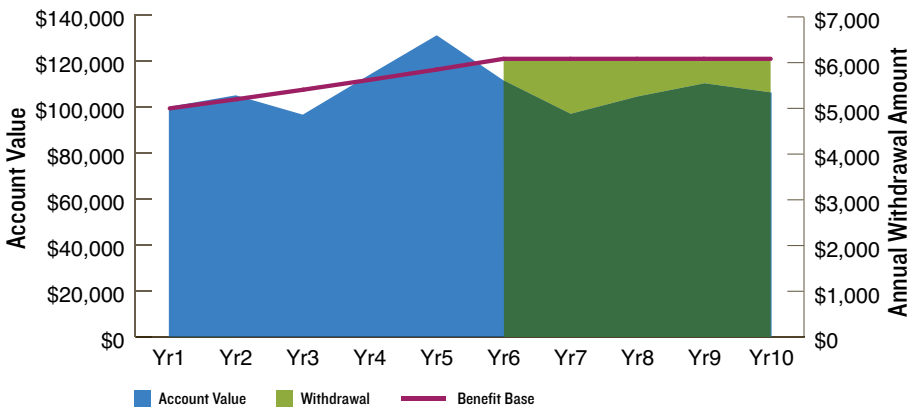
Deferral Bonus

A deferral bonus essentially rewards the contract owner for delaying, or deferring, withdrawals. The basic structure is fairly simple: the notional benefit base increases by a fixed percentage (generally 3 percent to 5 percent in the current market, but has been as high as 7 percent during periods when long-term interest rates are higher) as long as there are no withdrawals from the contract. The details can get a bit intricate, however; below are some of the ways in which deferral bonus features may differ from product to product:

1. The percentage increase may be credited to the benefit base on a simple or compound basis, which can ultimately result in a significant difference in the lifetime withdrawal amount. After 10 years, a 4 percent compounding deferral bonus would result in a 5.7 percent higher guaranteed lifetime withdrawal than one credited on a simple basis.
2. In most contracts taking a withdrawal terminates the bonus credit entirely, but some only suspend the credit in the year a withdrawal is taken.
3. There are typically limits on applying bonus credits to purchase payments made after the initial purchase of a contract. Some may only apply the credit to the benefit base resulting from investments made in the first contract year, while others may apply it to subsequent investments.

Figure 8-3 illustrates a typical compounding deferral bonus assuming withdrawals begin in the fifth contract year.

Figure 8-3 GLWB with Deferral Bonus



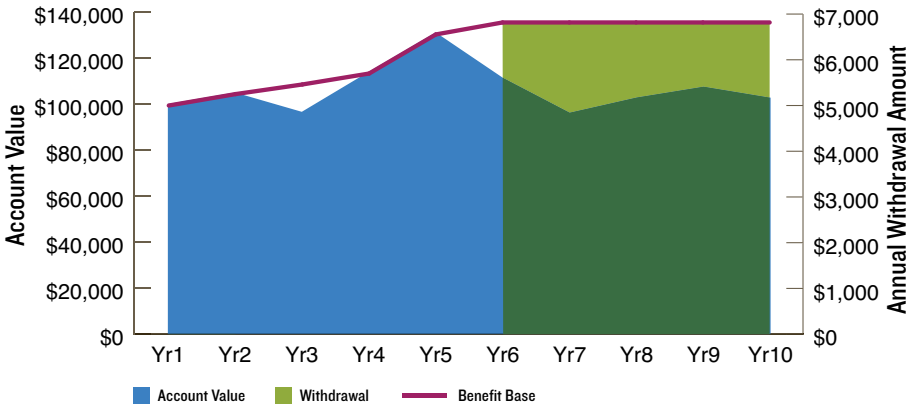
Source: Insured Retirement Institute

Combination of Step-up and Deferral Bonus

The deferral bonus may work in conjunction with a step-up, or it may be independent of it. A deferral bonus that works with a step-up is sometimes referred to as a “stackable” bonus because the bonus credit is calculated against a benefit base that has been stepped up — it “stacks” on top of the stepped-up amount. All else equal, a step-up with a stackable deferral

bonus affords the greatest opportunity to increase the benefit base and therefore the potential income. Figure 8-4 illustrates a compounding deferral bonus that is “stackable” with a step-up, also assuming withdrawals begin after the fifth contract anniversary.

Figure 8-4 GLWB with Step-Up and Stackable Deferral Bonus



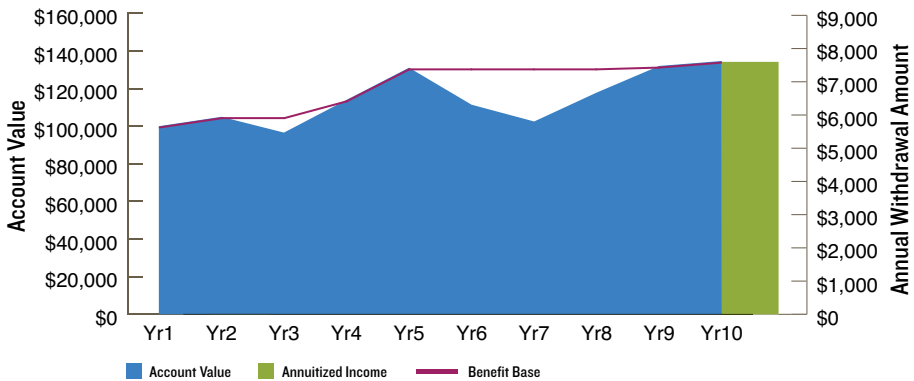
Source: Insured Retirement Institute

A deferral bonus is “non-stackable” when there is a step-up that is independent of the bonus, i.e., the deferral bonus is not credited to the stepped-up benefit base and the withdrawal amount, when set, is calculated against the greater of the benefit base as increased by step-up(s) or the benefit base as increased by the deferral bonus. In other words, the greater of the income amounts shown in Figures 8-2 and 8-3. The combination concept may also include a separate provision that guarantees a benefit base of at least 200 percent of the initial investment after a defined time period. This provision ensures that if the deferral bonus and/or step-up provisions do not result in a benefit base that is at least double the amount invested by the end of the specified contract year, the benefit base will be increased to equal that amount.

The Mechanics of GMIB

In the accumulation phase GLWB and GMIB can be quite similar; both employ the concept of a notional benefit base, the only purpose of which is to calculate an income amount, and both commonly offer opportunities to increase the benefit base through step-ups, deferral bonuses, and features that double the benefit base. It is in the generation of income payments that the two are very different. Whereas income payments from a GLWB are withdrawals from account value and only become payable directly by the insurance company in the event the account value is fully liquidated, income payments under a GMIB require the transfer of the full account value to the insurance company in exchange for life or life contingent annuity payments paid by the insurance company to the annuitant. Figure 8-5 illustrates the production of income under a GMIB from the investor’s point of view.

Figure 8-5 GMIB Annuitized at Year 10



Source: Insured Retirement Institute

When income begins under a GMIB the investor has no further rights to any account or cash value, only to periodic life or life contingent payments. The advantage, or tradeoff, relative to a GLWB is higher income: due to the effect of mortality pooling,⁴ the guaranteed income amount from an annuitized account balance is likely to be significantly higher than the amount guaranteed by a GLWB with a 4 percent withdrawal rate.

GLWB/GMIB Considerations

Both GLWB and GMIB features carry risk for the insurer. The basic concept of insurance is that of pooling risk: a large group of individuals pay an insurer to protect against an event that, while certain (death), rare (tornado damage), or even relatively common (structural damage, such as that caused by storms or fire), will statistically only affect a small number of a very large insured group in any given span of time. In the case of living benefit guarantees such as GLWB and GMIB the relationship is flipped: the insurer protects against a relatively rare event (catastrophic market correction) that impacts an entire large insured group (variable annuity contract owners with GLWB or GMIB) at the same time, while also protecting against longevity risk. Offsetting these risks is complex and involves the use of financial hedging instruments like options and futures to offset losses on the total portfolio of protected assets, as well as pricing structure, risk mitigating benefit features, and hedging instruments built directly into the funds invested in under the guarantees. These can be difficult to understand in terms of their application and impact. Here are a few of the mechanisms and strategies that mitigate the insurer's risk of offering these benefits; the list is by no means exhaustive, but rather is meant to provide an overview of the moving parts of GLWB and GMIB features.

If a withdrawal is taken that is greater than the benefit base times the applicable withdrawal percentage, the benefit base and future guaranteed income is typically reduced. If the contract value is lower than the benefit base the impact can be significant and will vary based on the adjustment method, where the benefit base is either reduced in proportion to the reduction in contract value or simply reset to equal the contract value immediately after the withdrawal. Figure 8-6 shows how each adjustment method impacts the benefit base and guaranteed withdrawal amount.

Figure 8-6 Impact of Benefit Base Reduction Method on Guaranteed Withdrawal Amounts

Value	Benefit Base Reduction Method	
	Pro-Rata	Reset
Pre-Withdrawal Benefit Base	\$100,000	\$100,000
Pre-Withdrawal Contract Value	\$80,000	\$80,000
Guaranteed Withdrawal	\$5,000	\$5,000
Actual Withdrawal	\$6,000	\$6,000
Post-Withdrawal Contract Value	\$74,000	\$74,000
Post-Withdrawal Benefit Base	\$92,500	\$74,000
New Guaranteed Withdrawal	\$4,625	\$3,700
Reduction in Guaranteed Withdrawal	\$(375)	\$(1,300)

Source: Insured Retirement Institute

In some contracts an excess withdrawal can also terminate the life payout component of the GLWB, meaning that after the excess withdrawal the benefit will only make income payments until the benefit base is exhausted. A GLWB investor with a cash need should carefully consider whether withdrawing excess dollars from a GLWB is the best option for meeting that need.

The fees for most GLWB and GMIB features are assessed against the benefit base rather than the account value, so an increase in the benefit base (e.g., due to a step-up) may increase the fee deducted from the account value. Investors must weigh the increase in the withdrawal amount due to the higher benefit base against the fee, which may be a higher percentage of invested assets if the account value has dropped. For example, if a benefit base is locked at \$100,000 and the account value falls to \$80,000, a 1 percent annual fee assessed against the benefit base would reduce the account value by 1.25 percent (ignoring other fees and market performance).

If the fee for the benefit has increased since the annuity was purchased, the increase is generally not applicable to the contract owner until there is a step-up. The investor must weigh whether the step-up is “worth it,” i.e., will the increase in the benefit base produce enough additional income to more than offset the annual increase in the benefit fee? Below is an example where it might not be to the contract owner’s advantage to accept a step-up.

Figure 8-7 Impact of Step-Up on Fees Associated with a Benefit Guarantee Rider

Contract Aspect	Before	After
Contract Value	\$100,000	\$110,000
Benefit Base	\$100,000	\$110,000
Annual Income (@4% of Benefit Base)	\$4,000	\$4,400
Income Increase	N/A	\$400
Fee %	1.00%	1.50%
Annual Fee Amount	\$1,000	\$1,650
Fee Increase	N/A	\$650

Source: Insured Retirement Institute

In benefits where the step-up is automatic the benefit base will generally not increase automatically if the fee has increased since contract issue or since the last step-up to afford the investor an opportunity to determine whether the step-up is large enough to offset the fee increase.

The allocation of the investment to subaccounts in the contract may be limited when a GLWB or GMIB is elected. The investor may be required to invest in a specific fund or among a small group of funds, for example asset allocations funds that limit equity exposure to 60 percent or 70 percent. Or the investor may be required to allocate a minimum of 30 percent of the investment to lower risk funds, limit the allocation to higher risk funds to a maximum of 10 percent, and may freely invest the remaining 60 percent among the remaining funds. In both models, periodic rebalancing (to ensure the portfolio has not skewed toward too much risk) is generally required. Volatility managed funds have also become a common requirement; “vol funds” typically allocate 5 percent to 30 percent of the fund, depending on market conditions, to index options purchases intended to offset the performance of the securities in the rest of the portfolio and reduce the volatility of returns. The theoretical result is returns that are neither as positive nor as negative as they would have been otherwise, reducing the insurers cost to hedge the risk of providing guaranteed lifetime withdrawals from the portfolio held in the VA. In contracts with no investment restrictions or periodic rebalancing requirements the portfolio may be subject to “dynamic rebalancing,” which is complex in terms of calculation but relatively simple in concept: when the contract value drops due to negative market performance, the portfolio is reallocated to more conservative investment options to preserve capital and help limit the issuer’s risk. Failure to adhere to portfolio allocation requirements can cause the benefit to terminate. The investor must weigh flexibility in managing the portfolio and the amount of risk exposure available in the contract against the features and cost of the guarantee.

Income payments under a GMIB merit special mention. Annuity payments are higher than interest payments due to the recovery of principal as part of each payment and the mortality component (those dying early fund larger payments for those living longer). Payments under a GMIB are subject to age setbacks (e.g., payments calculated based on age 55 for a 65-year-old), adjusted mortality tables (more conservative assumptions regarding the number of deaths per year), and lower interest rate assumptions. These adjustments result in a lower payment to the annuitant than an amount equal to the benefit base would produce if invested in a single premium immediate annuity (SPIA). Lower payments help protect the insurer against the risk that the actual account value, which may be lower than the benefit base at the point the contract is annuitized, is not sufficient to produce the income guaranteed by the GMIB. Annuitizing the GMIB may still be advantageous if the contract value is significantly lower than the benefit base, but it is important to understand that in general the benefit base of a GMIB produces a lower annuity payment than an equivalent cash amount invested in a SPIA.

GLWB and GMIB features offered in variable annuities are complex, but so are the risks they protect against. Whether one of these products is appropriate for a given investor is a function of many variables, such as the investor’s retirement income needs and goals, risk tolerance, health status, and bequeathing motives. Understanding the moving parts of an income guarantee, adhering to the requirements for maintaining it, and following a plan for how it will be employed as part of an overall retirement plan are the keys to using it successfully.

Deferred Income Annuities (DIAs)

A DIA is, in theory, an ideal retirement income product; purchased at a deep discount due to the time between purchase and payout, it is a pure risk management product, paying only if one lives to an advanced age. However, this waiting period is also the primary drawback, and difficult selling point, for DIAs because it leads to the notion that one might be “paying for nothing.” However, this is no more accurate than asserting that one “pays for nothing” when purchasing homeowner’s insurance without ever experiencing a fire or natural disaster. The reason homeowner’s insurance is purchased is because most people cannot self-insure the risk of losing a home in a fire or natural disaster — knowing this, banks generally make housing loans contingent upon proof of insurance coverage. Similarly, most individuals cannot self-insure the risk of living to an advanced age (Jeff Bezos, Mark Zuckerberg, Warren Buffet, Bill Gates, etc., being notable exceptions), therefore the reason for purchasing a DIA is to help ensure quality of life and dignity in one’s later years, not necessarily to maximize return on investment. However, the reality of the marketplace is that some form of liquidity is generally needed to help consumers become comfortable with the purchase, so recent innovations include the addition of a death benefit to many DIA products. In fact, the Qualifying Longevity Annuity Contract, or QLAC for short, rules enacted by the U.S. Treasury Department and the significant expansion of investment limits in SECURE 2.0 (see Chapter 7: Generating (Almost) Immediate Income for more details) specifically addresses the permissibility of return of premium death benefits in QLACs, which should eventually help drive higher sales of these products.

A DIA is, effectively, a SPIA with an extended waiting period between purchase and the start of income payments. Conceptually, the DIA allows planning to occur over a finite time horizon, providing a backstop in the event one lives to an advanced age. For example, an individual might use a portion of investable assets to purchase a DIA at age 65, schedule payments to begin at age 85, and use systematic withdrawals, interest, dividends, etc., from the remainder of the portfolio to provide income for the 20 years from age 65 to age 85. If the individual dies prior to age 85 the DIA may pay nothing to heirs, or it may pay a death benefit. Contracts that pay nothing to heirs provide a higher payment, or put another way require less premium to purchase the same payment as one that does provide a death benefit.

Endnotes

¹In its purest form, an annuity payment is a set dollar amount paid at regular intervals (e.g., monthly) for the life of one individual, called the “annuitant.” A life contingent annuity incorporates a minimum number of payments or minimum total cash payout in addition to the guarantee of lifetime payments, for example a “life annuity with 10 year certain” makes payments for a minimum 10 years even if the annuitant dies before that time expires, or continues to make payments for life if the annuitant survives beyond the 10 year certain period. All else equal, life contingent annuity payments are lower than pure life payments due to the guarantee of a minimum number of payments.

²While not properly referred to as “cash value,” some contracts may offer commutation features that permit the present value of some or all future payments to be received in a lump sum. Such features may be needs based, for example requiring a qualifying medical expense or long-term care event and exercising these options will reduce or eliminate future payments.

³CPI-based increases to payments may be available but reduce the amount of the initial payment; market performance-based increases are generally not available.

⁴Mortality pooling refers to the excess income generated in an annuity as a result of the distribution of deaths in a large group. A simple example illustrates this concept quite clearly: imagine four individuals, age 90, decide to each put \$10,000 into a joint account, with 5 percent of the account to be withdrawn each year and shared equally among the survivors. For simplicity assume no taxes and the account earns a net 5 percent each year, which results in each member of the group receiving \$500 at the end of each of the first five years ($\$40,000 \times 5\%/4 = \500). In the sixth year one member of the group dies, and each of the remaining three receives a \$667 payment ($\$40,000 \times 5\%/3 = \667). With no increase in principal the survivors each received a 33 percent “raise” due to mortality pooling. That, in principle, is how annuitization results in a higher payment than systematic withdrawals.



Focus on Accumulation with Income Flexibility

Building Investable Assets and Generating Lifetime Income

One of the core advantages of a variable annuity is the ability to accumulate a nest egg on a tax deferred basis without being subject to the investment limitations applicable to qualified plan savings. Particularly where expenses are relatively low, the ability to defer taxes can contribute meaningfully to growth, and in a properly managed annuity contract the tax advantages of annuitized income can help achieve income results equal or superior to a similar portfolio of mutual funds. Many fee-based and Investment Oriented Variable Annuities (IOVAs) focus on delivering a well-diversified lineup of investment options, including exposure to alternative asset classes such as commodities, and most offer either no insurance benefits or make such benefits optional, resulting in lower expense ratios. In 2021 fee-based and IOVA products represented approximately 11.3 percent of individual variable annuity sales (see Figure 15-7 in Chapter 15 for a complete breakdown of variable annuity sales by product type).

Provided the underlying portfolios are adequately diversified and the investment is made with post-tax dollars, variable annuities are not subject to current income, dividend, or capital gains taxes. If the contract value exceeds the total initial and subsequent contributions when a withdrawal is taken, or the contract is surrendered, the withdrawal is deemed taken as “earnings first” and the earnings portion is subject to ordinary income tax rates. If the contract is non-qualified and annuitized an Exclusion Ratio applies, meaning that a portion of every annuity payment is considered return of principal and not taxed. The principal portion of each payment is calculated based on the life expectancy of the annuitant; this is hypothetically shown in Figure 9-2.

The efficacy of tax deferral in variable annuities centers on the value of deferring taxation relative to the expense of the higher fees one might incur in a variable annuity versus a similar portfolio of mutual funds. Another issue is the more favorable tax treatment of dividends and capital gains in the mutual fund portfolio as compared to the taxation of earnings in a variable annuity, which are always taxed at higher ordinary income rates. A full discussion of the tax implications of variable annuities versus mutual funds is beyond the scope of this book, but two simple “back of the envelope” illustrations, based on reasonable and data-based assumptions, will help clarify the concept.

Tax Deferral and Income Potential

Figures 9-1 and 9-2 compare the hypothetical growth of a mutual fund portfolio to that of a variable annuity, and the potential income that can be generated from each, using the following assumptions:

- The initial after-tax investment is \$100,000 and there are no subsequent investments.
- The contract owner's taxable income is between \$86,351 and \$164,900 (single) or \$172,751 and \$329,850 (married filing jointly) per year.
- The ordinary income tax rate is 24 percent, applicable in 2023 to income above \$178,150 and below \$340,100 for a married couple filing jointly (in the progressive U.S. tax system, tax on ordinary income may be higher or lower than 24 percent at the margin but the rate is kept constant to simplify the analysis and avoid using the top brackets of 32, 35, and 37 percent, which would unrealistically favor the annuity other than for the very wealthy).
- Long term capital gains and qualified dividend income are taxed at 15 percent (rate applicable to married filing jointly income of \$89,251 to \$553,850 per year).
- Gains in the mutual fund portfolio are taxed as 50 percent ordinary income and 50 percent dividend/long-term capital gains based on the weighted average turnover ratio of 24,488 mutual fund share classes in the Morningstar database that meet the criteria of having reported assets under management and being available for new investment.
- The gross annual return for both the variable annuity and the mutual fund portfolio is 8 percent during the accumulation period. When distributions begin the mutual fund portfolio gross return is reduced to 5 percent based on the assumption that the portfolio would be more heavily weighted toward conservative investments with lower expected returns, especially in the current interest rate environment. In the 2021 Fact Book the assumed return during the distribution phase was 3.5 percent due to extremely low interest rates, but with rates having more than doubled since that publication it is appropriate to increase the assumed return. It would not be unfair to assume an even lower return in the mutual fund portfolio both prior to and after the start of income; according to 2019 research by DALBAR, Inc., the average subaccount investor outperformed the average mutual fund investor by 75 basis points or more in each of the prior five years, and outperformed investors overall in each of the prior 10 years. However, in order to illustrate using a conservative view this is not factored into the analysis.
- Total annual expenses for the variable annuity are 0.77 percent. This is the weighted average of the contract and underlying fund expenses (total expenses net of contractual waivers and reimbursements) for contracts that do not offer death or living benefits, which creates an "apples-to-apples" comparison as there are no expenses for lifetime income or death benefits, the values of which are not reflected in the analysis.
- Total annual expenses for the mutual fund portfolio are 0.48 percent, calculated as the weighted average of total fund expenses, less contractual waivers and reimbursements.

Figure 9-1 Comparison of Investment Growth in Variable Annuity Versus Mutual Fund Portfolio

Year	Accumulated Value		Liquidated Value	
	Variable Annuity	Mutual Funds	Variable Annuity	Mutual Funds
1	\$107,235	\$106,053	\$105,498	\$106,053
5	\$141,800	\$134,159	\$131,168	\$134,159
10	\$201,072	\$179,987	\$176,814	\$179,987
15	\$285,119	\$241,470	\$240,690	\$241,470
16	\$305,746	\$256,087	\$256,367	\$256,087
20	\$404,298	\$323,955	\$331,266	\$323,955
25	\$573,293	\$434,616	\$459,703	\$434,616

So, viewed strictly through an accumulation and liquidation lens as in Exhibit 9-1, the additional fees incurred in the average variable annuity result in a fully liquidated portfolio that is worth more than the mutual fund portfolio after 16 years, but a bit less in earlier years. Of course, the lower the fees in the variable annuity the more likely it is that the tax deferred earnings would accumulate to a point where the after-tax value would exceed that of the fund portfolio much earlier, but the differences in the tax treatment of earnings would likely still result in a break-even point several years after the initial investment. And of course, at the highest income and capital gains tax brackets the variable annuity would be farther ahead of the mutual fund portfolio. This analysis also overlooks many factors that could influence individual results, such as the actual turnover ratio of the mutual fund portfolio, which would result in a larger proportion of earnings being taxed as ordinary income, and the extent to which the portfolio is adjusted or rebalanced; buying and selling activity does not, in and of itself, impact the variable annuity from a tax standpoint but may have adverse tax consequences in the mutual fund portfolio. Those details aside, these are representations of retirement income portfolios so it is also important to compare them with a view toward the amount of income that would theoretically be produced, and how long (i.e., to what age) that income would be expected to last. Figure 9-2 compares the two portfolios based on drawing annual income in an amount equal to the annuitized income a 65-year-old male would receive from the VA.

Figure 9-2 Comparison of Income Generated by Variable Annuity Versus Mutual Fund Portfolio

Year	VA Annuity Income		Mutual Fund Portfolio Withdrawals		Annuitization of Mutual Fund Portfolio	
	Variable Annuity Value	After-Tax Annual Annuity Income	Portfolio Value	After-Tax Annual Withdrawals	Portfolio Value	After-Tax Annual Annuity Income
1	\$107,235		\$106,053		\$105,954	
10 (Age 65)	\$201,072		\$179,987		\$179,987	
11	\$0	\$12,427	\$173,657	\$12,427	\$0	\$8,882
15	\$0	\$12,427	\$145,947	\$12,427	\$0	\$8,882
20	\$0	\$12,427	\$105,248	\$12,427	\$0	\$8,882
25	\$0	\$12,427	\$56,585	\$12,427	\$0	\$8,882
30	\$0	\$12,427	\$0	\$10,829	\$0	\$8,882
31	\$0	\$11,227	\$0	\$0	\$0	\$8,882
32	\$0	\$11,227	\$0	\$0	\$0	\$8,882
33	\$0	\$11,227	\$0	\$0	\$0	\$8,882
34	\$0	\$11,227	\$0	\$0	\$0	\$8,882
35	\$0	\$11,227	\$0	\$0	\$0	\$8,882

When the variable annuity contract is annuitized, the exclusion ratio lowers the tax liability on each annuity payment. The exclusion ratio is calculated as the initial investment divided by the total expected payments over the life expectancy of the annuitant. In this example, with annuity payments beginning at age 65, the exclusion ratio is based on a pre-tax payment of \$13,324 per year for 20 years, totaling \$264,480. The exclusion ratio is therefore $\$100,000/\$264,480$, or 37.8 percent excluded from taxation. In the 21st year of income, when the initial investment is recovered, the full amount is taxed, and the after-tax payment drops to \$11,227. The pre-tax annual payment of \$13,224 is approximately 6.6 percent of the ending contract value, and the after-tax payment of \$12,427 is about 6.2 percent of that value. There is no contract value remaining, only the right to receive future payments until death. In the fund portfolio, when withdrawals of the same amount are made, after 19 years only \$10,885 remains, enough to make one partial payment at age 85, at which time the mutual portfolio is fully depleted.

One might assume that the fund portfolio continues to achieve an 8 percent gross annual rate of return, in which case the hypothetical fund portfolio could sustain withdrawals at the level of the annuity income until age 100 or longer. However, this is unlikely to be the case in reality; either immediately upon beginning to use the portfolio for income or as its value dwindles the portfolio is likely to be re-allocated toward more conservative investments with lower risk and lower expected returns, especially as the portfolio value moves closer to zero — at some point it might logically be assumed that the remaining balance would be completely allocated to cash, generating little or no return, in a bid to preserve the remaining principal.

The last part of the example in Figure 9-2 assumes the fund portfolio is annuitized by liquidating the portfolio and using the proceeds to purchase an immediate annuity, either fixed or variable. However, the after-tax annuity payment is 29 percent lower with the same loss of liquidity as when generating annuity income from the variable annuity, and in the event the individual lives

past age 85, when the exclusion ratio is no longer available, the after-tax annuity payment would be 29.3 percent lower in the annuitized mutual fund scenario than in the annuitized deferred VA approach. There are many variables in this analysis that would differ, perhaps substantially, in the “real world,” so these examples are not intended to state definitively that one approach is more favorable than the other for a unique individual. Rather, it is designed to reveal that when assessing whether tax deferral in a variable annuity delivers value to a specific investor it is critical to think about the investor’s need to utilize savings to maximize retirement income versus other goals. Is the end goal to achieve the largest lump sum possible, to structure a personal pension that maximizes income that cannot be outlived, to bequeath a large percentage of wealth to heirs, or a combination of all of these? Accurately assessing the expected, and desired, disposition of investable assets is critical in determining the optimal mix of investment and insurance products for each unique individual.



U.S. Households' Outlook on Retirement Advice

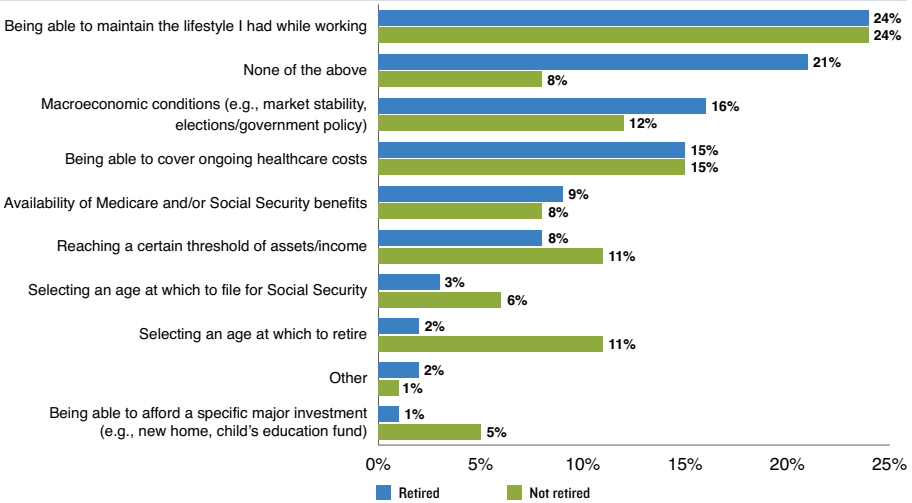
Attitudes and Concerns About Retirement Planning

In this chapter, Americans' views and concerns about various aspects of retirement, financial goals, and retirement investment products are examined, with findings reflecting responses to surveys of U.S. households in 2021, 2022, and 2023. Overall, the picture that emerges is one of significant variance in retirement outlooks, with wealthier households naturally feeling more confident in their ability to enjoy a financially secure retirement. Notably, respondents in or near retirement are primarily concerned with creating secure income from their investments and protecting their current wealth; themes that are repeated in Chapter 11, "*Consumer and Financial Advisor Views on Retirement and Annuities*."

Retirement Concerns and Financial Goals

Americans, retired and working, are primarily concerned with maintaining their lifestyles during retirement. Figure 10-1 shows this as their number one concern, with specific economic and financial concerns chosen less frequently.

Figure 10-1 Retirement Planning Concerns by Retirement Status, 2Q 2021



Sources: MarketCast, Cerulli Associates

Analyst Note: Respondents were asked, "Which of the following events are you most worried about being prepared for as you approach retirement, or if you are already retired, which event was most worrisome to you before retirement?"

Most respondents report feeling somewhat secure about their ability to enjoy a financially secure retirement, as demonstrated in Figure 10-2. More than one-third of respondents aged 70 or older feel very secure, but this drops to less than one in four for those between ages 60 and 70. It is likely there are multiple factors contributing to the difference, including the greater likelihood that those well over age 70 have pension income and have had more time to adjust to managing expenses in retirement.

Figure 10-2 Feelings of Security During Retirement by Age Range, 2022

Feelings About Living Securely During Retirement	Head of Household Age						All Respondents
	<30	30-39	40-49	50-59	60-69	≥70	
I feel very secure	28%	29%	27%	19%	23%	36%	27%
I feel somewhat secure	56%	57%	57%	64%	64%	56%	60%
I don't feel secure	15%	13%	15%	15%	12%	6%	12%
Not sure	2%	1%	1%	2%	1%	1%	1%

Sources: MarketCast, Cerulli Associates

Analyst Note: Respondents were asked, "Thinking about your planning specific to retirement income and expenses, which of the following phrases best describes how you and your family/household feel about living securely during retirement?"

Aggressively growing wealth is far more likely to be an important financial goal for younger Americans, while maintaining a current standard of living and protecting current wealth is more important for older Americans. The findings in Figure 10-3 echo those cited in Chapter 11, "Consumer and Financial Advisor Views on Retirement and Annuities," where both consumers and advisors cite guaranteeing income and protecting wealth as key investing objectives.

Figure 10-3 Investors' Most Important Financial Goals Databank, 2022

Most Important Financial Goal	Head of Household Age						All Respondents
	<30	30-39	40-49	50-59	60-69	≥70	
Assure comfortable standard of living in retirement	20%	26%	34%	50%	54%	43%	43%
Protect current level of wealth	9%	11%	12%	18%	29%	37%	23%
Improve household cash flow	29%	26%	19%	9%	4%	4%	11%
Aggressively grow wealth	20%	17%	14%	10%	4%	2%	9%
Leave an estate for heirs	2%	3%	3%	3%	3%	9%	4%
Better manage market risk	8%	7%	7%	4%	2%	2%	4%
College education financing	6%	4%	6%	4%	0%	0%	3%
Minimize income and capital gains taxes	1%	3%	3%	2%	2%	2%	2%
Charitable giving	3%	2%	1%	1%	1%	1%	1%

Most Important Financial Goal	Household Investable Assets						All Respondents
	\$100K-\$250K	\$250K-\$500K	\$500K-\$1m	\$1m-\$2m	\$2m-\$5m	>\$5m	
Assure comfortable standard of living in retirement	26%	46%	46%	46%	41%	35%	43%
Protect current level of wealth	8%	21%	25%	27%	30%	27%	23%
Improve household cash flow	31%	12%	8%	6%	5%	5%	11%
Aggressively grow wealth	16%	8%	7%	7%	7%	10%	9%
Leave an estate for heirs	3%	4%	5%	4%	5%	6%	4%
Better manage market risk	6%	4%	3%	4%	4%	7%	4%
College education financing	5%	3%	2%	2%	2%	2%	3%
Minimize income and capital gains taxes	2%	2%	2%	3%	3%	4%	2%
Charitable giving	2%	1%	1%	1%	2%	3%	1%

Sources: MarketCast, Cerulli Associates

Investors state they are primarily interested in flexibility (the ability to withdraw additional funds if needed) and having their assets continue to grow while they are taking income. Figure 10-4 puts these desires at the top of investors' wish lists, along with wanting to work with financial advisors. Less than one in four wanted a feature in their retirement income plan to guarantee continued payments even if their assets are depleted, a result that runs contrary to the research covered in Chapter 11, which shows a clear preference for guaranteed lifetime income among American workers. However, as respondents in Figure 10-4 are already retired, it may be that the respondent pool has many investors with sufficient guaranteed income from other sources (pensions, business cash flows, etc.), making an income guarantee in a retirement product relatively less important.

Investors would like to see retirement income products that allow for a degree of liquidity and provide growth of assets even during the income phase. Guaranteed lifetime withdrawal benefits (GLWBs) have the advantage of providing a lifetime income while maintaining an account value that the client can access during emergencies. Moreover, GLWBs allow for asset appreciation

in the income phase, but it may be difficult to realize meaningful gains due to the account value being depleted from withdrawals and fees. There is an opportunity to better educate investors and their advisors on these advantages.

Navigating Retirement Plans

Figure 10-4 Retiree Investors' Desired Features of Retirement Income Plans and Products by Age Range, 2022

Features of Retirement Income Plans/Products	Head of Household Age			All Respondents
	50-59	60-69	≥70	
The ability to withdraw additional funds from my accounts if I need them	52%	59%	61%	59%
Possibility for my assets to grow with the market even after I begin taking money out of my accounts	49%	55%	59%	56%
Having an advisor to work with me to manage my account	46%	47%	48%	47%
The ability to change my investments in the future if I decide I would like something different	37%	41%	43%	42%
Having a comprehensive financial plan which details how I will use my accounts to generate income for retirement	42%	40%	29%	35%
A guarantee so even if my assets run out, I still receive monthly payments	24%	25%	20%	22%
All of my retirement accounts will be located at one financial institution	18%	20%	25%	22%
Using one financial product that could be purchased with my retirement savings assets which would meet all of my retirement spending needs	9%	8%	7%	7%
Help with managing my expenses and help setting up a detailed budget	14%	7%	5%	7%

Sources: MarketCast, Cerulli Associates

Analyst Note: Respondents who indicated that they were retired or semi-retired were asked which of the following are important to them when spending assets from their retirement savings accounts.

Given their age and life cycle, younger cohorts are more interested in growing their assets aggressively, with hopes of eventually leaving a legacy for heirs. When saving and planning for retirement, younger investors can learn from the experiences of their elders. Figure 10-5 is important for investors under 50, and particularly those under 40, who should note the concerning number of households over 60 years of age that wish they had begun saving and planning sooner. Cerulli recommends that providers and advisors look to build real-life cases studies based on older investors' feedback. For example, many Generation X investors are in or approaching their prime earning years but may also be putting off retirement planning.

Figure 10-5 Desired Retirement Planning Changes, 2Q 2021

Desired Retirement Planning Changes	Head of Household Age					All Respondents
	<40	40-49	50-59	60-69	≥70	
Having a better understanding of financial laws and regulations	17%	20%	28%	30%	37%	28%
Having more free time to think about and plan financially	23%	22%	24%	21%	18%	22%
Having more information/interaction from financial professionals (e.g., your advisor, accountant)	25%	21%	18%	10%	6%	15%
Other	19%	18%	16%	13%	9%	14%
Having more information/interaction from financial companies (e.g., the firm where you invest)	1%	4%	8%	17%	22%	12%
Having more information/interaction from financial companies (e.g., the firm where you invest)	16%	14%	5%	9%	8%	10%

Sources: MarketCast, Cerulli Associates

Analyst Note: Participants were asked, "Aside from having more money, if you could improve or change one other aspect about your financial/retirement planning situation, what would it be?"

How and how much to save for retirement is of the most interest to those at younger ages, while many older respondents feel like they have enough information already. Those on the younger side of retirement age tend to be most interested in information around optimizing Social Security, converting savings to income, and managing healthcare costs. Figure 10-6 ranks financial topics in terms of how interest they are to investors in different age ranges.

Figure 10-6 Financial Topics of Interest, 2021

Topic	Age Range						All Respondents
	<30	30-39	40-49	50-59	60-69	≥70	
How much to save for retirement and which accounts to use (e.g., pre-tax or Roth)	45%	45%	47%	37%	17%	10%	32%
Social Security (e.g., how much to expect, how to optimize benefits)	28%	20%	32%	49%	27%	16%	28%
Investment selection (e.g., understanding stocks and bonds, choosing between mutual funds and ETFs)	40%	37%	26%	25%	19%	21%	27%
Tax implications of my financial decisions (e.g., understanding capital gains tax or early 401(k) withdrawals)	29%	24%	29%	27%	22%	23%	25%
How to convert my retirement savings to income (e.g., how much to withdraw from different accounts)	32%	21%	25%	30%	26%	17%	25%
How to manage healthcare costs or plan for long-term care	24%	15%	18%	28%	23%	17%	21%
Ways to guarantee portions of my income in retirement (e.g., how to compare annuities)	23%	18%	30%	22%	16%	11%	19%
I don't need more information, I already have enough	6%	10%	8%	13%	26%	39%	18%
Legacy/estate planning	7%	14%	12%	23%	21%	23%	17%
Prioritizing different financial obligations (e.g., whether to save in an emergency fund or pay off debt)	26%	30%	18%	9%	12%	11%	17%
Household budgeting	26%	33%	14%	8%	7%	9%	15%
How to financially prepare for specific events applicable to my situation (e.g., buying a house, getting married)	34%	27%	22%	8%	6%	1%	15%
Other	0%	0%	0%	0%	1%	1%	0.4%

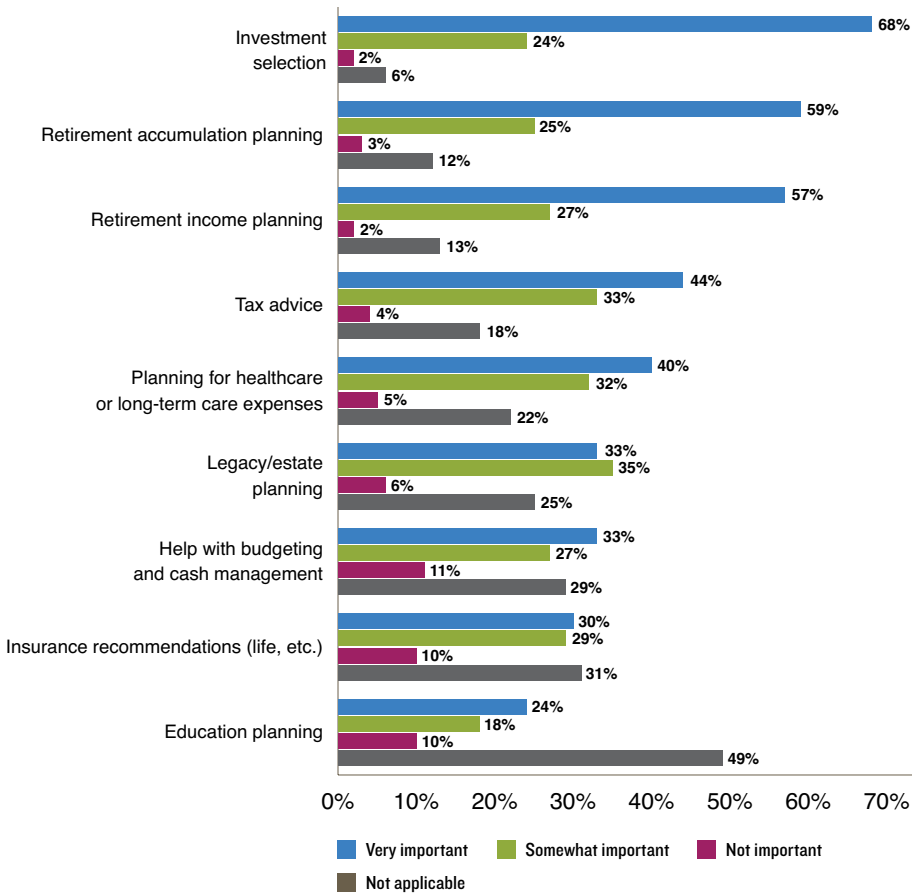
Source: Cerulli Associates

Analyst Note: Respondents were asked, "What financial topics would you like to learn more about, assuming the information came from a trusted source?" Respondents were asked to select up to four options.

Financial Advisor Relationships, Product Preferences and Retirement Income

Of all advisory services, help with investment selection is viewed as most important to households, followed by retirement accumulation strategies and retirement income planning. While financial planning is important, they tend to first engage with an advisor for help with selecting their investments due to the complexity of financial markets and available solutions. Devising a retirement savings strategy is second in importance because so many advisors are focused first on the client’s asset accumulation phase. Retirement income planning ranks third in importance to clients and, in many cases, annuities should play a role in those discussions. Figure 10-7 ranks the services provided by financial advisors in terms of their relative importance.

Figure 10-7 Most Valuable Services Provided by Financial Advisor, 2021



Source: Cerulli Associates
 Analyst Note: This question was asked to respondents who indicated they work with a financial advisor for their retirement assets. Data is sorted by very important.

Nearly half of all investors agree that they need more advice than in the past, particularly younger investors and those with under \$500,000 in investable assets.

Figure 10-8 Respondents That Need More Investment Advice by Age Range and Investable Assets, 2Q 2022

		Head of Household Age						
Needs More Advice	<30	30-39	40-49	50-59	60-69	≥70	All Respondents	
Agree	66%	68%	57%	44%	35%	24%	44%	
Neutral	26%	20%	24%	30%	29%	36%	29%	
Disagree	9%	13%	19%	26%	36%	40%	28%	

		Household Investable Assets						
Needs More Advice	\$100K-\$250K	\$250K-\$500K	\$500K-\$1m	\$1m-\$2m	\$2m-\$5m	>\$5m	All Respondents	
Agree	64%	43%	39%	39%	39%	44%	44%	
Neutral	24%	30%	31%	26%	29%	22%	29%	
Disagree	12%	27%	30%	35%	32%	34%	28%	

Sources: MarketCast, Cerulli Associates

Analyst Note: Respondents were asked how much they agreed or disagreed with the following statement: "I find that I need more financial and investment advice than I have in the past." Percentages may not sum to 100% due to rounding.

While familiarity with annuities is understandably greater at older ages, it is a bit disheartening to see so few respondents of any age in Figure 10-9 agreeing that annuities are a good tool for generating income and diversifying assets. However, there are also very few who assert that they do not need an annuity, or that the product is inherently too expensive or too complex, indicating more of a need to educate investors than to alter negative opinions.

Figure 10-9 Investors' Opinion of Annuities by Age Range and Investable Assets, 2022

Opinion	Head of Household Age						All Respondents
	<30	30-39	40-49	50-59	60-69	≥70	
I am not familiar with annuities	39%	33%	30%	26%	17%	14%	23%
Annuities are a good way to generate income	19%	19%	22%	21%	23%	22%	21%
Annuities are a good way to diversify my assets	20%	20%	25%	19%	20%	21%	21%
Annuities are a good way to protect my assets	23%	20%	22%	17%	19%	24%	20%
Based on my financial situation, I do not think I need an annuity	18%	12%	12%	15%	20%	24%	18%
I have seen much negative information about annuities	16%	6%	10%	15%	20%	20%	15%
Annuities are too confusing/complex	7%	14%	15%	12%	10%	7%	11%
Annuities are too expensive	4%	9%	9%	10%	12%	11%	10%
I plan to purchase an annuity in the next year	8%	13%	11%	5%	2%	1%	6%
None of the above	4%	9%	7%	11%	12%	13%	11%

Opinion	Household Investable Assets						All Respondents
	\$100K-\$250K	\$250K-\$500K	\$500K-\$1m	\$1m-\$2m	\$2m-\$5m	>\$5m	
I am not familiar with annuities	45%	26%	20%	12%	12%	17%	23%
Annuities are a good way to generate income	12%	20%	24%	24%	27%	17%	21%
Annuities are a good way to diversify my assets	15%	17%	22%	29%	26%	16%	21%
Annuities are a good way to protect my assets	13%	19%	23%	24%	23%	18%	20%
Based on my financial situation, I do not think I need an annuity	11%	15%	19%	20%	26%	22%	18%
I have seen much negative information about annuities	5%	14%	16%	17%	22%	22%	15%
Annuities are too confusing/complex	11%	13%	10%	8%	11%	8%	11%
Annuities are too expensive	5%	9%	10%	13%	14%	22%	10%
I plan to purchase an annuity in the next year	5%	6%	6%	5%	7%	7%	6%
None of the above	9%	11%	9%	13%	11%	12%	11%

Sources: MarketCast, Cerulli Associates

Analyst Note: Respondents were permitted to select more than one response.

Older retirees are more likely to cite Social Security payments as a primary source of income, but as one would expect those at the higher end of the wealth spectrum are more likely to get most of their income from stock and bond investments. Annuities are cited less frequently than any other form of savings or investment but are more commonly used for income than real estate or some type of employment in the \$500k to \$5m range of wealth. Figure 10-10 shows primary sources of retirement income for various age and income cohorts.

Figure 10-10 Primary Source of Retirement Income by Age Range and Investable Assets, 2Q 2023

Primary Source of Retirement Income	Head of Household Age			All Retired Respondents
	50-59	60-69	≥70	
Social security payments	13%	34%	45%	38%
Savings from 401(k), company pension plan or other employer-sponsored savings account	26%	22%	15%	19%
Other	25%	14%	12%	14%
Savings in Individual Retirement Accounts	14%	13%	10%	11%
Income from stocks and bonds (excluding assets held in personal trusts)	10%	8%	8%	8%
Income from annuities	5%	5%	5%	5%
Income from real estate investments	3%	2%	2%	2%
Income from part- or full-time employment	3%	2%	2%	2%
Income from personal trust(s)	1%	1%	1%	1%
Income from family business	1%	0%	0%	0%

Primary Source of Retirement Income	Household Investable Assets						All Respondents
	\$100K-\$250K	\$250K-\$500K	\$500K-\$1m	\$1m-\$2m	\$2m-\$5m	>\$5m	
Social security payments	51%	39%	28%	19%	8%	38%	43%
Savings from 401(k), company pension plan or other employer-sponsored savings account	17%	22%	21%	17%	10%	19%	23%
Other	14%	15%	13%	13%	14%	14%	11%
Savings in Individual Retirement Accounts	7%	11%	18%	16%	6%	11%	9%
Income from stocks and bonds (excluding assets held in personal trusts)	3%	3%	9%	24%	46%	8%	4%
Income from annuities	4%	6%	6%	6%	2%	5%	4%
Income from real estate investments	2%	1%	3%	2%	3%	2%	3%
Income from part- or full-time employment	2%	2%	1%	1%	5%	2%	2%
Income from personal trust(s)	1%	0%	2%	2%	5%	1%	1%
Income from family business	0%	1%	1%	0%	2%	0%	1%

Sources: MarketCast, Cerulli Associates

Generally, as age increases, a higher percentage of assets are held in designated retirement accounts. Conversely, as wealth increases the percentage tends to drop, in part due to retirement account contribution limits. Figure 10-11 provides some context for how investor assets are held in advisory accounts.

Figure 10-11 Percentage of Advisor-Held Assets in Designated Retirement Accounts by Age Range and Investable Assets, 2022

Percentage of Investments With Advisor in Designated Retirement Accounts	Head of Household Age						All Respondents
	<30	30-39	40-49	50-59	60-69	≥70	
0.0%	22%	15%	13%	17%	19%	21%	18%
1% to less than 25%	17%	18%	15%	12%	11%	12%	13%
25% to 49%	20%	24%	23%	17%	14%	15%	18%
50% to 74%	16%	18%	20%	16%	16%	15%	17%
75% to 89%	6%	9%	11%	13%	14%	11%	12%
90% to 99%	4%	4%	5%	6%	8%	7%	6%
100%	15%	12%	14%	19%	19%	18%	17%
Average Percentage of Assets	43%	47%	51%	54%	55%	52%	52%

Percentage of Investments With Advisor in Designated Retirement Accounts	Household Investable Assets						All Respondents
	\$100K-\$250K	\$250K-\$500K	\$500K-\$1m	\$1m-\$2m	\$2m-\$5m	>\$5m	
None	20%	19%	17%	15%	15%	15%	18%
1% to less than 25%	21%	12%	11%	11%	14%	20%	13%
25% to 49%	18%	16%	18%	18%	21%	25%	18%
50% to 74%	14%	15%	17%	20%	22%	22%	17%
75% to 89%	7%	11%	13%	15%	14%	12%	12%
90% to 99%	4%	6%	7%	8%	6%	3%	6%
100%	18%	21%	17%	13%	9%	4%	17%
Average Percentage of Assets	45%	53%	54%	54%	50%	42%	52%

Sources: MarketCast, Cerulli Assoc

Knowing the retirement aspirations and concerns of investors highlights a continued need—the industry must clearly and consistently promote the potential value of annuity solutions. Despite significant education campaigns across the industry, most investors remain unfamiliar with annuities as tools for generating income and diversifying and protecting wealth. Moreover, despite the industry’s historical tendency to place its greatest focus and emphasis (e.g., marketing and product development) on older investors, they are among the most likely to provide negative feedback regarding annuities. While there is a need to reverse this sentiment via more sound education and client engagement, it highlights the opportunity represented by younger investors who have yet to form pessimistic viewpoints.

Research Background: U.S. Annuity Markets 2022 and U.S. Retail Investor Advice Relationships 2022

The Cerulli Report—U.S. Annuity Markets 2022: Acclimating to Industry Trends and Changing Demand is an outcome of ongoing research and analysis of the retail annuity marketplaces by Cerulli Associates. The report focuses on key elements impacting the annuity marketplace, including distribution strategies, product development, advisor and intermediary channel trends, buying behaviors, and asset management opportunities. This report leverages Cerulli's continuous analysis of variable and fixed annuities, including fixed-indexed, fee-based, and registered index-linked annuities, as well as the subadvisory marketplace. Exhibits highlight key data and commentary, including the important tactical ramifications for insurers, asset managers, and wealth managers servicing the annuity market. The report is designed as a business planning tool, and additional support leveraging this data is available.

U.S. Retail Investor Advice Relationships 2022: Rethinking the Advice Continuum is part of an annual series of investor-focused reports, which is the outcome of a partnership between Cerulli Associates and MarketCast (formerly Phoenix Marketing International). It covers the provider-client relationship from end to end, starting with client acquisition, progressing through advice delivery, investment management, and pricing and client retention strategies, among other topics. In addition, the report includes a sizing of the retail investor marketplace by channel and product to help firms identify client acquisition and product distribution opportunities. The report is designed as a business planning tool, and additional support leveraging this data—in the form of customized workshops and other presentations—is available.



Consumer and Financial Advisor Views on Retirement and Annuities

Chapter 10 examined the outlook of U.S. households on retirement advice. This chapter presents findings from recent IRI research that support the findings and conclusions in Chapter 10, focusing on the retirement readiness, financial goals, and investment preferences of retirees and near-retirees, and the views of financial advisors as to their clients' financial health and preferences regarding investing and investment products, especially annuities.

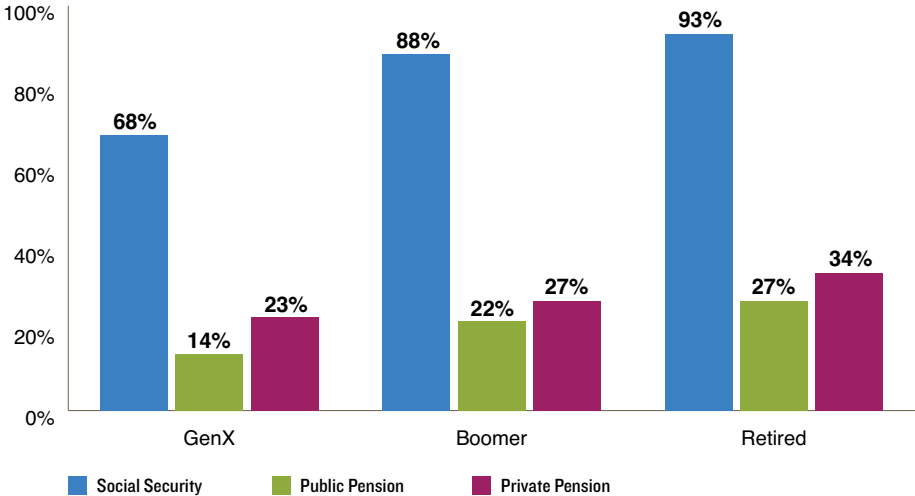
The Consumer View

Americans in Generation X (GenX), born between 1965 and 1980, currently number approximately 65 million. The larger Baby Boomer generation, born between 1946 and 1964, number approximately 71 million in the United States. The current generation of Americans receiving Social Security retirement benefits, a mix of Silent Generation at the oldest and Boomers at the youngest, are about 49 million strong. These three groups are quite different in some aspects of their expectations for retirement and in their preferences for investment vehicles.¹

The average retirement savings of workers in their peak earning years (Generation X) and near retirement (working Boomers) are insufficient to support income expectations, save for the relative few who anticipate receiving income from a public or private pension. It is also unlikely that pension income will be as common as the survey indicates, as defined contribution plans are often misunderstood to be equivalent to pensions. While only 16 percent of private sector workers have access to a defined benefit (pension) plan, 27 percent of baby boomers and 23 percent of GenXers believe they will receive pension income.²

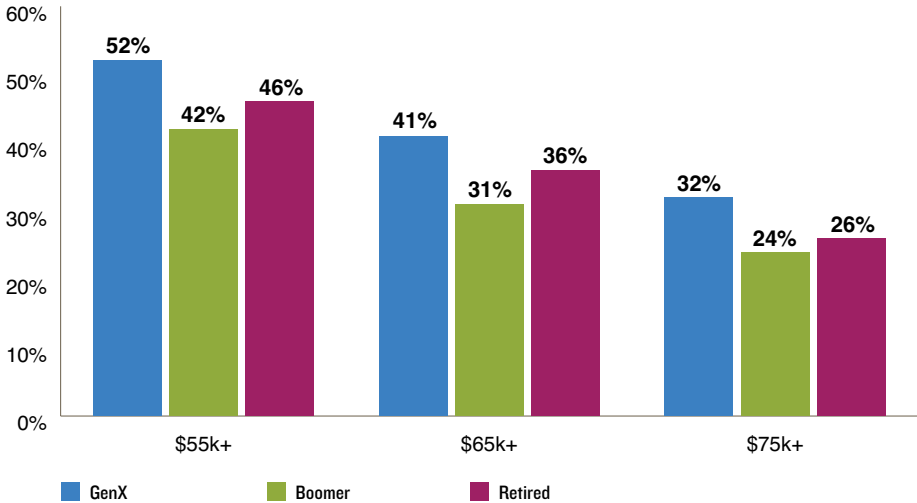
GenXers are significantly less likely to expect retirement income from a public or private pension than either Boomers or current retirees, and almost one-third of GenX does not expect to receive Social Security in retirement. Figure 11-1 shows how generational cohorts differ in terms of their expected income sources. This no doubt reflects the fact that the Social Security trust fund is expected to be exhausted in 2034, only two years after the oldest GenXers reach the full retirement age of 67. While current projections show Social Security can remain solvent, paying 76 percent of benefits after 2034, many GenXers appear to believe payments will simply cease.

Figure 11-1 Expected Sources of Retirement Income



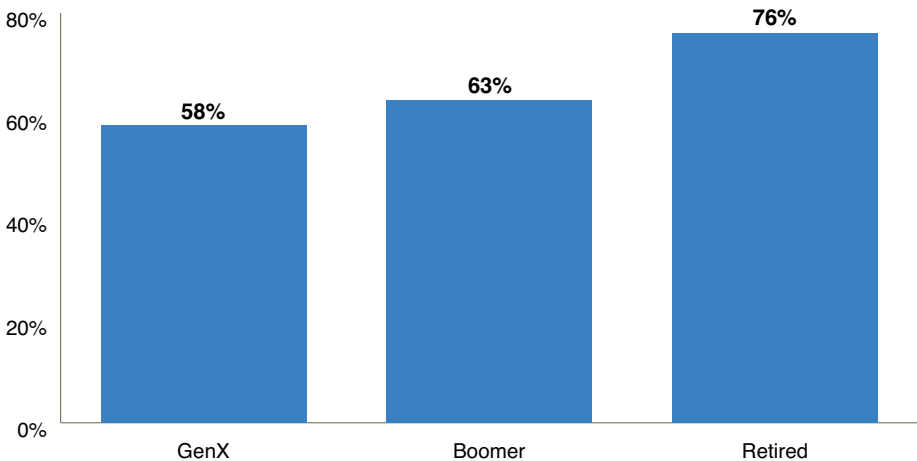
At the same time, while GenX is less confident than older generations in traditional sources of retirement income such as Social Security and pensions, they have higher expectations for their income needs. A greater number of GenXers believe they will need more income than either Boomers or current retirees in today's dollars. The implication is that many GenXers believe they need to save aggressively to have sufficient retirement savings to create the income they do not believe will come from Social Security and pensions. Figure 11-2 shows how much annual income these different generations believe they will need in retirement.

Figure 11-2 Expected Retirement Income Need



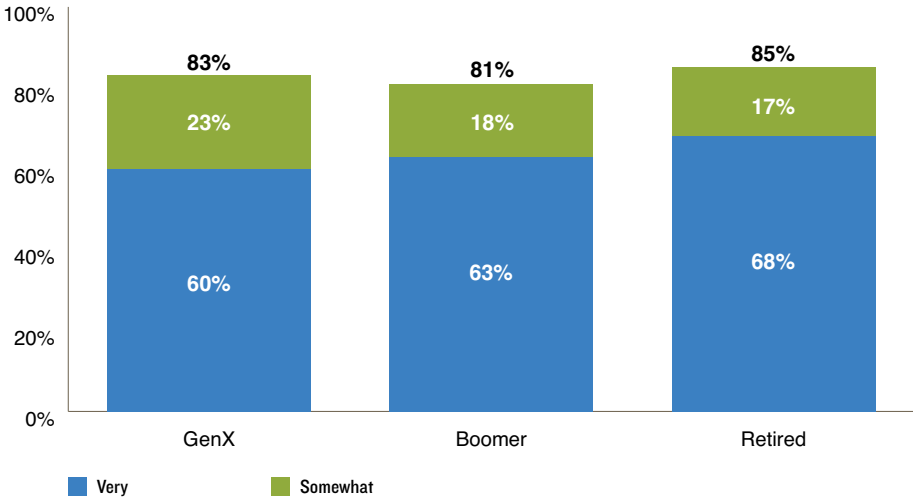
Many Americans, from almost six in 10 GenXers to over three-quarters of retirees, expect that their retirement income will be sufficient to pay for their basic living expenses (food, clothing, shelter, and medical costs), as well as leisure activities and travel. Figure 11-3 shows younger Americans less confident in terms of their lifestyles expectations. Perhaps this is why their stated income needs are much higher than what Social Security will provide. With only a relative few expecting income from a pension, especially among the younger generations, personal savings will have to make up the gap for a substantial number of retirees.

Figure 11-3 Expect to Cover Expenses and Travel/Leisure



Older workers and retirees alike overwhelmingly want retirement income other than Social Security to also be guaranteed for life. This is the “annuity paradox,” where studies repeatedly show that consumers have very high levels of interest in guaranteed lifetime income but relatively low levels of interest in purchasing annuities. Figure 11-4 shows that the majority in all generations in or near retirement believe it is very important for income from investments to be guaranteed for life in order to ensure they can continue to realize income that will match their expense expectations throughout retirement. Financial advisors report this about their clients as well, as the rest of this chapter highlights.

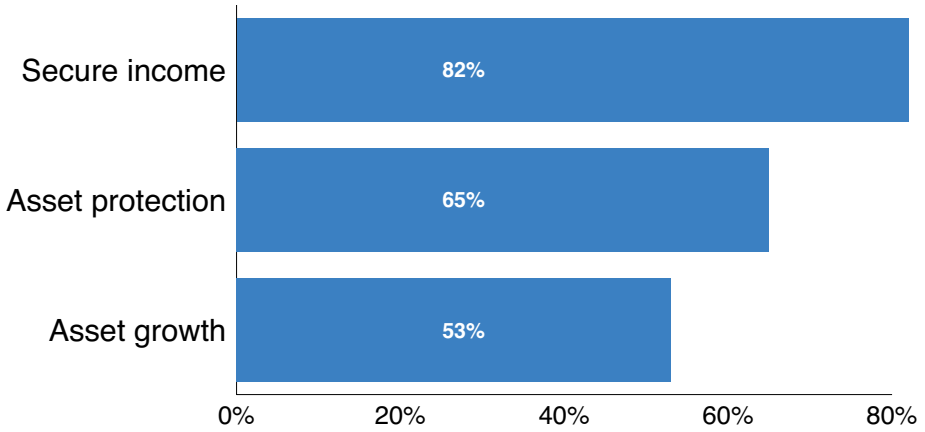
Figure 11-4 Importance of Income Sources Being Guaranteed for Life



The Financial Advisor View

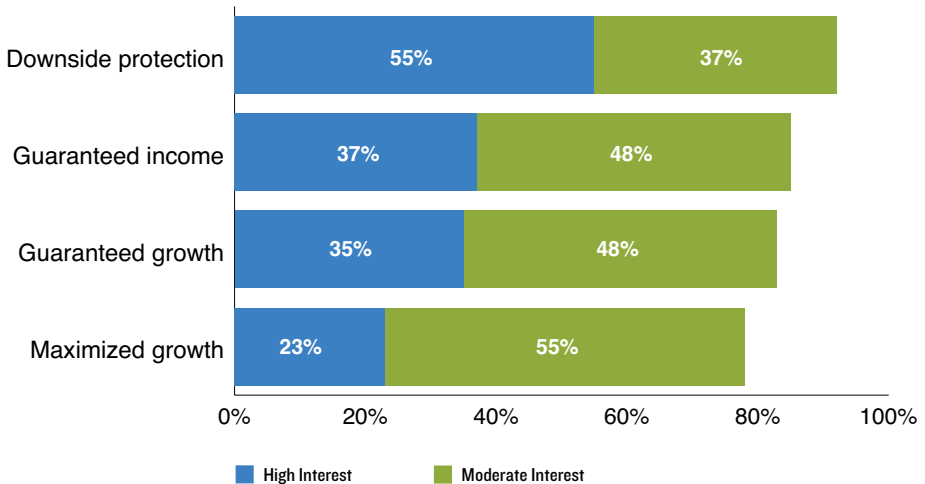
All types of annuities can provide guaranteed lifetime retirement income, and many can provide full or partial protection from losses due to market downturns. Figure 11-5 reflects financial advisors’ views regarding their clients’ top financial goals, showing that securing income and protecting assets are significantly more important to clients than investment growth.

Figure 11-5 Top Client Financial Goals



Advisors can use annuities to protect assets and generate guaranteed lifetime income from client portfolios, the two aspects of investment products in Figure 11-6 in which advisors who use annuities say their clients have the highest interest. Annuities that provide both market growth and downside protection may have lower upside potential than investment products without such protection, but maximizing growth is the lowest priority for many clients. Even guaranteed growth, despite having more client interest than maximized growth, takes a back seat to protection and income. Annuities can essentially meet clients at the intersection of protecting what they have and providing growth to address their top financial concerns.

Figure 11-6 Client Interest in Investment Product Features



The findings in this chapter are excerpted from the following reports:

1. “July 2023 IRI Research Brief: Evolving Retirement Expectations Among American Workers and Retirees,” (Insured Retirement Institute, July 2023)
2. “September 2023 IRI Research Brief: Advisor Views on Client Goals, Concerns and Preferences,” (Insured Retirement Institute, September 2023)

¹U.S. Census Bureau

²U.S. Bureau of Labor Statistics



Tax-Qualified Retirement Plans

The role of Social Security and employer-provided defined benefit pension plans in providing a secure retirement income is diminishing for many Americans. The importance of self-directed plans such as 401(k)s and 403(b)s is increasing. Yet despite the significance of this shift, many people still do not understand the types of retirement plans available to them and the options they have. This understanding is essential if individuals are going to be able to effectively plan for their own retirement and make appropriate decisions about managing their income once they retire.

In recognition of the need to encourage individuals to save for retirement, the U.S. Government has codified preferential tax treatment for assets held in several types of retirement plans. These “tax-qualified” plans must meet the specific requirements of the Internal Revenue Code, as well as the requirements of various other laws that have been enacted over the years, such as the Employee Retirement Income Security Act of 1974 (ERISA).

Some of the most common types of tax-qualified retirement plans are described below.

Personal Retirement Savings Plans

Individual Retirement Arrangements (IRAs)

An individual retirement arrangement (also known as an individual retirement account or individual retirement annuity) is a tax-deferred retirement plan, typically set up through a bank, mutual fund company, or brokerage firm (in the case of an account), or a life insurance company (in the case of an annuity). An individual can contribute money earned each year to an IRA, subject to certain limits. In 2023, individuals younger than age 50 generally can contribute up to \$6,500, while individuals age 50 and older generally can contribute up to \$7,500. Earnings on contributions (investments) grow tax deferred. Amounts withdrawn before age 59½ generally incur a 10 percent tax penalty, subject to certain exceptions.

Amounts generally can be transferred or “rolled over” between IRAs tax-free, subject to certain rules and restrictions. Likewise, amounts in other types of qualified retirement plans (such as 401(k) plans and defined benefit plans) generally can be rolled over tax-free to an IRA. In that regard, it is common for employees to roll over their retirement plan assets to an IRA when they switch jobs or retire.

The most common types of IRAs are Traditional IRAs and Roth IRAs, both of which are discussed in this chapter. Other types include SEPs (simplified retirement plans for self-employed individuals or small business owners) and SIMPLEs (flexible, easy-to-administer retirement plans for businesses with 100 or fewer employees).

- **Traditional IRA:** Anyone with earned income can make contributions to a Traditional IRA. However, only those who do not participate in an employer-sponsored retirement plan, or who participate in such a plan but meet certain income limits, can make tax-deductible contributions. Distributions of tax-deductible contributions and all earnings or interest from a Traditional IRA are taxed as ordinary income in the year received. As noted above, amounts withdrawn before age 59½ generally incur a 10 percent early-withdrawal tax penalty. Beginning in 2023, in accordance with provisions of SECURE 2.0, minimum distributions from a Traditional IRA generally must begin by April 1 following the year the owner turns 73, for those who turn 72 on or after January 1, 2023 (although no RMD is required in 2023, interestingly).
- **Roth IRA:** A Roth IRA is like a Traditional IRA, but with several important differences. Similarities include the application of the same contribution limits (which apply on an aggregated basis to Traditional and Roth IRAs), the same earned income requirement, and the same penalty tax for distributions made before age 59½.

The key differences between Traditional and Roth IRAs are that (1) contributions to a Roth IRA are never tax deductible; (2) anyone with earned income can make contributions to a Roth IRA regardless of age; and (3) distributions from a Roth IRA are tax free if made on or after the taxpayer turns 59½ and at least five years after the year in which the taxpayer made his or her first contribution to any Roth IRA. Distributions also are tax free if made after death, upon disability, or for the first-time purchase of a primary residence. Traditional IRAs are subject to income limits, with the deductibility of contributions in 2023 disallowed above adjusted gross income of \$83,000 for single filers and above \$136,000 for married filing jointly when the individual or spouse making the contribution is covered by a workplace retirement plan. If your income in 2023 is between \$73,000 and \$83,000 for individuals and between \$116,000 and \$1136,000 for married couples filing a joint return, you may take a partial deduction for amounts contributed to the Traditional IRA. Unlike Traditional IRAs, Roth IRAs are not subject to minimum distribution requirements during the owner's lifetime. In 2023, individuals with annual incomes above \$153,000 for single filers and \$228,000 for married filing jointly cannot contribute to a Roth IRA. If your income in 2023 is between \$138,000 and \$153,000 for single filers and \$218,000 and \$228,000 for married couples filing a joint return, you may contribute a modified amount to a Roth IRA. An individual can convert a Traditional IRA to a Roth IRA without regard to the annual income limits that otherwise would apply to Roth IRA contributions. Such a conversion will trigger tax on the fair market value of the amount converted.

Defined Benefit Plans

With a traditional defined benefit plan (pension plan), upon commencement of retirement a retiree receives a specific monthly payment (the defined benefit) from his or her employer based on salary history, years of service, and age. These payments are typically guaranteed by the employer no matter how the underlying investments perform or how long the retiree lives. If returns are less than expected, or employees live longer than expected, the employer may have to increase contributions to the plan — thus bearing both the investment and longevity risks. Employees rarely contribute any of their own money to private sector defined benefit plans. Many public sector defined benefit plans, such as the California Public Employees'

Retirement System (CalPERS), require employees to contribute. Pension payments generally begin at retirement and are taxable as ordinary income when received.

Defined Contribution Plans

A defined contribution plan is a plan in which an employee's benefits during retirement primarily depend on the contributions made to his or her account by the employee and/or the employer as well as the investment performance of the assets in his or her account, rather than on the employee's years of service or earnings history. Unlike a defined benefit plan, in a defined contribution plan the exact benefit to be received at and during retirement is not known. Instead, the final amount available in a defined contribution plan for retirement income is the total account balance for the employee at the time the benefit commences. This is comprised of the value of the total of employee and employer contributions and the investment earnings (or losses) on the account, less investment and administrative fees. The amount contributed to the plan and decisions about how those assets are invested among the investment vehicles included in the plan are typically made by the employee, who bears the entire investment risk in addition to the longevity risk. Some of the most common types of defined contribution plans are discussed below.

401(k)

A 401(k) is an employer-sponsored retirement plan that allows employees to specify the amount of income to be deducted from their paychecks and placed in the plan. Contributions are made on a pre-tax basis and all contributions and earnings remain untaxed until withdrawn. In 2023, individuals younger than age 50 can contribute up to \$22,500 to their 401(k)s, while individuals age 50 and older can contribute up to \$30,000. In many plans, a portion of the employee's contribution is matched by the employer based on a set formula (e.g., 50 percent of the employee's contribution up to a maximum of 6 percent of employee compensation). Employers can also make other types of contributions. Employee and employer contributions combined generally can total up to \$66,000 in 2021 (\$73,500 if age 50 or older).

In-service distributions from a 401(k) plan generally are subject to restrictions. In addition, if a distribution is made, it generally will be subject to a 10 percent tax penalty unless the participant is at least age 59½ or another specified exception applies (e.g., disability, death). Beginning in 2023 minimum distributions must begin by April 1 following the calendar year in which the employee turns 73 or, if later (and depending on the plan's provisions), the calendar year in which the employee retires.

Roth 401(k)

401(k) plans are now permitted to offer designated Roth accounts. A designated Roth account under a 401(k) plan is like a Roth IRA in that contributions are made with after-tax dollars (i.e., contributions are included in the participant's gross income when made) and distributions are tax free if certain conditions are met. However, designated Roth accounts under a 401(k) plan differ in certain ways from a Roth IRA. For example, lifetime minimum distribution requirements apply beginning at age 72 or retirement, and in-service distributions are restricted, whereas such rules do not apply to Roth IRAs. In addition, the same limits that apply to non-Roth employee contributions to a 401(k) plan apply to employee contributions to a designated Roth account under the plan (\$22,500 in 2023). Non-Roth amounts within a 401(k) plan may be converted to a designated Roth account within the same plan if certain conditions are met. A 401(k) plan now may permit rollovers from non-Roth to Roth accounts for amounts that would not otherwise be eligible for distribution at the time of rollover. (A similar expansion applies to 403(b) plans and governmental 457(b) plans.)

403(b)

A 403(b) plan is also like a 401(k) plan, but is offered to the employees of educational, religious, and charitable organizations. Although several types of contribution limits apply to 403(b) plans, employee elective contribution limits through salary deduction are generally the same as for 401(k)s. Also, like 401(k)s, in-service withdrawals generally are restricted, and a 10 percent tax penalty applies to permissible withdrawals made before age 59½ (subject to certain exceptions). Earnings grow tax deferred until they are withdrawn, at which point they are taxed as ordinary income. Minimum distributions must begin by April 1 following the calendar year in which the employee turns 73 or, if later (and depending on the plan's terms), the calendar year in which the employee retires. A 403(b) plan can only invest in annuities or mutual funds, and most are invested in annuities.

Roth 403(b)

403(b) plans are now permitted to begin offering designated Roth accounts. Designated Roth accounts under a 403(b) plan are like such accounts under a 401(k) plan. Thus, as described above, contributions are made with after-tax dollars and distributions are tax free if certain conditions are met. Like their 401(k) counterparts, designated Roth accounts under a 403(b) plan also are subject to in-service withdrawal restrictions and minimum distribution requirements beginning at age 73 or retirement. Rollovers from non-Roth to Roth 403(b) plans are subject to rules like those for 401(k) plans.

457(b)

A 457(b) plan is a deferred compensation plan that is available only to employees of state and federal governments and tax-exempt organizations. Contribution limits for governmental 457(b) plans generally resemble 401(k) plans. Special catch up contribution rules allow participants to increase their catch-up contribution three years prior to the normal retirement date specified in the plan. One notable exception is that the aggregate employer and employee contributions to a governmental 457(b) plan are limited to \$22,500 (or \$30,000 for participants age 50 or older) in 2022, rather than the \$66,000 aggregate limit that generally applies to 401(k) plans. Non-governmental 457(b) plans are subject to the somewhat less favorable rules governing nonqualified deferred compensation, and increased contributions are not allowed for participants age 50 or older.

Governmental Roth 457(b)

Governmental 457(b) plans are now permitted to begin offering designated Roth accounts. Designated Roth accounts under a governmental 457(b) plan are like such accounts under a 401(k) or 403(b) plan. Rollovers from non-Roth to governmental Roth 457(b) plans are subject to rules similar to those for 401(k) and 403(b) plans. Designated Roth accounts are not allowed under non-governmental 457(b) plans.

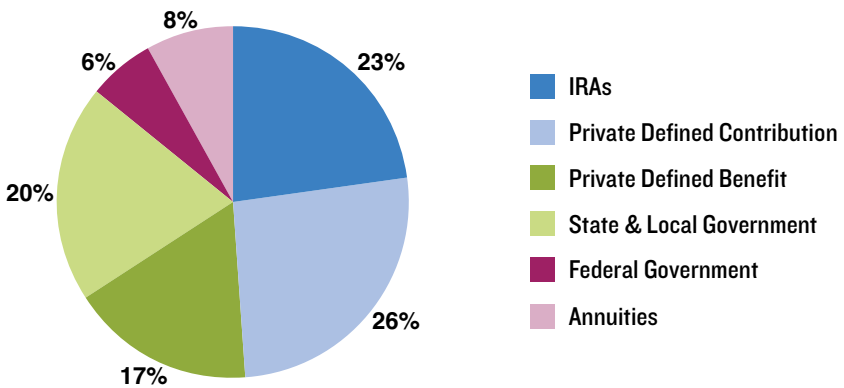
Shift in Retirement Plan Assets

The percentage of assets held in various types of retirement plans has changed significantly over the last few decades, reflecting a shift from employer-sponsored defined benefit plans to employee-funded defined contribution plans, such as 401(k) plans.

At the end of 2022, assets held in IRAs and Keoghs (tax-deferred retirement savings plans for self-employed individuals or small business owners) accounted for the largest segment of the retirement plan market with \$12.0 trillion, or 35 percent of total assets, as compared to 23 percent in 2000. Assets in defined contribution plans were \$9.3 trillion, or 27 percent of total assets in 2022, compared to 26 percent in 2000. In contrast, assets held in employer-sponsored defined benefit plans decreased from 17 percent to only nine percent of total retirement plan assets between 2000 and 2020.

Figure 12-1 Total U.S. Retirement Market Assets – 2000

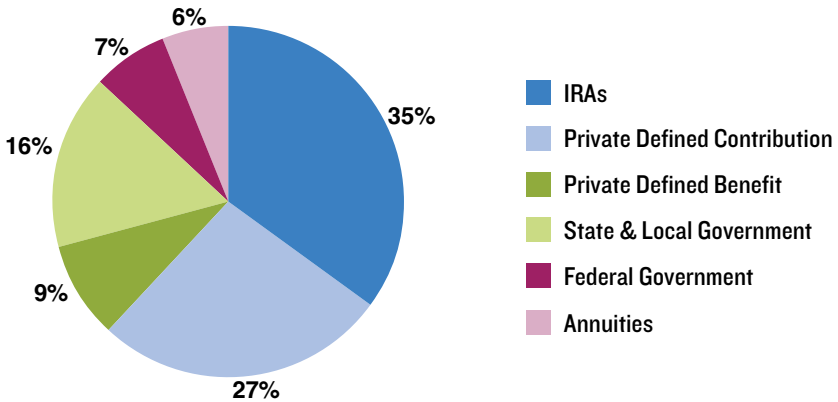
(100% = \$11.6 trillion)



Source: Investment Company Institute

Figure 12-2 Total U.S. Retirement Market Assets – 2022

(100% = \$34.2 trillion)



Source: Investment Company Institute

The Use of Annuities in Qualified Plans

The use of annuities in funding a qualified retirement plan is both longstanding and widespread.

As more and more Americans face retirement without the safety net of a traditional defined benefit pension plan that provides retirement income for life, new sources of guaranteed income will need to be identified. Annuities are uniquely suited to fill this need.

In 1952, the Teachers Insurance and Annuity Association - College Retirement Equities Fund (TIAA-CREF, now known as simply TIAA) developed the first variable annuity for use in college and university retirement plans. Due to the structure of regulations in this area, group and individual annuity contracts came to dominate the retirement plan arena for the non-profit sector. As time went on annuities also evolved into funding vehicles for other tax-qualified arrangements such as IRAs and 401(k)s. Annuities that are specifically created and designed for the qualified (i.e., retirement plan) market are subject to a variety of rules that are different from annuities in the non-qualified market. For example, the required minimum distribution requirements applicable to qualified plans include specific rules for the use of variable annuities in satisfying those requirements.

At the end of 2022, variable annuity assets invested in qualified retirement plans totaled \$1.16 trillion, or 68 percent of total variable annuity assets. The legitimacy of using a variable annuity to fund a qualified retirement plan is sometimes questioned because the annuity does not provide any additional tax-deferred treatment of earnings beyond that already provided by the plan itself. However, annuities also offer many benefits that can make them suitable for use in qualified plans, such as lifetime income, principal protection, death benefits, and fee guarantees.

The financial crisis and the associated reduction of many workers' retirement savings in qualified retirement plans has prompted a fresh look at annuities. While not using the word "annuity," in 2010 the Obama administration's Middle Class Task Force advocated "promoting the availability of guaranteed lifetime income products" to reduce "the risks that retirees will outlive their savings

or that their living standards will be eroded by investment losses or inflation.” And in 2014, the U.S. Treasury issued rules specifically addressing the use of Qualified Longevity Annuity Contracts (QLACs) in qualified plans, including setting purchase limits at the greater of 25 percent of qualified plan assets or \$125,000 (raised to \$130,000 in 2018 and to \$135,000 in 2020 and 2021, and to \$145,000 for 2022). Beginning in 2023, in accordance with provisions of SECURE 2.0, the purchase limit increases to \$200,000 and the 25 percent restriction is eliminated. Annuities are designed to help consumers reach their retirement goals by providing for the accumulation of assets during the owner’s income-producing years and guaranteeing payments in retirement that last a lifetime — a benefit that defined contribution plans not funded using annuities, or not offering annuity options such as QLACs, do not otherwise provide participants.

In-Plan Guaranteed Lifetime Income Options

Fixed immediate annuities were endorsed by the Government Accountability Office (GAO) and the federal government has been encouraging employer sponsors of defined contribution plans, such as 401(k)s, to offer them as options for retiring employees. See Chapter 7: *Generating (Almost) Immediate Income*, to learn more about these types of annuities. On December 20, 2019, the Setting Every Community Up for Retirement Enhancement (SECURE) Act was signed into law as part of the Further Consolidated Appropriations Act, 2020. The SECURE Act contains several provisions designed to encourage the use of in-plan guaranteed lifetime income options. In December 2023, the SECURE 2.0 Act was passed, further strengthening retirement security for Americans.

Advantages of In-Plan Guaranteed Lifetime Income Options

It is important to remember that the primary goal of a retirement plan is not to obtain tax deferral, but rather to provide retirement income that will last for the life of the retiree. In recognition of this there is a relatively new twist on the use of annuities within 401(k) plans — allowing employees to invest a percentage of ongoing contributions in an “in-plan” investment option that will build up a stream of “guaranteed income” for life that is not subject to the same market volatility of a typical equity or bond investment option in a 401(k) plan. These in-plan guaranteed income options typically provide downside income protection through insurance guarantees, upside income potential through participation in financial markets, and guaranteed income for life.

There is a widespread need for education on understanding and creating income in retirement, and employers can be a trusted source for that education. Employers and service providers often provide financial education on the topic of saving for retirement. Adding education on managing those assets in retirement is a logical next step. Employees will benefit from ongoing education on the value of guaranteed income options. Specifically, within an employer plan, participant education materials should clearly and concisely explain the benefits of guaranteed lifetime income products and how they compare to other options that are offered by their plan. This would include information such as the historic return patterns of each of the options, the specific risk ratios associated with each of the plan choices, the expense ratios or fees associated with each option, and an explanation of differences between and among different options. Similar educational information is already provided in the accumulation stage under the plans.

For employers, in-plan guaranteed options present advantages through enhanced value of the defined contribution plan as a labor force management tool. According to 2017 research by Prudential, 67 percent of defined contribution plan participants said investing in an in-plan guaranteed retirement income option made them more confident in general about their

retirement security. In addition to the enhanced security of the participant, such options can help ensure employees retire on time — delayed retirements can limit companies' abilities to hire new staff and provide advancement opportunities for existing talent and may represent a significant cost. In another 2017 study, Prudential found that employers incur an incremental cost of over \$50,000 for each employee whose retirement is delayed by one year. For an employer with 3,000 employees and workforce costs of \$200 million, a one-year delay in retirement age may cost \$2-\$3 million.

Other Sources of Insured Retirement Income

In addition to annuities, there are other retirement income instruments insured to last one’s lifetime.

The following table provides an overview of these other insured lifetime income vehicles, who provides the funding, and who provides the insurance that income will last one’s lifetime.

Figure 13-1 Other Sources of Insured Retirement Income

Instrument	Who Provides Funding	Who Provides Insurance for Lifetime Income
Defined benefit plans	Employers (public and private)	Private plans: Pension Benefit Guaranty Corporation Public plans: Federal and State governments
Social Security and Medicare	Payroll taxes into trust funds	Social Security Administration and the Federal Government
Life insurance	Individual	Life insurance companies
Long-term care insurance	Individual	Life insurance companies
Reverse mortgages	Individual	Federal Housing Administration
Fixed-income vehicles	Individual	Varies

Employer-Sponsored: Defined Benefit Plans

As with owners of annuities that include a guaranteed source of retirement income, individuals fortunate enough to be covered by a defined benefit program through their employer can look to a steady, guaranteed income source in retirement.

Defined benefit programs, also known as pensions, used to be the standard retirement benefit offered to employees. Over the years, this standard has given way to the defined contribution plan such as 401(k) plans, with which the employee assumes a much greater responsibility for his or her retirement savings and guarantees are no longer provided.

How a Defined Benefit Plan Works

A defined benefit plan guarantees an employee a certain benefit upon retirement. That amount generally depends on factors such as salary, age, and years of service with the company. For tax year 2021, the maximum retirement benefit permitted under a defined benefit plan is \$230,000 (unchanged from 2020).

Each year, pension actuaries calculate the future benefits that are projected to be paid from the plan and ultimately determine what amount, if any, needs to be contributed to fund that projected benefit payout. Employers are normally the only contributors to the plan. Defined benefit plans can require that employees contribute to the plan also, but it is uncommon. The employer is also responsible for making the decisions about how to invest the contributions.

Employees are always entitled to the vested accrued benefit earned to date. If an employee leaves the company before retirement, the benefits earned up to that point are frozen and held in a trust for the employee until he or she reaches retirement age. The defined benefit plan must allow its vested employees to receive their benefits no later than the 60th day after the end of the plan year in which the latest of the following occurs:

- They reach age 65 or the normal retirement age specified in their plan. Starting in 2002, the maximum benefit was reduced for retirement prior to age 62 and increased for retirement after age 65.
- They have been in the plan for 10 years.
- They leave their employer.

The plan cannot force employees to receive benefits before normal retirement age unless they have less than \$5,000 vested in the plan. However, employees must begin to receive their benefits no later than April 1 following the last year of employment or age 73, whichever is later.

Defined benefit plans distribute their benefits through life annuities. In a life annuity, employees receive equal periodic benefit payments (monthly, quarterly, etc.) for the rest of their lives. If married, and the employee has chosen the joint and survivor option, upon his or her death the surviving spouse can continue to receive distributions of at least 50 percent of the employee's periodic payment amount. Some plans may also allow employees to receive their entire benefit in one lump sum at retirement.

While still popular with government and public employees, according to the Department of Labor the number of private pension plans in the U.S. fell from a peak of 175,143 single- and multi-employer plans in 1983 to 46,577 plans in 2020, the most recent year for which data is available. As of 2022, the Pension Benefit Guaranty Corporation (PBGC) insures about 24,000 defined benefit plans, down from a high of about 114,000 in 1985. PBGC states that this decline was due primarily to the elimination of plans with 100 or fewer participants. A likely reason most were eliminated is the complexity and cost required to administer pension plans.

The Pension Benefit Guaranty Corporation, a federal agency, provides protection against a private pension not being able to meet its obligations. Pension plans for public employees are guaranteed by the federal and various state governments.

Government Programs

The most widely used source of insured retirement income in the United States is Social Security. Social Security provides insured retirement income for most non-governmental employees, assuming they have earned a minimum number of credits; generally, one must have worked 10 years to be eligible for benefits.

Many government employees are not covered by Social Security. They are commonly covered by other retirement pension programs, or by a combination of Social Security and other programs.

While Medicare technically does not provide insured income, it does provide health insurance for those age 65 and older (as well as for some under age 65 with disabilities). Like Social Security, Medicare is operated by trusts set up by the Federal government and is funded primarily via payroll taxes.

Individually Purchased Vehicles

The previous two sections — Employer-Sponsored Defined Benefit Plans and Government Programs — focused on insured retirement income that is not directly funded by an individual. This section focuses on sources for insured retirement income plans that individuals can purchase directly.

Life Insurance as a Source of Income in Retirement

The cash value available in a whole life insurance policy can be used to supplement retirement income. Whole life insurance includes any life insurance with a cash value, including universal life, variable life, and variable universal life. The advantage to this funding source is the flexibility in terms of when, how, and how much an individual can leverage.

Even for individuals who have done a good job saving for retirement — funding their IRAs, 401(k)s, and taxable retirement accounts — the market may not be “right” when it comes time to start drawing down their assets. While individuals may think they have accumulated enough savings to supply from 70 percent to 80 percent of their working income in retirement, a sustained market downturn can negatively impact their savings. In turn, this can increase the risk they will outlive their assets. A whole life insurance policy can be used to soften the effects of a down market by allowing investors to either withdraw cash or take a loan from the life policy and avoid drawing down their other retirement savings at the least opportune time.

There are other incentives to incorporating life insurance into a retirement portfolio. While some retirement plans can grow on a tax-deferred basis (called qualified retirement plans), whole life insurance makes cash available tax free. Plus, life insurance provides a tax-free insurance benefit to beneficiaries when the policyholder passes away.

In addition, while 401(k)s, IRAs, and other qualified savings plans are important, there are restrictions — such as the 10 percent tax penalty imposed on money withdrawn before age 59½.

One of the benefits of using life insurance as a part of retirement planning is that it allows one to access cash value. Highly rated life insurance companies invest primarily in highly rated bonds. That means one is participating in an insurance company’s bond portfolio without the downside risk of the bond market, because most whole life insurance policies provided a guaranteed

interest rate and cash value.

While using whole life insurance to help save for retirement can be beneficial, there are also pitfalls that could result in adverse tax consequences. Investors need to pay careful attention to the basis of their contract, which is usually the premium that has been paid, as well as the gain earned on the policy.

For example, take someone who has a contract with \$200,000 in basis and \$50,000 in gain. If \$210,000 is withdrawn, \$200,000 would be tax free and \$10,000 would be taxable.

To avoid current tax liability for amounts above cost basis (the amount invested), the consumer should consider a loan. Loans against a life insurance policy are not taxable, but if they are not repaid, they will reduce the death benefit and could cause the policy to lapse. Outstanding loans also reduce the interest or investment gains that accrue, so it is also important to ensure that the life insurance policy remains in force and matures as a death claim, as any gains, including gains on amounts taken as loans, are taxable in the year the policy lapses. For beneficiaries who are no longer relying on the investor for financial support, the life insurance policy can become an additional retirement fund to the extent the death benefit proceeds net of loan repayment are paid out.

Long-term Care Insurance

Long-term care (LTC) is the name given to the spectrum of daily living and health services provided to individuals who can no longer function independently due to a physical or cognitive impairment and/or aging. Services may be provided on an inpatient, outpatient, or at-home basis. Long-term care insurance (LTCI) is insurance that is purchased to cover an individual's ongoing need for long-term care services.

Many people don't anticipate they will need LTC or mistakenly think LTC will be covered by Medicare, but statistics show that at least 70 percent of people turning 65 today will need long-term care services at some point in their lives (U.S. Department of Health and Human Services).

LTC, especially if confined to a nursing home, is extremely expensive and only the very financially well-off can typically pay for extended LTC on an out-of-pocket basis. Figure 13-2 provides an overview of different types of services and care levels available and their 2021 costs (2022 data was not available at time of publication).

Figure 13-2 Costs of Long-Term Care and Related Services

Type of Service	Services Provided	2021 Median Cost	Median Annual Cost	Change from 2020
Licensed Homemaker Services	Hands-off care such as helping with cooking and cleaning and running errands	\$26/hour	\$59,488	10.64%
Licensed Home Health Aide Services	Hands-on personal care such as help in bathing, dressing, and transferring	\$27/hour	\$61,776	12.50%
Adult Day Health Care	Social and other related support services in a community-based setting for part of the day	\$78/day	\$20,280	5.41%
Assisted Living Facility (One Bedroom)	Hands-on personal care as well as medical care for those unable to live by themselves	\$148/day	\$54,000	4.65%
Nursing Home (Semi-Private Room)	24-hour skilled nursing care	\$260/day	\$94,900	1.96%
Nursing Home (Private Room)	24-hour skilled nursing care	\$297/day	\$108,405	2.41%

Source: Genworth Cost of Care Survey 2021

LTCI can be purchased individually or at the workplace as part of a group employee benefit, with most sales occurring in the individual market. Approximately eight million Americans have LTCI; even if every policy owner is at least age 65, only about 17 percent of the 48 million Americans who are 65 or older would be covered by LTCI (American Association for Long-Term Care Insurance; United States Census Bureau).

Over the past several years, many insurance companies have struggled to make long-term care insurance a profitable product line. LTC services are wide-ranging, expensive, and difficult to predict. With annuities, the amount and timing of payments is known but the duration is not; with life insurance, the timing of payment is unknown, but the amount is, and the payment is typically a one-time event. With LTCI, the amount, timing, and duration of payments are all unknown, and small pools of insureds make it difficult to price the product at a point where it will be both affordable for the consumer and profitable for the insurer. However, LTC and an aging population that will consume ever more of these services is not an issue that will disappear. Government and the private sector must work together to resolve the LTC crisis.

Other Income-Generating Products

Reverse Mortgages

Reverse mortgages provide lifetime retirement income and are insured by the Federal Housing Administration.

A reverse mortgage is a loan that enables older homeowners, 62 or older, to convert part of the equity in their homes into tax-free cash without having to sell the home, give up title, or take on a new monthly mortgage payment. Seniors with an outstanding first mortgage or other debt on their home may also qualify for a reverse mortgage. The proceeds of the reverse mortgage,

however, must first be used to pay off such debts.

To qualify for a reverse mortgage, a person must:

- Be at least 62 years old. In the case of a couple or co-owners, both must be 62 if their names appear on the title to the home
- Own as primary residence a single-family home, qualified condominium, townhouse, manufactured home, or one- to four-family owner-occupied property

The payment options available under a reverse mortgage include:

- An up-front lump-sum payment
- Line of credit
- Fixed monthly payments for as long as you remain in your home (or a predetermined, shorter period)
- A combination of monthly income and line of credit

In the 2022 fiscal year there were 64,489 Home Equity Conversion Mortgages (HECMs) completed in the United States, up 31.1 percent from 49,207 in fiscal year 2021.¹

The bipartisan Reverse Mortgage Stabilization Act was signed into law in 2013. “The new law gives FHA the authority to make administrative decisions on an expedited basis in order to manage the HECM program more responsively based on lessons learned along the way and ever-changing economic conditions” (*Reverse Mortgage Magazine*, November-December 2013; National Reverse Mortgage Lenders Association).

Fixed-income Vehicles

It is possible to withdraw interest from fixed-income vehicles while maintaining the principal. If the underlying principal is guaranteed, the individual is guaranteed income for life. However, it is important to note that the level of income is not guaranteed.

We will use a certificate of deposit (CD) as an example. Assume someone puts \$100,000 into a one-year CD; as of this writing, the best rate for a one-year CD on bankrate.com was 5.4%, which would provide \$54 of income and the owner will still have \$1,000 at the end of the year to reinvest. And since the CD is guaranteed by the FDIC (up to certain limits), the person is guaranteed income for his or her lifetime.

However, the person is not guaranteed \$1,000 a year in this example. The guaranteed income amount will vary in future years based on future interest rates. Inflation is also of far greater concern than at any point in the past 40 years. While the headline inflation rate for the 12-month period ending June 2023 was only three percent, inflation was significantly higher in certain categories, some of particular importance to those living on a fixed income. For example, the Economic Research Service of the U.S. Department of Agriculture predicts food prices to increase 5.9 percent in 2023, more than the best one-year CD rate available.

¹ National Reverse Mortgage Lenders Association



Regulation and Taxation of Annuities

Annuities are insurance contracts regulated under state insurance laws. Variable annuities and certain other types of annuities are also regulated as securities under federal and state securities laws.

Regulation Under State Insurance Laws

All fixed and variable annuities are governed by a comprehensive state regulatory framework. State laws govern the organization and licensing of insurance companies, and state insurance departments oversee insurance company operations. Generally, annuity contracts and amendments must be filed with, and approved by, the state in which contracts are sold or by the Interstate Insurance Product Regulation Commission (IIPRC) (often referred to as the “Interstate Compact”), an important modernization initiative that benefits state insurance regulators, consumers, and the insurance industry. Insurance salespersons (often referred to as “producers”) need to be licensed in each state in which they operate. Only licensed producers may sell annuity contracts.

The National Association of Insurance Commissioners (NAIC) is a voluntary organization of the chief insurance regulatory officials of the 50 states, the District of Columbia, and five U.S. territories. The NAIC promotes best practices and uniformity in state insurance laws through the development of “model laws” and “model regulations” that are designed to protect consumers and maintain the financial stability of the insurance marketplace. Each state can decide whether to adopt these model laws and model regulations and are free to modify them as they deem appropriate.

Insurance Company Licensing

To offer annuity products in a state, an insurance company must be licensed in that state. A company needs to be licensed regardless of whether it is a “domestic” insurance company (i.e., organized in the state) or a “foreign” insurance company (i.e., organized in another state). To be licensed, an insurance company must be organized according to specific state laws. Before it is granted a license, an insurance company must demonstrate compliance with strict capital, surplus, and financial requirements. In addition, the state scrutinizes the experience and character of the company’s management.

Producer Licensing and Appointment

Insurance producers must be licensed by state insurance departments. Applicants must submit a form to the state providing information about their experience, character, and financial responsibility. They also must pass an examination. Insurance producers also must be appointed by an insurance company before the producer may sell the company's products.

Contract Requirements and Prior Regulatory Approval

Annuity contracts and related forms generally must be filed and approved in every state where they will be sold. An alternative, more streamlined method of obtaining state approval is to file through the Interstate Insurance Product Regulation Commission (IIPRC), of which 46 states and territories are currently members. While there is no standard required form for annuity contracts, states and the IIPRC set forth standards that are applicable for contracts filed with the IIPRC.

Generally, contracts need to be readable and set forth the contract's benefit terms and conditions before the state or the IIPRC will approve the annuity for sale. Amendments to contracts also must be filed and approved. If the amendment could adversely affect existing contract owners' rights, prior approval from the contract owners may be required.

Protection Against Insurance Company Insolvency

State Guaranty Funds

All states, the District of Columbia, and Puerto Rico have guaranty funds to protect contract owners against insurance company insolvency. Insurers doing business in a state must contribute to that state's guaranty fund. The actual coverage provided for annuity contracts varies from state to state, but cash values and annuity benefits generally are protected for at least \$100,000. Coverage generally is not provided for variable annuity contracts other than those portions that are guaranteed by the insurance company, e.g., fixed accounts.

Insulation from Insurance Company's Creditors

Variable annuity contracts are issued through life insurance company separate accounts. When a contract owner allocates purchase payments to a variable investment option under a variable annuity contract, those assets are held in the separate account. The assets in the separate account are insulated against the creditors of the insurance company in the event of the company's insolvency (in some states, annuity assets are also shielded from the contract owner's creditors).

Regulation Under Federal Securities Laws

Besides being governed by the state regulatory framework, absent an exemption, certain types of annuities, such as contingent deferred annuities (CDAs), market value adjusted (MVA) annuities, and registered index-linked annuities (RILAs), variable annuities are regulated as securities under the federal securities laws (Federal Securities Laws), including:

- the Securities Act of 1933 (1933 Act) and the rules thereunder, which govern the registration of the offerings of annuities that are securities, including, among other things, the disclosures (e.g., prospectuses) that must be provided to investors;
- the Securities Exchange Act of 1934 (1934 Act) and the rules thereunder, which govern the registration and other requirements applicable to persons, known as broker-dealers, who are permitted to sell securities;
- the Investment Company Act of 1940 and the rules thereunder, which govern the registration and other requirements applicable to investment companies, such as life insurance company separate accounts that serve as investment options under variable annuities and the mutual funds in which they invest; and
- the Investment Advisers Act of 1940 and the rules thereunder, which govern the registration and other requirements applicable to investment advisers who may be providing advice about annuities that are securities.

The SEC administers the Federal Securities Laws and promulgates rules thereunder. Fixed annuities, under which the insurance company guarantees a specific rate of return to the contract owner, generally are not subject to these laws. In addition, the Dodd-Frank Act (discussed below) effectively exempts fixed indexed annuities from the 1933 Act, subject to compliance with certain conditions.

In summary, the Federal Securities Laws require certain disclosure documents, including a prospectus and certain periodic reports, to be filed with the SEC and given to investors. In addition, written marketing materials such as advertisements are subject to regulation under SEC and FINRA rules. These requirements are discussed in more detail on the following pages.

Securities Act of 1933

Registration

Because variable annuities and certain other annuities (collectively, “registered annuities”) are securities, they generally must be registered with the SEC under the 1933 Act before they can be offered to the public (with two exceptions noted below). The SEC staff reviews and comments on registration statements, which usually must be amended in response to staff comments before they will be declared effective. (The SEC does not, however, approve or disapprove of any securities, including registered annuities, and does not pass on the accuracy or adequacy of any prospectus.) A “post-effective” amendment updating the registration statement generally must be filed at least annually.

The first registration exception is for registered annuity contracts issued in connection with certain qualified plans, such as 401(k) plans. The second exception is for annuities that are offered on a private placement basis, typically to sophisticated investors who meet certain requirements under the Federal Securities Laws (and not to members of the general public). Even with these exceptions, however, the anti-fraud provisions of the Federal Securities laws still apply.

Prospectus Delivery

When an investor purchases a registered annuity, he or she receives a prospectus, which includes detailed descriptions of the salient features of the product, such as annuity and death benefits, fees and charges, and investment options. Registered annuity prospectuses, which insurers update regularly, can be lengthy and sometimes over one hundred pages. The prospectuses that describe the mutual funds that serve as underlying investment options in variable annuities (underlying funds), for example, can also be quite lengthy and depending on the number of investment options selected investors may receive numerous underlying fund prospectuses.

To its credit, the SEC has adopted rules that address concerns about potentially overwhelming investors with information, by permitting the use of “summary prospectuses” for both variable annuities and variable life insurance products (variable insurance products) as well as for mutual funds. The use of summary prospectuses reflects a “layered disclosure approach” that involves the provision of key information in a much shorter, user-friendly format with more detailed information, including the full statutory prospectus, available to investors online. For variable insurance products, insurers may use an initial summary prospectus for variable annuities currently offered to new investors, and an updating summary prospectus for existing investors that briefly describes certain changes to the contract that occurred during the previous year. Although the use of summary prospectuses is optional, the SEC expects widespread adoption by insurers.

Notably, when the SEC adopted its rule to permit the use of variable insurance product summary prospectuses, it included a provision that deems the obligation to deliver underlying fund prospectuses as satisfied if: (1) an initial summary prospectus is used for each currently offered variable insurance product contract described in the relevant registration statement, (2) the underlying fund uses a summary prospectus, and (3) the current summary prospectus, statutory prospectus, statement of additional information, and most recent annual and semi-annual reports of the underlying fund are available online. This provision eliminates the need to deliver underlying fund prospectuses and summary prospectuses in paper form, except when requested by an investor. Although the use of summary prospectuses is optional, the SEC expects widespread adoption by insurers issuing variable insurance products.

For variable insurance products that were discontinued as of July 1, 2020, the SEC permits the delivery of alternative disclosures instead of a current prospectus contained in an updated registration statement. These alternative disclosures consist of the current prospectuses or summary prospectuses, periodic reports, proxy materials, and other shareholder materials of the underlying funds, audited financial statements of the insurer’s separate account through which interests in the variable insurance products are issued, audited financial statements of the insurer (delivered in the case of variable life insurance policies; available in the case of variable annuities), transaction confirmations, and an annual statement of the number of units and values in each investor’s account, all delivered in paper format. The SEC also conditionally permits the use of an optional “modernized” alternative disclosure approach under which in lieu of providing prospectuses or summary prospectuses in paper format, the insurer would deliver a “notice” document containing essentially the same information that would be included in an updating summary prospectus, while providing the prospectuses, SAI, and most recent periodic reports for the underlying funds online. The modernized alternative disclosure approach also would require the insurer to file its financial statements and those of the relevant separate accounts with the SEC.

Registered annuities that are not variable annuities do not have their own SEC registration form. As a result, they register on a “catch-all” registration form that is not tailored to their particular situation. In response to efforts by the IRI and others, and in light of the growing popularity

of RILAs, Congress passed the Registration for Index-Linked Annuities (RILA) Act of 2020 in December 2022. The RILA Act requires the SEC to adopt a registration form specifically for RILAs within 18 months after passage of the Act. If the SEC fails to do so, the Act authorizes RILAs to be registered on the same registration form used for variable annuities.

Disclosure of Fees and Expenses

Variable annuity prospectuses currently contain fee tables that disclose the maximum guaranteed charge for all contract transaction expenses and recurring charges. These amounts are expressed in dollars or percentages of the contract value so purchasers will know what they will pay if they buy the contract. The fee tables also list the range of total operating expenses for the underlying funds offered by the contract. Historically, variable annuity prospectuses contained numerical examples showing in dollars per \$10,000 what a hypothetical contract owner would pay for the contract and the maximum fees and expenses charged by any of the funds over one-, three-, five-, and 10-year periods. These examples assume a 5 percent return and that the contract is surrendered at the end of the relevant period. Additional examples are required that assume the investor does not surrender the contract if a sales load or other fee is charged upon surrender. This format shows the effect of any surrender charge. On January 1, 2022, certain revisions to the SEC registration statement for variable annuities became effective that require, among other things, the inclusion in the prospectus of a “Key Information Table” that shows the minimum and maximum annual fees for the variable annuity contract, the underlying fund investment options, and available optional benefits. The Key Information Table also must include figures for the lowest and highest annual costs, based on current charges, assuming an investment of \$100,000, 5% annual appreciation, the least and most expensive combination of contract “classes,” optional benefits, and underlying fund fees and expenses, no withdrawals, additional purchase payments, or transfers, and no sales charges. The \$100,000 investment assumption also applies in lieu of the previous \$10,000 investment assumption for the numerical example in the fee table.

Securities Exchange Act of 1934

The 1934 Act regulates the distribution of registered annuities through registered broker-dealer firms and their registered representatives. Broker-dealers and their representatives are subject to extensive operational and financial rules that cover minimum net capital requirements, reporting, recordkeeping, supervision, advertising, and sales activities.

In addition to the broker-dealer regulatory framework established by the 1934 Act, registered broker-dealer firms that sell registered annuities also must be members of FINRA, which is a self-regulatory organization overseen by the SEC. It has an extensive body of rules with which broker-dealers must comply. For example, examinations are required; fingerprints must be provided; and numerous supervisory, suitability, advertising, recordkeeping, and reporting rules apply.

A 1934 Act rule requires broker-dealers to send confirmation statements to contract owners to reflect purchase and sale transactions involving a registered annuity. In addition, insurance companies send variable annuity contract owners periodic account statements showing a beginning balance, transactions during the period, and an ending balance so that the owner will have a record of all activity in his or her contract.

Investment Company Act of 1940

The 1940 Act imposes an extensive federal regulatory structure on investment companies, including variable annuity separate accounts and underlying funds. (Some separate accounts and funds, however, such as those used in connection with tax-qualified retirement plans, are excluded from 1940 Act regulation.) For example, the 1940 Act governs how variable annuities and shares of underlying funds are issued and redeemed. There are also corporate governance requirements and prohibitions against self-dealing.

Each separate account regulated under the 1940 Act must file a report on its operations annually with the SEC. In addition, annual and semi-annual reports containing information about the underlying mutual funds that serve as investment options for variable annuities must be sent to contract owners. In some cases, these reports also contain information on the variable annuities themselves.

The SEC follows a risk-based approach in inspecting variable annuity separate account operations. The SEC and FINRA also inspect various locations, such as broker-dealer branch offices, from which variable annuities are sold. Examination recommendations are made, and any deficiencies are noted. If the situation is serious enough, it may lead to regulatory enforcement.

Regulation of Fees and Charges

Currently, the SEC does not regulate individual variable annuity fees and charges. However, the 1940 Act makes it unlawful for any registered separate account funding variable annuity contracts, or for the sponsoring insurance company, to sell any such contract unless the fees and charges deducted under the contract are, in the aggregate, reasonable in relation to the services rendered, the expenses expected to be incurred, and the risks assumed by the insurance company. The insurer must represent in the annuity contract's registration statement that the fees and charges are reasonable.

Investment Advisers Act of 1940

The Advisers Act regulates investment advisers who are compensated for providing advice about securities to others and who manage more than \$100 million. (State securities regulation applies to investment advisers who manage less than that.) Some annuities, such as fee-only variable annuities, have been specifically designed to facilitate their use by investment advisers. The Advisers Act imposes a number of qualification, registration, compliance, custody, disclosure, recordkeeping and other requirements on investment advisers. Investment advisers are subject to a fiduciary duty standard of conduct, unlike broker-dealers who are subject to a "best interest" standard of conduct, discussed below.

Standard of Conduct for Financial Professionals

For more than a decade, Congress and regulators at the federal and state levels have been working to formulate appropriate standards of conduct for financial professionals who provide

personalized advice about investments and/or insurance to retail consumers. IRI and its members have long supported the principle that financial professionals should be required to act in their clients' best interest, and IRI has been among the leaders of the financial services industry's efforts to advocate for adoption of a clear, consistent, and workable best interest standard that will provide meaningful and effective consumer protections without depriving Americans of access to valuable financial products and services.

SEC Regulation Best Interest and Form CRS

On June 5, 2019, the SEC voted to adopt a rulemaking "package" consisting of: (1) new SEC "Regulation Best Interest," (Reg BI) which establishes a best interest standard of conduct for broker-dealers (BDs) and their associated persons when making a recommendation of any securities transaction or investment strategy involving securities to a retail customer; and (2) disclosure changes, including a new Form CRS Relationship Summary, required disclosures in retail communications, and limitations on the use of the title "adviser" and similar words. Concurrent with the release of Reg BI and Form CRS, the SEC issued guidance regarding the fiduciary standard of conduct applicable to investment advisers (IAs), as well as guidance regarding the "solely incidental" prong of the BD exclusion from the definition of "investment adviser" under the Advisers Act.

Reg BI imposes a best interest obligation on a BD and its individual associated persons by requiring them to act in the best interest of a "retail customer" when recommending a securities transaction or investment strategy involving securities, without placing their financial or other interests ahead of the interest of the retail customer. The best interest obligation is satisfied if the BD or its individual associated persons meets four component obligations: a disclosure obligation, a care obligation, a conflict of interest obligation, and a compliance obligation.

The disclosure obligation under Reg BI requires that, prior to or at the time of a recommendation, a BD and its individual associated persons must fully and fairly disclose to retail customers, in writing, all material facts relating to the scope and terms of the relationship with the retail customer, as well as all material conflicts of interest associated with the recommendation." The adopting release for Reg BI noted that the use by broker-dealers and their individual associated persons of the words "adviser" or "advisor" as part of a name or title when communicating with retail investors would be presumed to be a violation of the capacity disclosure requirement under the disclosure obligation of Reg BI if the BD or individual associated person is not also registered as an IA or a supervised person of an IA.

The care obligation under Reg BI requires that, in making a recommendation to a retail customer, a BD and its individual associated persons must exercise reasonable diligence, care, and skill to: (1) understand the potential risks, rewards, and costs (including both acquisition costs and costs related to a future sale or exchange, such as deferred sales charges or liquidation costs) associated with the recommendation; (2) have a reasonable basis to believe that the recommendation could be in the best interest of at least some retail customers, and is in the best interest of a particular retail customer based on that retail customer's investment profile and the potential risks, rewards, and costs associated with the recommendation; and (3) have a reasonable basis to believe that a series of recommended transactions, even if in the retail customer's best interest when viewed in isolation, is not excessive and is in the retail customer's best interest when taken together in light of the retail customer's investment profile."

The conflict of interest obligation under Reg BI requires that BDs establish, maintain, and enforce written policies and procedures reasonably designed to: (1) identify and at a minimum disclose, or eliminate, all material conflicts of interest that are associated with such recommendations; and (2) identify and mitigate any conflicts of interest associated with recommendations that create an incentive for individual associated persons of the BD to place their own interests ahead of the interests of the retail customer; (3) identify and fully/fairly disclose any material limitations placed on the securities or investment strategies involving securities that may be recommended to a retail customer and any conflicts of interest associated with such limitations; and prevent such conflicts from causing the BD or individual associated persons to place their own interests ahead of the interests of the retail customer; and (4) identify and eliminate any conflicts of interest associated with sales contests, bonuses, and non-cash compensation that are based on the sales of specific securities or specific types of securities within a limited period of time.

The compliance obligation under Reg BI requires that BDs establish, maintain, and enforce policies and procedures reasonably designed to achieve compliance with Regulation Best Interest as a whole.

Form CRS requires BDs and IAs to provide a client or customer relationship summary (“Form CRS”) to retail investors to inform them about (1) the type of client and customer relationships and services the firm offers; (2) the fees, costs, conflicts of interest, and required standard of conduct associated with those relationships and services; (3) whether the firm and its financial professionals currently have reportable legal or disciplinary history; and (4) how to obtain additional information about the firm.

Reg BI and Form CRS became effective as of June 30, 2020. In 2022 and 2023, the SEC staff issued bulletins to assist firms with compliance regarding account recommendations (March 2022), conflicts of interest (August 2022), and the care obligation (April 2023).

The SEC filed its first complaint alleging violations of Reg BI in June 2022. FINRA brought its first Reg BI enforcement action in October 2022 and subsequent actions in 2023. According to press reports, a FINRA enforcement executive announced in March 2023 that FINRA is planning to complete at least 1,000 Reg BI exams of broker-dealers by year’s end.

On January 30, 2023, the SEC’s Division of Examinations issued a risk alert highlighting what it considered to be deficiencies and weak practices noted during Reg BI examinations, including the following:

- Compliance Obligation – not having adequate written policies and procedures, including instances of generic written policies and procedures that were not tailored to the firm’s business model.
- Care Obligation – directing financial professionals to consider reasonably available alternatives to recommendations, or costs, without providing any guidance on how to do so.
- Conflict of Interest Obligation – identifying only those conflicts associated with prohibited activities (e.g., churning), rather than identifying all conflicts; or using high-level, generic language (e.g., “we have conflicts related to compensation differences”) that did not describe the conflicts with enough specificity.
- Disclosure Obligation – not providing disclosures to retail customers in writing but instead posting Reg BI disclosures only on the broker-dealers’ websites or merely referencing the disclosures in other documents delivered to customers.

Likewise, in its 2023 Report on Examination and Risk Monitoring Program, issued on January 10, 2023, FINRA outlined several variable annuity sales practices that it found problematic under Reg BI, including:

- Key Information – not adequately collecting and retaining key information on variable annuity transactions, particularly in connection with recommended exchanges into new variable annuity contracts.
- Training – not sufficiently training registered representatives and supervisors on how to assess and compare costs and fees, surrender charges, and long-term income riders.
- Exchanges – not reasonably supervising recommendations of exchanges into new variable annuity contracts.
- Insurer Buyout Offers – not reasonably supervising recommendations related to issuer offers to “buy out” variable annuity contracts from existing holders.
- Additional Premium Payments – not evaluating and supervising registered representatives’ recommendations of additional premium payments into existing variable annuity contracts, including review of disclosure, any applicable surrender fees related to the transaction, and the rationale for the addition.
- Reasonably Available Alternatives – insufficiently considering reasonably available alternatives to a recommended variable annuity purchase, surrender, or exchange.

Reg BI continues to be an area of regulatory examination focus, as discussed below under “SEC and FINRA Examination Priorities.”

FINRA Suitability Rule for Deferred Variable Annuities – Rule 2330

FINRA Rule 2330 imposes a wide range of requirements tailored specifically to deferred variable annuity transactions, including suitability, principal review, supervision, and training. This Rule provides that, in recommending a deferred variable annuity, a registered representative must have a reasonable basis to believe that (1) the customer has been informed in general terms of various features of a deferred variable annuity; (2) the customer would benefit from certain features of deferred variable annuities, such as tax-deferred growth, annuitization, or a death or living benefit; and (3) the particular deferred variable annuity as a whole, the underlying subaccounts to which funds are allocated at the time of purchase or exchange of the deferred variable annuity, and riders and product enhancements, if any, are suitable for the particular customer based on required customer information. These specific requirements are in addition to the requirements of FINRA Rule 2111 governing suitability generally. As discussed above, the NAIC Suitability Model is patterned after FINRA’s suitability standards. FINRA has published substantive guidance, in question-and-answer format, on the suitability obligations of member firms and registered representatives under FINRA Rule 2111, including with respect to hold recommendations, implicit recommendations, investment strategies, non-securities products, and recordkeeping, among other things.

On June 18, 2020, the SEC approved a rule change proposed by FINRA to provide clarity and remove certain inconsistencies with Reg BI. Among other things, FINRA amended Rule 2111 to state that it does not apply to recommendations that are subject to Reg BI. The underlying rationale is that compliance with Reg BI would necessarily result in compliance with FINRA’s suitability standard. FINRA did not eliminate Rule 2111 altogether because it applies to all recommendations to customers whereas Reg BI applies only to recommendations to “retail

customers,” (i.e., a natural person or the natural person’s legal representative who receives a recommendation of a securities transaction (or an investment strategy involving securities) and who uses the recommendation primarily for personal, family, or household purposes). FINRA Rule 2111 continues to apply to recommendations to entities and institutions such as pension funds, as well as natural persons who use the recommendations other than primarily for personal, family, or household purposes. Examples provided in the proposed rule change include small business owners and charitable trusts.

FINRA has taken a number of steps to assist member firms in complying with Reg BI, such as providing a checklist for that explains key differences between FINRA’s rule and the SEC rule and related disclosure requirements under SEC Form CRS and posting podcasts and virtual conferences on topics such as SEC Reg BI implementation and regulatory compliance inspections and examinations.

DOL Fiduciary Investment Advice Rule

On April 14, 2015, the DOL issued a proposed regulation that would re-define the circumstances under which firms and individuals who provide “investment advice” to employee benefit plans or individual retirement accounts would be considered fiduciaries. On April 6, 2016, the DOL issued a final version of its fiduciary rule, and related prohibited transaction exemptions, which drastically expanded the universe of financial professionals who would be deemed to be “fiduciaries” under the law. Shortly thereafter, several industry trade associations, including IRI, filed lawsuits seeking to overturn the rule on a variety of grounds.

On March 15, 2018, the U.S. Court of Appeals for the Fifth Circuit invalidated the DOL Fiduciary Rule, including the Best Interest Contract (BIC) Exemption, the Principal Transactions Exemption, and related amendments to existing prohibited transaction exemptions, in a case involving a challenge by the U.S. Chamber of Commerce and other plaintiffs including IRI. Among other things, the Fifth Circuit found that the DOL Fiduciary Rule conflicted with the language of ERISA. On June 21, 2018, the Fifth Circuit issued a formal mandate vacating the DOL Fiduciary Rule.

Following the Fifth Circuit’s opinion, the DOL issued Field Assistance Bulletin (FAB) 2018-02, announcing a temporary enforcement policy pursuant to which it would not pursue prohibited transaction claims against investment advice fiduciaries who are working “diligently and in good faith” to comply with the impartial conduct standards for transactions that would have been exempted under the BIC Exemption or the Principal Transactions Exemption, or treat the fiduciaries as violating the applicable prohibited transaction rules. The temporary enforcement policy announced in FAB 2018-02 remains in place until December 20, 2021.

On June 29, 2020, the DOL formally restored the original investment advice regulation and its five-part test for defining an investment advice fiduciary, while also restoring DOL Interpretive Bulletin 96-1 regarding participant investment education and the prohibited transaction exemptions that were amended in 2016 to their pre-amendment forms.

On July 7, 2020, the DOL proposed to create a new prohibited transaction class exemption, entitled “Improving Investment Advice for Workers & Retirees,” that would be available for investment advice fiduciaries in lieu of the prohibited transaction exemptions issued by the DOL in 2016. The proposed prohibited transaction exemption would be available to financial institutions such as registered investment advisers, broker-dealers, banks, insurance companies and their employees, representatives, and agents.

Under the proposed prohibited transaction exemption, financial institutions and investment professionals, and their affiliates and related entities, would be able to receive reasonable compensation as a result of providing fiduciary investment advice, including commissions, 12b-1 fees, trail commissions, loads, markups and mark-downs, and revenue sharing from third parties. The proposed prohibited transaction exemption also would cover compensation received as a result of investment advice to roll over assets from a plan to an IRA, and would provide relief for a financial institution to engage in the purchase or sale of an asset in a riskless principal transaction or a covered principal transaction, and receive a mark-up, mark-down, or other payment for rollovers and allow principal transactions between financial institutions, plans, and IRAs.

To rely on the proposed prohibited transaction exemption, the financial institution and investment professional would be required to act in accordance with impartial conduct standards. The impartial conduct standards have three components, including a best interest standard, a reasonable compensation standard, and a requirement to make no misleading statements about investment transactions and other relevant matters. The DOL noted, among other things, that the proposed best interest standard is to be interpreted and applied in a manner consistent with the best interest standard set forth in the SEC's Reg BI. Under the proposed prohibited transaction exemption, financial institutions would be required to acknowledge in writing their fiduciary status, as well as that of their investment professionals, with respect to any fiduciary investment advice provided by the financial institution or investment professional to the retirement investor. In addition, financial institutions would be required to provide reasonable oversight of their investment professionals, adopt a "culture of compliance," and engage in an annual retrospective review of compliance with the impartial conduct standards.

On December 18, 2020, the DOL adopted the foregoing exemption as Prohibited Transaction Exemption (PTE) 2020-02 under ERISA and the Internal Revenue Code for investment advice fiduciaries with respect to employee benefit plans and individual retirement accounts (IRAs). PTE 2020-02 expressly covers prohibited transactions resulting from rollover advice and advice on how to invest assets within a plan or an IRA. PTE 2020-02 became effective on February 16, 2021.

In April 2021, the DOL issued FAQs on PTE 2020-02 in which it stated that it anticipated taking further regulatory actions, including "amending the advice fiduciary regulation, amending PTE 2020-02, and amending or revoking some of the other existing class exemptions available to investment advice fiduciaries."

In June 2021, the DOL published its Spring 2021 regulatory agenda, which indicated that proposed rulemaking regarding the definition of the term "Fiduciary" would be issued in December 2021. In its Spring 2022 regulatory agenda, the DOL indicated that this initiative was delayed until December 2022. The DOL's Spring 2023 regulatory agenda indicated an August 2023 date for a new fiduciary rule, but that date passed with no new rule.

In the meantime, on February 2, 2022, the Federation of Americans for Consumer Choice (FACC) and several insurance agents and agencies based in Texas sued the DOL in a Texas federal court seeking to set aside the DOL's new interpretation of the investment advice fiduciary regulation "five part test" set out in the preamble to PTE 2020-02 on grounds that it exceeded the DOL's statutory jurisdiction and is arbitrary, capricious, and contrary to law. Among other things, the FACC argued that the DOL's new interpretation carried forward the core problem that the Fifth Circuit identified in vacating the Fiduciary Rule, namely, the DOL's impermissible effort to rewrite and expand the definition of fiduciary under ERISA and the Internal Revenue Code. The

FACC also asked the court to vacate the DOL's interpretation in its entirety.

On February 9, 2022, the American Securities Association (ASA) filed suit against the DOL in a Florida federal court challenging guidance that it issued regarding what constitutes making rollover recommendations on a "regular basis" for purposes of determining when a financial professional serves as a fiduciary under ERISA and the Internal Revenue Code, and regarding the documentation and investigation requirements that apply when making rollover recommendations. The ASA alleged that the DOL violated the Administrative Procedures Act in issuing the guidance.

In February 2023, the Florida federal court struck down the DOL's guidance regarding when rollover recommendation advice is considered to be on a "regular basis," but upheld the DOL's guidance on the documentation and investigation requirements.

In June 2023, a federal magistrate judge in the FACC case concluded that the DOL's new interpretation that a single rollover "can be the beginning of an ongoing advice relationship" to Title II plans, inclusion of potential "future, ongoing relationships" to Title II plans, and conclusion that "an ongoing advisory relationship spanning both the Title I Plan and the IRA satisfies the regular basis prong" exceed the DOL's authority under ERISA and constitute arbitrary and capricious interpretations of the five-part test for defining an investment advice fiduciary. The magistrate judge recommended that the federal court vacate the portions of PTE 2020-02's text and preamble that allow consideration of Title II investment advice relationships when determining Title I fiduciary status.

On September 8, 2023, the DOL submitted a new rule proposal to the White House Office of Management and Budget for review pursuant to E.O 12866. The text of the proposal is not made public while it is under review by OMB. Review by OMB could take anywhere from 60 to 90 days, and based on its review, OMB will determine whether to (a) clear the proposal for issuance with or without changes, (b) return the proposal to DOL for reconsideration or further study, or (c) encourage DOL to withdraw the proposal.

NAIC Suitability in Annuity Transactions Model Regulation

The NAIC adopted its Suitability in Annuity Transactions Model Regulation (#275) (the "Suitability Model") to set standards to ensure the suitability of an annuity recommendation. The Suitability Model also requires insurers to establish a system to supervise annuity recommendations. The Suitability Model was originally adopted in 2003 and has since been revised on multiple occasions (2006, 2010, 2015, 2020). As of this writing, the current version has been adopted in 40 states.

New York adopted its own enhanced annuity sales practice rules prior to the adoption of the revised Suitability Model. The First Amendment to Insurance Regulation 187 (Regulation 187) became effective in August 2019 with respect to annuities and in February 2020 with respect to life insurance. Lawsuits in New York challenging the legality of Regulation 187 were filed in 2018. The consolidated lawsuits alleged, among other things, that Regulation 187 imposes a vague standard and fails to instruct agents/brokers whose best interest they must consider, e.g., the policyholder, beneficiary, or owner of a policy. The consolidated lawsuits were dismissed in August 2019. The plaintiffs appealed the decision and on April 29, 2021, the Appellate Division of the New York State Supreme Court reversed on grounds that Regulation 187 was unconstitutionally vague. The New York Department of Financial Services (DFS) appealed the

decision overturning Regulation 187 to the New York Court of Appeals, the state's highest court. In October 2022, the Court of Appeals reversed the Appellate Division's decision, finding that the DFS appropriately exercised its authority to create a carefully considered and clear regulation" and that there was no basis to invalidate the regulation.

In February 2020, NAIC members approved revisions to the Suitability Model that require producers to act in the "best interest of the consumer when making a recommendation of an annuity." As before, the revised Suitability Model requires insurers to establish and maintain a system to supervise annuity recommendations, but with the goal of "effectively" and not merely "appropriately" addressing the insurance needs and financial objectives of consumers at the time of the transaction. The new best interest obligation explicitly prohibits the producer from putting the financial interests of the producer or the insurer ahead of the consumer's interest. At the same time, the revised Suitability Model provides, among other things, that the Model does not subject the producer to civil liability under the best interest standard of care or under standards applicable to fiduciaries.

The revised Suitability Model provides that a producer will have acted in the best interest of the consumer if the producer satisfies certain prescribed obligations regarding care, disclosure, conflict of interest, and documentation. Notably, these obligations correspond to the four component obligations under Reg BI. To avoid the imposition of duplicative requirements on any particular transaction, the revised Suitability Model includes a safe harbor provision that treats recommendations and sales of annuities that are made in compliance with "comparable standards" (defined to include Reg BI, the fiduciary standard imposed on registered investment advisers under the Advisers Act, and the fiduciary standard imposed on providers of investment advice under ERISA) as satisfying the requirements of the Model. Under the revised Suitability Model, the best interest obligation applies to "every producer who has exercised material control or influence in the making of a recommendation and has received direct compensation as a result of the recommendation or sale" regardless of whether the producer had direct contact with the consumer. The best interest obligation does not apply to activities such as providing product wholesaling and other back-office support, providing or delivering marketing or educational materials, or providing general supervision of a producer, who do not themselves constitute material control or influence.

Until the revised Suitability Model is adopted in a state, the requirements of the existing Suitability Model, as adopted in that state, will continue to apply. The requirements of the existing Suitability Model are discussed below along with some differences with the revised Suitability Model.

The Suitability Model is similar to Financial Industry Regulatory Authority (FINRA) requirements governing the suitability of variable annuity transactions, which are described below. The pre-2020 versions of the Suitability Model provided a safe harbor under which compliance with FINRA requirements on suitable recommendations and supervision of producers is deemed to satisfy the similar requirements of the Suitability Model. As noted above, the revised Suitability Model expanded this safe harbor to a broader range of comparable standards.

Among other things, the pre-2020 versions of the Suitability Model required an insurance producer, when making a recommendation to a consumer to purchase or exchange an annuity, to make reasonable efforts to obtain "suitability information," such as the consumer's age, annual income, financial objectives, and risk tolerance, that is "reasonably appropriate" to determine the suitability of the recommendation. The revised Suitability Model requires the producer to "exercise reasonable diligence, care and skill" to "know the consumer's financial situation, insurance needs and financial objectives" and to make reasonable efforts to obtain "consumer profile information" before making an annuity recommendation. The consumer profile information

is a prescribed list of at least 14 factors, including many factors in the existing Suitability Model. The revised Suitability Model also requires the producer to make a reasonable inquiry into available recommendation options and to understand them but does not require the producer to consider products outside the scope of the producer's license or to consider other possible alternative products or strategies available in the market at the time of the recommendation.

The pre-2020 versions of the Suitability Model also required the insurance producer to have "reasonable grounds" for believing that the recommendation is suitable for the consumer based on the suitability information and other facts provided by the consumer. In addition, the insurance producer must have a "reasonable basis" for believing: that the consumer has been "reasonably informed" of the annuity's features; that the consumer would benefit from certain of those features; that the annuity as a whole, the underlying investment options selected by the consumer, and any riders or similar product enhancements are suitable for the consumer; and in the case of an exchange or replacement of an annuity, the exchange or replacement is suitable. If no insurance producer is involved, these requirements apply to the insurer. The revised Suitability Model requires the producer to have a reasonable basis to believe that a recommended product "effectively addresses the consumer's financial situation, insurance needs and financial objectives over the life of the product" in light of the consumer's profile information.

The revised Suitability Model also requires the producer to disclose certain information to the consumer prior to the recommendation or sale of an annuity, including a description of the scope and terms of the producer's relationship with the consumer, the producer's role in the transaction, and the way the producer is compensated, among other things. Similar to the pre-2020 versions of the Suitability Model, under the revised Suitability Model, the producer must have a reasonable basis for believing that the consumer has been "informed" (rather than "reasonably informed") of various features of the annuity, and that the consumer "would benefit from certain features of the annuity, such as annuitization, death or living benefits or other insurance-related features." The revised Suitability Model does not require the recommendation of the annuity "with the lowest one-time or multiple occurrence compensation structure" nor does it impose an ongoing monitoring obligation on the producer. The revised Suitability Model requires the producer to document in writing any recommendation covered by the Model and the basis for the recommendation, and, if the consumer refuses to provide consumer profile information or wishes to proceed with a non-recommended annuity transaction, to obtain the consumer's signed statement to that effect. The revised Suitability Model requires a 60-month rather than a 36-month look-back on whether the consumer has had an annuity exchange or replacement.

The pre-2020 versions of the Suitability Model also required insurers to establish a supervisory system that is "reasonably designed" to achieve compliance with its requirements, including procedures for reviewing recommendations before issuing an annuity to ensure there is a "reasonable basis" to determine that the recommended annuity, as well as "reasonable procedures" for detecting recommendations that are not suitable. The revised Suitability Model prohibits an insurer from issuing an annuity that has been recommended to a consumer absent a "reasonable basis to believe the annuity would effectively address the particular consumer's financial situation, insurance needs and financial objectives based on the consumer's consumer profile information." In addition, the revised Suitability Model requires the insurer to establish and maintain reasonable procedures to "assess" whether the producer has provided information required by the Model to the consumer, to identify and address "suspicious consumer refusals to provide consumer profile information," and to identify and eliminate "sales contests, sales quotas, bonuses, and non-cash compensation that are based on sales of specific annuities within a limited period of time." The revised Suitability Model provides that the last requirement is "not intended to prohibit the receipt of health insurance, office rent, office support, retirement

benefits or other employee benefits by employees as long as those benefits are not based upon the volume of sales of a specific annuity within a limited period of time.”

The Suitability Model also imposes training requirements for producers. Specifically, it provides that producers may not solicit annuity sales unless they have adequate knowledge to recommend the product and comply with the insurer’s product-specific training standards. Insurers are required to provide producers with product-specific training and materials that explain all material features of its annuity products. Producers can rely on insurer-provided training and materials to meet this requirement. In addition, producers must complete a one-time, four-credit Continuing Education (CE) training course that is approved by the department of insurance and provided by a department of insurance-approved training provider. New producers cannot sell annuities until they complete this course. Existing producers must complete the training within six months. The revised Suitability Model imposes additional training obligations, including training on the appropriate standard of conduct and appropriate sales practices, and replacement and disclosure requirements under the revised Suitability Model.

To date, 40 states have adopted the revised Suitability Model, including Alabama, Alaska, Arizona, Arkansas, Colorado, Connecticut, Delaware, Florida, Georgia, Hawaii, Idaho, Illinois, Iowa, Kansas, Kentucky, Maine, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Montana, Nebraska, New Mexico, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Carolina, South Dakota, Tennessee, Texas, , Virginia, Washington, West Virginia, Wisconsin, and Wyoming.

State Fiduciary Regulations

Unlike investment advisers who owe a fiduciary duty to their clients, broker-dealers who sell annuities have historically been subject to a suitability standard under federal and state securities laws. Following the vacatur of the DOL Fiduciary Rule by the U.S. Court of Appeals for the Fifth Circuit in 2018, several states have pushed forward with their own regulations that impose, or would impose, a fiduciary duty on broker-dealers.

The Massachusetts Securities Division of the Office of the Secretary of the Commonwealth (“Division” or “Massachusetts Division”) proposed amendments to its securities regulations on December 13, 2019, to apply a fiduciary conduct standard to broker-dealers when making recommendations and providing investment advice to customers. On February 21, 2020, Massachusetts adopted the amendments, which deem the failure to adhere to a fiduciary standard to be a dishonest or unethical practice. The Massachusetts fiduciary standard became effective on March 6, 2020. In the first enforcement action of the Massachusetts fiduciary rule, the Enforcement Section of the Division (“Enforcement Section”) filed an administrative complaint on December 16, 2020 against Robinhood Financial, LLC (“Robinhood”), alleging that Robinhood had violated Massachusetts law and regulations “by aggressively marketing itself to Massachusetts investors without regard for the best interests of its customers and failing to maintain the infrastructure and procedures necessary to meet the demands of its rapidly growing customer base.” In response, on April 15, 2021, Robinhood sued William Galvin in his role as the Massachusetts Secretary, and the Division, on grounds that the Massachusetts fiduciary rule is “invalid under both Massachusetts and federal law.” On March 30, 2022, a Massachusetts Superior Court judge issued an order invalidating the Massachusetts fiduciary rule on grounds that the promulgation of the rule by the Secretary “was beyond his authority.” On August 25, 2023, the Massachusetts Supreme Judicial Court reversed the lower court’s decision in favor of Robinhood, concluding that the Secretary did not overstep his authority, that the fiduciary duty

rule does not override common law protections available to investors, that the Massachusetts Uniform Securities Act (MUSA) is not an impermissible delegation of legislative power, and that the rule is not preempted by the SEC's determination to impose a national "best interest" standard of care on broker-dealers.

Following the enactment of a fiduciary statute in 2017, Nevada issued a proposed fiduciary regulation and solicited comments on January 18, 2019, but has not yet adopted a final regulation. New Jersey released a proposed fiduciary regulation on April 15, 2019, but has not yet adopted a final rule. On April 14, 2020, the rulemaking process in New Jersey was temporarily paused under an executive order issued by Governor Phil Murphy until after 270 days after the public health emergency resulting from COVID-19 for rule proposals published in the New Jersey Register on or after April 15, 2019. On June 4, 2021, Governor Murphy signed an executive order terminating the public health emergency previously declared in 2020. Thereafter, on December 24, 2021, the New Jersey Bureau of Securities announced that it will not adopt the 2019 fiduciary rule proposal "in light of developments in the securities industry since the proposal was first announced" and the proposal expired on January 1, 2022.

In Maryland, a bill was introduced in the state senate on February 4, 2019, that would impose a fiduciary duty on broker-dealers and empower the Maryland commissioner of financial regulation to adopt fiduciary duty regulations. The Maryland Senate Finance Committee overwhelmingly voted to reject the fiduciary bill on April 4, 2019.

Other Annuity Sales Practices Rules Advertising

All states prohibit advertising that is misleading, deceptive, or confusing, based on the overall impression that the advertisement may reasonably be expected to create upon a person of average intelligence within the segment of the public to which the advertisement is directed. In addition, states have adopted rules governing the general content of advertising and rules regarding specific types of advertising materials, such as illustrations.

SEC rules govern variable annuity advertising. Among other things, if past performance of a fund or variable annuity is presented, performance must be calculated according to standardized formulas. "Non-standardized" performance may also be shown but must be presented along with standardized performance. In addition, performance advertisements should include a toll-free (or collect) telephone number or a website where an investor may obtain total returns current to the most recent month end, unless the advertisement includes total returns current to the most recent month ended seven business days prior to date of the advertisement's use.

FINRA rules govern broker-dealer communications with the public about variable annuities. These rules impose principal approval, filing, and recordkeeping requirements on broker-dealer firms that disseminate retail communications about variable annuities.

Social Media

Both the SEC and FINRA, as well as state insurance regulators, have taken a keen interest in the use of social media by financial services firms, including insurance companies and insurance

producers. The SEC has issued guidance urging investors to use caution in using social media when considering an investment or establishing an account on a social media website, such as Facebook or Twitter, and identifying steps investors can take to protect themselves when using social media. The SEC also has issued guidance to financial services firms regarding their social media and social networking practices and has taken enforcement actions against firms that use social media in connection with violations of the Federal Securities laws.

Similarly, FINRA has issued regulatory notices that provide guidance to member firms and registered representatives on the application of FINRA rules governing communications with the public to the use of social media sites, including blogs and social networking sites. Among other things, these notices address responsibilities with respect to recordkeeping; suitability; third party posts, links, and content; interactive electronic forums; supervision; and personal communications and other devices. In addition, FINRA's Advertising Regulation Department has conducted a "spot check" of social media communications to determine how firms and their associated persons were using social media in the conduct of their businesses. Among other things, the spot check included reviewing written supervisory procedures regarding the production, approval, and distribution of social media communications, and steps firms were taking to monitor compliance with the firms' social media policies.

FINRA also has published guidance in the form of questions and answers on how its rules apply to various uses of social media in public communications, such as text messaging; hyperlinks and sharing; so-called "native advertising" in which the advertisement's content bears a similarity to the news, product reviews, and other material that surrounds it; and testimonials and endorsements. FINRA also has taken disciplinary action against member firms, principals, and representatives involving the use of websites and social media in the conduct of their businesses. These disciplinary actions involve allegations that cover several areas, including failure to supervise; failure to comply with advertising requirements; false, misleading, or inadequate disclosures; and failure to safeguard customer information.

Unfair Trade Practices

All states have adopted unfair trade practices acts with provisions that apply to an insurer's activities. These laws define and prohibit unfair methods of competition and unfair or deceptive business practices, including those involved with the issuance, sale, and administration of annuity contracts.

Annuity Disclosures

The NAIC Annuity Disclosure Model Regulation (#245) (the "Disclosure Model") requires that consumers be provided an Annuity Buyer's Guide and a disclosure document.

The current version of the Disclosure Model, which has been periodically revised, applies to fixed, fixed indexed, and variable annuities (except for non-registered variable annuities issued exclusively to accredited investors or qualified purchasers), while the previous version applied only to fixed and fixed indexed annuities.

The current version of the Disclosure Model also includes standards for fixed and fixed indexed annuity illustrations that require, among other things: a narrative summary (unless the information

is provided at the same time in a disclosure document); a numeric summary; for annuities with market value adjustment (MVA) features, a narrative explanation of the MVA, a demonstration of the MVA under at least one positive and one negative scenario, and actual MVA floors and ceilings; and for fixed indexed annuity illustrations, specific requirements on illustrating non-guaranteed values. The Disclosure Model also prohibits the illustration of indexes that have not been in existence for a least ten (10) years. While the Disclosure Model establishes these standards for the use of illustrations, it does not require that illustrations be provided. These illustration standards do not apply to variable annuity illustrations.

The NAIC adopted a new Buyer's Guide in 2013. The new Buyer's Guide is available in three alternate versions — one for fixed and fixed indexed annuities, one for variable annuities, and one for all deferred annuities — and can be delivered in print or electronically.

Recent Developments

SEC and FINRA Examination Priorities

On February 7, 2023, the SEC's Division of Examinations (previously known as the Office of Compliance Inspections and Examinations or OCIE) until December 2020) published its examination priorities for 2023. As in prior years, the 2023 priorities reflect a continuing focus on key areas of risk affecting retail investors as well as the intermediaries that interact with retail investors, the products marketed to retail investors, and the disclosures provided about fees and expenses as well as conflicts of interest.

Notably, SEC examinations of all regulated entities will continue to focus on, among other things: (a) cybersecurity and policies, procedures, governance practices, and responses to cyber-related incidents; (b) firms' practices to prevent account intrusions and safeguard customer records and information; and (c) crypto assets and emerging financial technologies, such as mobile apps, digital investment advice, and digital engagement practices.

Several new and significant topics have been added to the SEC's examination priorities for all regulated entities in 2023, including, among other things, compliance with (i) the recently adopted Advisers Act marketing rule; (ii) applicable standards of conduct including Reg BI for broker-dealers and fiduciary duty for investment advisers; (iii) Form CRS; and (iv) ESG-related advisory services and fund offerings.

Examinations of broker-dealers will focus on compliance and supervisory programs generally, including those relating to electronic communications relating to firm business; compliance with rules relating to the safeguarding of assets; and conflicts of interest in order routing and execution.

Investment adviser examinations will prioritize whether an adviser's operations and compliance practices have appropriately considered current market factors, including factors that might affect valuation and the accuracy of the adviser's regulatory filings, as well as an adviser's policies and procedures for retaining and monitoring electronic communications and selecting and using third party vendors.

For mutual funds and ETFs, examinations in 2023 will focus on assessing compliance programs, governance practices, disclosures to investors, and accuracy of reporting to the SEC. This includes the fiduciary obligations of investment advisers to registered investment companies,

fund board processes for evaluating and approving advisory and other fees; and the effectiveness of funds' derivative risk and liquidity risk management programs.

The SEC's 2023 priorities report refers to annuities only in the context of advice or recommendations regarding high cost and illiquid products.

On February 7, 2023, FINRA released its "2023 Report on FINRA's Examination and Risk Monitoring Program" ("2023 Report"). The 2023 Report describes itself as providing "firms with insights into findings from recent oversight activities of FINRA'S Member Supervision, Market Regulation and Enforcement Programs." The 2023 Report, according to FINRA, addresses a broader range of topics than in prior years, and introduces a new Financial Crimes Sections covering three topics: Anti-Money Laundering, Fraud and Sanctions; Cybersecurity and Technological Governance; and Manipulative Trading. The intent of the Report is to "be an up-to-date, evolving resource or library of information for firms" and builds on the prior year's report.

As in prior years, the 2023 Report includes a section on variable annuities. The 2023 Report cites one negative examination finding relating to variable annuities, which was the failure to ensure that recommendations involving variable annuities complied with Reg BI. Examples included not adequately collecting and retaining key information on variable annuity transactions, and not sufficiently training registered representatives and supervisors to determine whether variable annuity exchanges complied with the standards of Reg BI.

The 2023 Report also highlights several effective practices including, among others, using automated tools, exception reports, and surveillance to review variable annuity exchanges; requiring registered representatives to provide detailed written rationales for variable annuity transactions and principal verification of the information provided by registered representatives; standardizing review thresholds for rates of variable annuity exchanges and monitoring for emerging trends relating to representatives, customers, products, and branch offices; creating automated solutions to synthesize variable annuity data in situations warranted by the volume of transactions; engaging with insurance carriers and third-party data providers to address inconsistencies in available data, data formats, and reporting processes for variable annuities; and establishing a supervisory system that collects and uses key transaction data.

SEC Regulatory Proposals and Guidance

In 2023, several SEC rulemaking proposals from the prior year remain pending, including among others, proposals relating to ESG disclosures for investment advisers and investment companies, investment company names, the enhancement and standardization of climate-related disclosures for investors, and cybersecurity risk management for investment advisers and registered investment companies. The SEC did adopt several new rules and rule amendments, including, among others, amendments to Rule 2a-7 governing money markets (but without mandatory swing pricing, which had been contemplated in the proposing release), a new rule to enhance and standardize disclosures by public reporting companies regarding cybersecurity risk management, strategy, governance, and incidents; and rule amendments shortening the securities transaction settlement cycle to one business date after the trade date (T+1). The SEC also proposed several highly significant new rules and rule amendments in 2023, including, among others, a new Advisers Act rule regarding custody of assets; new rules designed to eliminate or neutralize the effects of certain conflicts associated with the use of predictive data analytics by broker-dealers and investment adviser; and rule amendments that would require broker-dealers, investment companies, and investment advisers to adopt policies

and procedures for incident response programs to address unauthorized access to or use of customer information.

Taxation of Annuities

This section explains the federal income taxation of annuities. The focus is on annuities that are not part of a qualified plan, although the basic differences between qualified and non-qualified annuities are discussed. State taxes and federal estate and gift taxes are not discussed; however, these taxes may also affect annuity owners.

Premiums

If an annuity contract is part of an employer-sponsored retirement plan, such as a 401(k), premiums are plan contributions and generally not includible in the employee's income when paid. However, if an annuity is used in a "Roth" type of arrangement, such as a Roth 403(b) annuity, the premiums are includible in income. Premiums paid for an IRA annuity may be deductible in whole or in part. For a non-qualified annuity, premiums are paid with after-tax monies and are not tax deductible.

Tax Deferral

Dividends, interest, and capital gains credited to an annuity are not taxed until they are withdrawn. In other words, earnings are tax deferred and reinvested to help accumulate assets for retirement. As a result, money may be transferred from one investment option to another inside a variable annuity without incurring a tax liability. This is not true for taxable investments, in which transferring amounts from one investment to another, such as from one mutual fund to another, will be treated as a sale and any gains will be taxable.

If a deferred annuity contract is not owned by an individual, but rather by an entity such as a corporation, the contract is not eligible for tax deferral in most cases. Rather, the entity is taxed each year on the increase in the net surrender value of the contract, minus premiums paid during the year. (Special rules allow trusts and other entities to own an annuity and still be eligible for tax deferral in certain circumstances.) Congress enacted this requirement to ensure that the tax deferral granted by annuities is used primarily as a vehicle for individuals' retirement savings.

Withdrawals

When a contract owner begins to receive money from an annuity, distributions taken in excess of the amount invested are subject to taxation at the owner's ordinary income tax rate. Just as with IRAs, 401(k) plans, and other tax-qualified plans, when money is withdrawn, it does not receive favorable capital gains treatment. As discussed below, however, annuity income payments receive more favorable tax treatment than lump sum payments or withdrawals. Also, unlike qualified plans, income payments under a non-qualified annuity can be deferred past age 73 and taken when the need arises.

Because Congress set the rules on tax deferral to encourage long-term retirement savings, withdrawals made before age 59½ may be subject to a 10 percent federal tax penalty on the taxable amount of earnings withdrawn, in addition to any income taxes due on that amount. (There are exceptions to the 10 percent penalty.) This is similar to the 10 percent penalty tax on premature distributions from IRAs and underscores the fact that annuities are designed to be long-term retirement vehicles. (There also may be surrender charges, as discussed in Chapter 4: Annuities 101, if the withdrawal exceeds any annual free-withdrawal amount or the surrender charge period has not run out. Surrender charges are imposed by the terms of the contract and should not be confused with the 10 percent federal tax penalty.)

For non-qualified annuity contracts, the tax rule on withdrawals is “interest and earnings first.” Under this rule, interest and earnings are considered withdrawn first for federal income tax purposes. For example, if someone invested \$25,000 in a fixed or variable annuity and the contract is now worth \$45,000, the first \$20,000 withdrawn is taxable. The remaining \$25,000 is not taxed because it is considered a return of principal. Withdrawals are taxed until all interest and earnings are withdrawn; the principal then can be withdrawn without tax.

The “interest and earnings first” rule is intended to encourage the use of annuities for long-term savings and retirement. Congress decided that the advantage of tax deferral should not be accompanied by the ability to withdraw principal first, with no tax payable until all principal is withdrawn. Different rules apply to tax-qualified annuities (such as IRAs), under which withdrawals are taxed on a pro rata basis to the extent there were any after-tax contributions made to the contract.

Complete Surrenders

When an owner surrenders an annuity contract, the excess of the amount received over the owner’s investment in the contract is taxable. Generally, the investment in the contract is the amount of premiums paid (less any principal that has been previously returned to the contract owner without tax) at the time of distribution.

Gifts and Assignments of Annuity Contracts

If a contract owner gives an annuity contract as a gift, the contract owner may have to pay income tax at the time of the transfer. The contract owner must include in income the difference between the cash surrender value of the contract and the owner’s investment in the contract at the time of the transfer. This rule does not apply if the transfer is made between spouses or former spouses as part of a divorce. (Gift taxes also may apply.)

In addition, any assignment or pledge of (or agreement to assign or pledge) any portion of an annuity contract’s cash surrender value is treated as a withdrawal of such amount from the contract. Hence, the tax treatment that normally applies to withdrawals also applies to assignments or pledges of annuity contracts.

Premature Distributions

For non-qualified annuities, a 10 percent federal tax penalty may apply to the taxable portion of an amount received before age 59½. There may be exceptions to the 10 percent penalty, for example, if the payment is made upon the owner's death or disability. As noted earlier, this penalty is intended to encourage the use of annuities for retirement savings purposes. For that reason, similar penalties generally apply to withdrawals from IRAs and qualified plans, which also are intended for retirement savings.

Taxation of Annuity Payouts

Annuity owners can elect several payout options, as discussed in Chapter 4: Annuities 101. The basic rule for annuity payouts (as distinguished from withdrawals or other non-periodic payments) is that the money a contract owner invests in the contract is returned in equal tax-free installments over the payment period. The remainder of the amount received each year is treated as the earnings on the owner's premiums and is included in income. The income portion is taxed at ordinary income tax rates, not capital gains rates. The total amount that is received tax-free can never exceed the premiums the owner paid for the contract.

The taxable portion of each payment is equal to the excess of the payment over the "exclusion amount." With a fixed annuity, the exclusion amount generally is computed by (1) dividing the premiums paid for the annuity by the total expected return from all scheduled annuity payments, and (2) multiplying each payment by this "exclusion ratio." With a variable annuity, because the expected return cannot be predicted, the exclusion amount is generally computed by dividing the premiums paid for the contract by the number of years that payments are expected to be made. For a lifetime annuity, the expected return is always computed by reference to the annuitant's life expectancy as determined using IRS tables.

To illustrate, assume that a male age 65 elects a lifetime annuity and his investment in the contract is \$100,000. Assume further that he has elected to receive annual variable annuity payments and the payment for the first year is \$8,000. Since the payments are variable, they will vary each year thereafter (for simplicity, this illustration assumes annual annuity payments, although monthly or quarterly payments are more common). Applicable IRS tables indicate that such a person is expected to live 20 years. The portion of each annuity payment excluded from income is \$5,000, which is \$100,000 divided by 20. During the first year, \$5,000 of the \$8,000 will be excluded from income and \$3,000 will be included and taxable. The \$5,000 is excluded each year until the total investment in the contract has been received.

It is important to note that these definitions and examples are specific to non-qualified annuities; that is, annuities purchased with pre-tax dollars. When annuities are purchased and held within a qualified account such as an IRA, withdrawals and annuitized payments are fully taxed at the federal and state tax rates applicable to ordinary income.

Partial Annuitizations

In some cases, the owner of a deferred annuity contract may wish to apply only a portion of the contract's cash value (rather than the entire cash value) to produce a series of annuity

payments under the contract, while leaving the contract's remaining cash value in the deferral or accumulation stage. For example, the owner's current financial need may be for annuity payments that are less than the payments the contract's full cash value would produce, or the owner may wish to "ladder" or "stagger" annuity payments to take advantage of future changes in annuity purchase rates. Prior to 2011, there was no specific rule in the tax code regarding such "partial annuitizations." Starting in 2011, however, the tax code provides that partial annuitizations of non-qualified annuities are treated the same as other annuitizations, as long as the resulting annuity payments are made for a period of at least 10 years or over the life or lives of one or more individuals. In such cases, the annuitized and non-annuitized portions of the contract are treated as separate contracts and the after-tax investment in the contract is allocated pro rata between them for purposes of applying the rules governing the taxation of distributions.

Death of an Owner

When an owner of an annuity dies, the general rule is that certain distributions must be made. (Similar rules apply to qualified plans.) The tax policy behind this rule is to prevent the prolonged deferral of income tax on the gains in an annuity contract that would occur if ownership could be passed from person to person without taxation occurring.

If an owner dies on or after the annuity commencement date, but before the entire interest in the contract has been distributed (e.g., if the owner dies five years into a 10-year guaranteed payout term), the remaining portion must be distributed at least as rapidly as under the method of distribution in effect at the time of death.

If an owner dies before the annuity commencement date, the general rule is that the entire interest in the contract must be distributed within five years after the date of the owner's death. Under this rule, a beneficiary has the following choices:

- Take the amount due under the contract and pay taxes at that time.
- Make withdrawals over the course of the next five years and pay taxes on each withdrawal, with the remainder of the contract value growing tax deferred.
- Wait up to five years with the contract value growing tax deferred, then take the entire amount due and pay taxes.

An exception to the five-year rule described above is available for cases in which payments are made to a beneficiary over life or life expectancy. Specifically, within 12 months of the owner's death, a beneficiary can (1) annuitize the remaining interest over his or her life or life expectancy and receive the favorable tax treatment accompanying annuity payments, or (2) begin withdrawals over a period not exceeding the beneficiary's life expectancy, calculated in a manner specified in IRS rules, and pay taxes on each withdrawal on an income-first basis.

For purposes of the foregoing after-death distribution rules, if an individual is the owner under a contract and the spouse is the beneficiary, then following the owner's death the surviving spouse is treated as the "owner" of the contract. In such case, the after-death distribution rules take effect upon the surviving spouse's death, rather than upon the original owner's death.

In the case of a non-natural owner (such as a corporation), the foregoing after-death distribution rules apply on the death of the primary annuitant.

Replacement Contracts/1035 Exchanges

When a contract owner purchases a new annuity contract to replace an existing one, the new contract is referred to as a replacement contract. Replacement contracts usually occur in connection with a tax-free exchange of non-qualified contracts under Section 1035 of the Internal Revenue Code, or because of a rollover or direct transfer of a qualified plan contract (e.g., an individual retirement annuity) from one life insurance company to another. Annuity owners generally can exchange their annuity contracts for new ones, tax free. In both qualified plans and non-qualified annuities, depending upon the terms of the contract, it also may be possible to transfer, tax-free, a portion of the contract to a new contract issued by the same or a different carrier, while continuing the remaining portion of the contract from which the partial transfer was taken. Special rules must be followed to assure that either a complete or a partial exchange or transfer qualifies for tax-free treatment.

The reasons for an exchange of annuity contracts can include:

- The owner has a fixed annuity with a substantially lower interest rate than other contracts currently available.
- The company that issued the current contract is not as financially strong as it was in the past.
- The new contract may have better features, such as an enhanced death benefit, guaranteed minimum income benefit, portfolio rebalancing, or dollar cost averaging.
- The new contract may have more or better-performing investment options.
- The new contract may have lower fees and charges.

Many states have passed regulations requiring certain procedures be followed before an annuity contract is replaced. The contract purchaser and the agent must sign a statement as to whether the contract being purchased will replace an existing one. If so, the new insurance company must promptly notify the old insurance company. The new insurance company must provide the purchaser with a prescribed statement about important factors to consider before buying the replacement contract. In some cases, a surrender charge may be incurred by exchanging the old contract and a new surrender charge period may start on the new contract. For this reason, an individual and his or her financial advisor should carefully evaluate a proposed exchange to ensure that it is in the contract owner's best interest. States have adopted replacement regulations ensuring full disclosure in these situations and affording other protections. States also may provide longer free-look periods for replacement contracts than for other annuity contracts.

Medicare Tax on Investment Income

Since 2013, distributions from non-qualified annuity contracts, to the extent not excludible from income, have generally been subject to the 3.8 percent Medicare tax on investment income for taxpayers with adjusted gross income (with certain modifications) over \$250,000 in the case of married couples filing jointly and qualifying widow(er)s with dependent children, \$125,000 in the case of married taxpayers filing separately, or \$200,000 in the case of other taxpayers.

Data Section

Total Annuity Market

Figure 15-1 Annuity Industry
Net Assets (dollars in billions)

Year	Variable	Fixed	Total
2002	777.4	421.0	1,198.4
2003	972.6	490.0	1,462.6
2004	1,165.9	510.0	1,675.9
2005	1,187.3	534.0	1,721.3
2006	1,386.6	519.0	1,905.6
2007	1,499.3	511.0	2,010.3
2008	1,129.4	556.0	1,685.4
2009	1,354.5	620.2	1,974.7
2010	1,504.4	658.6	2,163.0
2011	1,502.3	676.0	2,178.3
2012	1,639.9	691.6	2,331.5
2013	1,868.5	721.2	2,589.7
2014	1,920.4	747.1	2,667.5
2015	1,871.6	782.0	2,653.6
2016	1,896.7	827.5	2,847.2
2017	1,985.7	861.5	2,847.2
2018	1,814.3	902.3	2,716.6
2019	2,018.0	946.6	2,964.6
2020	2,105.8	983.5	3,089.3
2021	2,130.4	1,030.9	3,161.3
2022	1,703.0	1,122.7	2,825.7

Sources: Morningstar, Inc.; LIMRA Secure Retirement Institute

Figure 15-2 Annuity Industry
Total Sales (dollars in billions)

Year	Variable	Fixed	Total
2002	114.8	103.3	218.1
2003	126.1	84.1	210.2
2004	129.9	86.7	216.6
2005	133.4	76.5	209.9
2006	157.6	74.0	231.6
2007	183.4	66.6	250.0
2008	154.8	106.7	261.5
2009	125.6	104.2	229.8
2010	136.8	76.4	213.2
2011	154.6	75.6	230.2
2012	143.9	67.0	210.9
2013	142.1	78.1	220.2
2014	137.8	91.5	229.3
2015	131.1	98.4	229.5
2016	104.6	108.0	212.6
2017	96.2	97.8	194.0
2018	99.2	125.0	224.2
2019	98.3	129.5	227.8
2020	95.8	111.7	207.5
2021	122.1	114.1	236.2
2022	98.7	203.5	302.2

Sources: Beacon Research; Morningstar, Inc.

Figure 15-3 Annuity Industry Sales by Quarter

(dollars in billions)

Year	Variable	Fixed	Total
Q1 2005	31.7	18.8	50.5
Q2 2005	33.5	21.9	55.4
Q3 2005	33.8	18.4	52.2
Q4 2005	34.4	17.4	51.8
Total 2005	133.4	76.5	209.9
Q1 2006	38.3	17.4	55.7
Q2 2006	41.8	18.8	60.6
Q3 2006	37.1	20.5	57.6
Q4 2006	40.4	17.3	57.7
Total 2006	157.6	74.0	231.6
Q1 2007	41.3	14.1	55.4
Q2 2007	47.5	16.4	63.9
Q3 2007	46.5	18.1	64.6
Q4 2007	48.1	18.0	66.1
Total 2007	183.4	66.6	250.0
Q1 2008	41.7	19.6	61.3
Q2 2008	42.0	25.3	67.3
Q3 2008	37.8	27.7	65.5
Q4 2008	33.3	34.1	67.4
Total 2008	154.8	106.7	261.5
Q1 2009	30.5	34.8	65.3
Q2 2009	31.9	27.8	59.7
Q3 2009	31.1	22.1	53.2
Q4 2009	32.1	19.5	51.6
Total 2009	125.6	104.2	229.8
Q1 2010	31.5	17.9	49.3
Q2 2010	34.2	20.4	54.6
Q3 2010	33.9	20.5	54.4
Q4 2010	37.2	17.6	54.8
Total 2010	136.8	76.4	213.2
Q1 2011	39.0	18.6	57.6
Q2 2011	39.8	20.7	60.4
Q3 2011	38.9	19.0	57.9
Q4 2011	37.0	17.3	54.3
Total 2011	154.6	75.6	230.2
Q1 2012	35.9	16.9	52.8
Q2 2012	37.9	17.2	55.1
Q3 2012	36.0	16.6	52.6
Q4 2012	34.1	16.2	50.3
Total 2012	143.9	67.0	210.9
Q1 2013	34.4	15.0	49.4
Q2 2013	37.1	17.1	54.2
Q3 2013	34.9	22.5	57.4
Q4 2013	35.6	23.5	59.1
Total 2013	142.1	78.1	220.2
Q1 2014	33.5	22.5	56.0
Q2 2014	35.6	24.3	59.9
Q3 2014	35.2	21.7	56.9
Q4 2014	33.6	23.0	56.6
Total 2014	137.8	91.5	229.3
Q1 2015	32.1	20.9	53.0
Q2 2015	35.8	22.8	58.6
Q3 2015	32.2	26.5	58.7
Q4 2015	31.1	28.2	59.3
Total 2015	131.1	98.4	229.5
Q1 2016	26.5	29.6	56.2
Q2 2016	27.0	29.1	56.2
Q3 2016	26.0	25.7	51.7
Q4 2016	25.0	23.5	48.5
Total 2016	104.6	108.0	212.6

Figure 15-3 Annuity Industry Sales by Quarter

(dollars in billions)

Year	Variable	Fixed	Total
Q1 2017	24.4	25.2	49.6
Q2 2017	24.8	26.1	50.9
Q3 2017	21.9	22.6	44.5
Q4 2017	25.0	23.9	48.9
Total 2017	96.2	97.8	194.0
Q1 2018	24.5	25.5	50.0
Q2 2018	25.7	31.8	57.5
Q3 2018	24.6	31.9	56.4
Q4 2018	24.5	35.9	60.3
Total 2018	99.2	125.0	224.2
Q1 2019	21.9	35.9	57.8
Q2 2019	24.9	35.8	60.7
Q3 2019	25.6	30.1	55.7
Q4 2019	25.9	27.7	53.6
Total 2019	98.3	129.5	227.8
Q1 2020	25.0	27.6	52.6
Q2 2020	20.4	26.5	46.9
Q3 2020	23.3	30.2	53.5
Q4 2020	27.1	27.4	54.5
Total 2020	95.8	111.7	207.5
Q1 2021	29.2	27.5	56.7
Q2 2021	31.5	30.8	62.3
Q3 2021	29.7	28.0	57.7
Q4 2021	31.7	27.8	59.5
Total 2021	122.1	114.1	236.2
Q1 2022	25.5	33.9	59.4
Q2 2022	23.8	50.6	74.4
Q3 2022	23.5	54.3	77.8
Q4 2022	25.9	64.7	90.6
Total 2022	98.7	203.5	302.2

Sources: Beacon Annuity Solutions; Morningstar, Inc.

Figure 15-4 Annuity Industry Net Assets – Qualified Versus Non-Qualified

(dollars in billions)

Year	Qualified			Non-Qualified			Total
	Variable	Fixed	Total	Variable	Fixed	Total	
2002	445.6	167.0	612.6	331.8	254.0	585.8	1,198.4
2003	569.2	201.0	770.2	403.4	289.0	692.4	1,462.6
2004	705.5	208.0	913.5	460.4	302.0	762.4	1,675.9
2005	736.1	214.0	950.1	451.2	320.0	771.2	1,721.3
2006	847.3	225.0	1,072.3	539.3	312.0	851.3	1,923.6
2007	925.4	211.0	1,136.4	573.9	300.0	873.9	2,010.3
2008	739.1	242.0	981.1	390.3	314.0	704.3	1,685.4
2009	969.5	272.0	1,241.5	385.0	348.0	733.0	1,974.5
2010	1,036.7	297.0	1,333.7	467.7	362.0	829.7	2,163.4
2011	1,012.5	315.0	1,327.5	489.8	360.0	849.8	2,177.3
2012	1,099.3	325.0	1,424.3	540.6	367.0	907.6	2,331.9
2013	1,220.8	346.0	1,566.8	647.7	376.0	1,023.7	2,590.5
2014	1,253.3	363.6	1,616.9	667.1	395.0	1,062.1	2,679.0
2015	1,235.8	385.1	1,620.9	635.8	418.8	1,054.6	2,675.5
2016	1,311.5	409.2	1,720.7	585.2	445.0	1,030.2	2,750.9
2017	1,373.1	433.3	1,806.4	612.6	471.1	1,083.7	2,890.1
2018	1,175.7	484.9	1,660.6	638.6	417.4	1,056.0	2,716.6
2019	1,307.7	530.1	1,837.8	710.3	416.5	1,126.8	2,964.6
2020	1,354.0	759.6	2,113.6	751.8	223.9	975.7	3,089.3
2021	1,427.4	784.2	2,211.6	703.0	246.7	949.7	3,161.3
2022	1,158.0	617.5	1,775.5	545.0	505.2	1,050.2	2,825.7

Sources: Morningstar, Inc. (Variable); LIMRA Secure Retirement Institute (Fixed)

Figure 15-5 Annuity Total Sales – Qualified Versus Non-Qualified

(dollars in billions)

Year	Qualified			Non-Qualified			Total
	Variable	Fixed	Total	Variable	Fixed	Total	
2003	73.8	30.0	103.8	52.3	54.2	106.5	210.3
2004	78.6	31.1	109.7	51.3	55.6	106.9	216.6
2005	82.7	28.6	111.3	50.7	47.9	98.6	209.9
2006	96.3	27.6	123.9	61.3	46.4	107.7	231.6
2007	113.2	22.0	135.2	70.2	44.6	114.8	250.0
2008	101.3	41.6	142.9	53.5	65.1	118.6	261.5
2009	89.9	43.7	133.6	35.7	60.5	96.2	229.8
2010	94.2	34.2	128.4	42.7	42.2	84.9	213.3
2011	104.1	33.6	137.7	50.5	42.0	92.5	230.2
2012	96.1	34.8	130.9	47.8	32.2	80.0	210.9
2013	92.8	39.2	132.0	49.3	38.9	88.2	220.2
2014	89.9	50.9	140.8	47.9	40.6	88.5	229.3
2015	86.7	56.7	143.3	44.4	41.7	86.2	229.5
2016	72.9	61.9	134.9	31.7	46.1	77.7	212.6
2017	63.4	53.9	117.3	32.8	43.9	76.7	194.0
2018	66.1	69.7	135.7	33.1	55.3	88.5	224.2
2019	62.8	75.7	138.5	35.5	53.8	89.3	227.8
2020	61.6	58.9	120.5	34.2	52.8	87.0	207.5
2021	74.1	59.0	133.1	48.0	55.1	103.1	236.2
2022	69.1	111.9	181.0	29.6	91.6	121.2	302.2

Sources: Beacon Annuity Solutions; Morningstar, Inc.

Figure 15-6 Annuity Industry Total Sales – Deferred Versus Immediate

(dollars in billions)

Year	Deferred	Immediate	Total
2003	205.2	5.2	210.3
2004	210.1	6.5	216.6
2005	203.0	6.9	209.9
2006	224.5	7.1	231.6
2007	243.1	7.0	250.0
2008	252.4	9.0	261.5
2009	221.8	7.9	229.8
2010	205.1	8.1	213.2
2011	221.7	8.5	230.2
2012	201.7	9.2	210.9
2013	209.2	11.0	220.2
2014	216.2	13.1	229.3
2015	216.9	12.6	229.5
2016	200.1	12.5	212.6
2017	183.4	10.6	194.0
2018	212.7	11.5	224.2
2019	215.9	11.9	227.8
2020	200.1	7.4	207.5
2021	229.1	7.1	236.2
2022	290.9	11.1	302.2

Sources: Beacon Annuity Solutions; Morningstar, Inc.

Figure 15-7 Annuity Industry Total Sales – Product Type

(dollars in billions)

Year	Group VA	VA GLWB	Fee Based	RILA	IOVA	Fixed BV	Fixed MVA	FIA	Income	Total
2011	14.0	136.3	3.8	0.5	0.0	28.1	6.0	33.0	8.5	230.2
2012	14.7	121.8	4.7	1.4	1.4	18.8	4.8	34.2	9.2	210.9
2013	14.5	115.9	5.8	1.8	4.1	21.7	6.7	38.7	11.0	220.2
2014	13.3	111.7	5.9	1.8	5.1	20.8	9.8	47.9	13.0	229.3
2015	13.5	103.0	6.0	3.7	4.8	20.2	11.1	54.6	12.5	229.5
2016	13.8	75.4	5.3	7.3	2.8	20.9	16.0	58.8	12.3	212.6
2017	13.1	64.7	6.8	9.1	2.6	20.6	12.4	54.3	10.5	194.0
2018	11.6	67.5	6.8	11.2	2.2	27.9	15.9	69.8	11.4	224.2
2019	11.1	62.2	5.8	17.4	1.9	25.2	19.9	72.5	11.9	227.8
2020	9.9	56.3	5.7	22.0	1.9	24.4	24.5	55.4	7.4	207.5
2021	9.5	61.5	10.2	38.4	2.5	24.5	22.4	60.2	7.0	236.2
2022	9.6	44.9	5.4	36.4	2.4	59.5	53.0	79.7	11.3	302.2

Sources: Beacon Annuity Solutions; Morningstar, Inc.

Analyst Note: GLWB = Guaranteed Lifetime Withdrawal Benefit; RILA = Registered Index-Linked Annuity; IOVA = Investment Oriented Variable Annuity; BV = Book Value; MVA = Market Value Adjusted; FIA = Fixed Indexed Annuity

Figure 15-8 Annuity Total Sales Percentages by Distribution Channel

Year	Banks	Career Agents	Direct Response	Independent Broker Dealers	Independent Agents	Full Service Nat'l BDs	Regional Broker/Dealers
2003	25.7%	24.4%	1.5%	18.8%	13.7%	8.1%	7.8%
2004	23.7%	24.7%	1.5%	19.8%	15.9%	6.9%	7.6%
2005	19.9%	27.0%	1.7%	20.3%	16.8%	7.1%	7.3%
2006	18.3%	25.8%	2.0%	24.3%	14.8%	8.1%	6.6%
2007	16.9%	24.6%	2.2%	27.2%	13.3%	9.0%	6.9%
2008	20.5%	23.9%	2.6%	23.0%	15.5%	7.9%	6.6%
2009	19.9%	25.1%	2.2%	22.0%	16.6%	7.0%	7.1%
2010	15.8%	25.5%	2.5%	23.1%	18.2%	6.8%	8.2%
2011	16.5%	24.7%	2.1%	24.1%	15.5%	7.7%	9.5%
2012	14.4%	26.2%	2.7%	24.1%	16.8%	7.6%	8.2%
2013	16.3%	25.4%	2.9%	23.5%	16.8%	7.1%	8.1%
2014	16.8%	23.6%	2.6%	25.1%	16.9%	6.9%	8.0%
2015	17.8%	24.8%	2.2%	23.6%	17.3%	5.8%	8.5%
2016	18.1%	24.6%	2.2%	22.0%	19.8%	4.9%	8.3%
2017	18.2%	23.0%	2.5%	23.5%	19.2%	4.9%	8.7%
2018	18.9%	20.6%	2.8%	23.9%	20.2%	4.6%	9.0%
2019	18.1%	20.4%	2.9%	24.4%	20.3%	4.7%	9.2%
2020	18.2%	19.7%	3.5%	25.9%	18.5%	4.3%	9.9%
2022	23.7%	17.4%	5.0%	20.5%	19.6%	2.8%	11.0%

Sources: Beacon Annuity Solutions; Morningstar, Inc.

Figure 15-9 2022 Annuity Total Sales by Top 25 Issuers

Company	Total Flow (\$MM)	Rank	% Share	Cumulative % Share
New York Life	24,393.9	1	8.1%	8.1%
Athene	20,408.7	2	6.8%	14.8%
Massachusetts Mutual	20,154.7	3	6.7%	21.5%
Corebridge Financial	18,650.2	4	6.2%	27.7%
Jackson National	15,053.8	5	5.0%	32.6%
Allianz Life	14,140.6	6	4.7%	37.3%
Equitable	13,880.5	7	4.6%	41.9%
Lincoln National	12,097.5	8	4.0%	45.9%
Brighthouse Financial	10,943.2	9	3.6%	49.5%
Pacific Life	9,798.1	10	3.2%	52.8%
Global Atlantic	9,430.6	11	3.1%	55.9%
F & G Life	8,294.8	12	2.7%	58.7%
Sammons Financial Group	8,261.4	13	2.7%	61.4%
TIAA	7,563.1	14	2.5%	63.9%
Western Southern	6,304.3	15	2.1%	66.0%
Symetra Financial	6,124.8	16	2.0%	68.0%
Prudential	6,018.8	17	2.0%	70.0%
Nassau	5,940.9	18	2.0%	72.0%
Nationwide	5,366.5	19	1.8%	73.7%
USAA	5,236.9	20	1.7%	75.5%
Security Benefit	4,497.2	21	1.5%	77.0%
American Equity	3,321.1	22	1.1%	78.1%
Thrivent Financial	3,163.7	23	1.0%	79.1%
RiverSource	2,888.2	24	1.0%	80.1%
Delaware Life	2,488.0	25	0.8%	80.9%

Sources: Beacon Annuity Solutions; Morningstar, Inc.

Variable Annuity Market

Figure 15-10 Annual VA Net Flow, Total Sales and Net Assets (dollars in billions)

Year	Net Flow	Total Sales	Net Assets
2002	30.7	114.8	777.4
2003	46.0	126.1	972.6
2004	40.2	129.9	1,165.9
2005	20.4	133.4	1,187.3
2006	29.7	157.6	1,386.6
2007	33.4	183.4	1,499.3
2008	23.8	154.8	1,129.4
2009	17.0	125.6	1,354.5
2010	21.6	136.8	1,504.4
2011	27.7	154.6	1,502.3
2012	14.7	143.9	1,639.9
2013	1.3	142.1	1,868.5
2014	-5.4	137.8	1,920.4
2015	-12.9	131.1	1,871.6
2016	-32.0	104.6	1,896.7
2017	-66.7	96.2	1,985.7
2018	-79.2	99.2	1,814.3
2019	-90.3	98.3	2,018.0
2020	-75.9	95.8	2,105.8
2021	-86.4	122.1	2,130.4
2022	-81.8	98.7	1,703.0

Source: Morningstar, Inc.

Figure 15-11 Quarterly VA Net Flow, Total Sales and Net Assets (dollars in billions)

Year	Net Sales	Total Sales	Net Assets
Q1 2005	4.8	31.7	1,108.5
Q2 2005	5.2	33.5	1,138.7
Q3 2005	4.6	33.8	1,191.4
Q4 2005	5.8	34.4	1,187.3
Total 2005	20.4	133.4	
Q1 2006	7.0	38.3	1,300.5
Q2 2006	8.2	41.8	1,271.9
Q3 2006	9.3	37.1	1,309.4
Q4 2006	5.2	40.4	1,386.6
Total 2006	29.7	157.6	
Q1 2007	6.4	41.3	1,409.8
Q2 2007	8.7	47.5	1,476.6
Q3 2007	9.4	46.5	1,515.2
Q4 2007	8.9	48.1	1,499.3
Total 2007	33.4	183.4	
Q1 2008	7.2	41.7	1,413.6
Q2 2008	7.5	42.0	1,425.1
Q3 2008	4.9	37.8	1,303.1
Q4 2008	4.2	33.3	1,129.4
Total 2008	23.8	154.8	
Q1 2009	5.2	30.5	1,067.9
Q2 2009	6.1	31.9	1,185.6
Q3 2009	2.8	31.1	1,311.2
Q4 2009	2.9	32.1	1,354.5
Total 2009	17	125.6	
Q1 2010	3.6	31.5	1,397.8
Q2 2010	6.2	34.2	1,319.6
Q3 2010	6.4	33.9	1,418.0
Q4 2010	5.4	37.2	1,504.4
Total 2010	21.6	136.8	

Figure 15-11 Quarterly VA Net Flow, Total Sales and Net Assets

(dollars in billions)

Year	Net Sales	Total Sales	Net Assets
Q1 2011	5.8	39.0	1,558.0
Q2 2011	5.8	39.8	1,567.3
Q3 2011	8.9	38.9	1,421.7
Q4 2011	7.2	37.0	1,502.3
Total 2011	27.7	154.6	
Q1 2012	3.8	35.9	1,610.9
Q2 2012	4.9	37.9	1,559.3
Q3 2012	5.8	36.0	1,621.9
Q4 2012	0.1	34.1	1,639.9
Total 2012	14.7	143.9	
Q1 2013	0.9	34.4	1,715.9
Q2 2013	1.6	37.1	1,716.4
Q3 2013	1.6	34.9	1,787.0
Q4 2013	-2.8	35.6	1,868.5
Total 2013	1.3	142.1	
Q1 2014	-1.2	33.5	1,882.1
Q2 2014	1.6	35.6	1,934.8
Q3 2014	-2.5	35.2	1,903.3
Q4 2014	-3.3	33.6	1,920.4
Total 2014	-5.4	137.8	
Q1 2015	-3.5	32.1	1,947.2
Q2 2015	2.9	35.8	1,982.5
Q3 2015	-7.1	32.2	1,841.0
Q4 2015	-5.2	31.1	1,871.6
Total 2015	-12.9	131.1	
Q1 2016	-9.8	26.5	1,874.7
Q2 2016	-5.6	27.0	1,880.2
Q3 2016	-10.8	26.0	1,921.0
Q4 2016	-5.8	25.0	1,896.7
Total 2016	-32.0	104.6	
Q1 2017	-17.8	24.4	1,941.2
Q2 2017	-14.8	24.8	1,985.2
Q3 2017	-15.9	21.9	1,958.0
Q4 2017	-18.2	25.0	1,985.7
Total 2017	-66.7	96.2	
Q1 2018	-18.4	24.4	1,953.2
Q2 2018	-21.1	25.7	1,967.2
Q3 2018	-19.4	24.5	2,004.4
Q4 2018	-20.3	24.4	1,814.3
Total 2018	-79.2	99.1	
Q1 2019	-24.8	21.9	1,932.4
Q2 2019	-20.4	24.9	1,960.9
Q3 2019	-21.5	25.6	1,946.5
Q4 2019	-23.6	25.9	2,018.0
Total 2019	-90.3	98.3	
Q1 2020	-20.2	25.0	1,704.7
Q2 2020	-13.6	20.4	1,887.1
Q3 2020	-18.0	23.3	1,952.3
Q4 2020	-24.1	27.1	2,105.8
Total 2020	-75.9	95.8	
Q1 2021	-24.8	29.2	2,104.1
Q2 2021	-18.5	31.5	2,079.8
Q3 2021	-20.8	29.7	2,069.7
Q4 2021	-22.3	31.7	2,130.4
Total 2021	-86.4	122.1	
Q1 2022	-21.9	28.1	1,998.3
Q2 2022	-17.2	26.2	1,683.6
Q3 2022	-17.6	23.2	1,664.7
Q4 2022	-25.1	21.2	1,703.0
Total 2022	-81.8	98.7	

Source: Morningstar, Inc.

Figure 15-12 Variable Annuity Net Assets - Qualified Versus Non-Qualified (dollars in billions)

Year	Qualified	Non-Qualified	Total
2002	445.6	331.8	777.4
2003	569.2	403.4	972.6
2004	705.5	460.4	1,165.9
2005	736.1	451.2	1,187.3
2006	847.3	539.3	1,386.6
2007	925.4	573.9	1,499.3
2008	739.1	390.3	1,129.4
2009	969.5	385.0	1,354.5
2010	1,036.7	467.7	1,504.4
2011	1,012.5	489.8	1,502.3
2012	1,099.3	540.6	1,639.9
2013	1,220.8	647.7	1,868.5
2014	1,253.3	667.1	1,920.4
2015	1,235.8	635.8	1,871.6
2016	1,311.5	585.2	1,896.7
2017	1,373.1	612.6	1,985.7
2018	1,175.7	638.6	1,814.3
2019	1,307.7	710.3	2,018.0
2020	1,263.5	842.3	2,105.8
2021	1,278.2	852.2	2,130.4
2022	1,158.0	545.0	1,703.0

Source: Morningstar, Inc.

Figure 15-13 Variable Annuity Total Sales - Qualified Versus Non-Qualified (dollars in billions)

Year	Qualified	Non-Qualified	Total
2002	65.8	49.0	114.8
2003	73.8	52.3	126.1
2004	78.6	51.3	129.9
2005	82.7	50.7	133.4
2006	96.3	61.3	157.6
2007	113.2	70.2	183.4
2008	101.3	53.5	154.8
2009	89.9	35.7	125.6
2010	94.2	42.7	136.9
2011	104.1	50.5	154.6
2012	96.1	47.8	143.9
2013	92.8	49.3	142.1
2014	89.9	47.9	137.8
2015	86.7	44.4	131.1
2016	72.9	31.7	104.6
2017	63.4	32.8	96.2
2018	66.1	33.1	99.2
2019	62.8	35.5	98.3
2020	61.6	34.2	95.8
2021	74.1	48.0	122.1
2022	68.0	30.7	98.7

Source: Morningstar, Inc.

Figure 15-14 Variable Annuity Total Sales - Deferred Versus Immediate (dollars in billions)

Year	Deferred	Immediate	Total
2002	114.3	0.5	114.8
2003	125.9	0.5	126.4
2004	129.5	0.4	129.9
2005	132.8	0.6	133.4
2006	156.8	0.8	157.6
2007	183.1	0.3	183.4
2008	154.4	0.4	154.8
2009	125.5	0.1	125.6
2010	136.8	0.1	136.9
2011	154.6	0.0	154.6
2012	143.9	0.0	143.9
2013	142.1	0.0	142.1
2014	137.7	0.1	137.8
2015	131.0	0.1	131.1
2016	104.5	0.1	104.6
2017	96.1	0.1	96.2
2018	99.1	0.1	99.2
2019	98.2	0.1	98.3
2020	95.7	0.1	95.8
2021	122.0	0.1	122.1
2022	98.6	0.1	98.7

Source: Morningstar, Inc.

Figure 15-15 Variable Annuity Total Sales – Product Type (dollars in billions)

Year	Group VA	VA GLWB	Fee Based	RILA	IOVA	Total
2011	14.0	136.3	3.8	0.5	0.0	154.6
2012	14.7	121.8	4.7	1.4	1.4	143.9
2013	14.5	115.9	5.8	1.8	4.1	142.1
2014	13.3	111.7	5.9	1.8	5.1	137.8
2015	13.5	103.0	6.0	3.7	4.8	131.1
2016	13.8	75.4	5.3	7.3	2.8	104.6
2017	13.1	64.7	6.8	9.1	2.6	96.2
2018	11.6	67.5	6.8	11.2	2.2	99.2
2019	11.1	62.2	5.8	17.4	1.9	98.3
2020	9.9	56.3	5.7	22.0	1.9	95.8
2021	9.5	61.5	10.2	38.4	2.5	122.1
2022	9.6	44.9	5.4	36.4	2.4	98.7

Sources: Beacon Annuity Solutions; Morningstar, Inc.

Figure 15-16 Variable Annuity Total Sales by Distribution Channel

(dollars in billions)

Year	Captive Agents	Independent NASD	Banks/ Credit Unions	Wirehouses	Regional Investment Firms	Direct Response	Total
2002	40.7	29.9	12.7	15.0	15.1	1.4	114.8
2003	41.6	37.3	17.2	15.7	13.2	1.1	126.1
2004	43.1	41.1	17.4	13.9	13.4	1.0	129.9
2005	47.0	40.9	17.3	13.9	13.0	1.3	133.4
2006	49.8	53.9	20.9	17.0	13.1	2.9	157.6
2007	53.5	65.6	24.1	21.0	15.4	3.8	183.4
2008	47.9	54.6	18.5	18.0	12.6	3.2	154.8
2009	41.8	44.8	12.6	14.0	10.2	2.2	125.6
2010	44.5	46.5	15.5	13.7	14.1	2.6	136.9
2011	48.1	51.9	17.8	16.4	17.8	2.6	154.6
2012	46.9	47.8	17.2	15.1	14.0	2.9	143.9
2013	45.9	48.4	17.7	14.7	12.1	3.3	142.1
2014	43.3	48.8	16.4	14.7	11.5	3.2	137.8
2015	44.1	44.3	16.5	11.7	11.1	3.4	131.1
2016	40.9	34.5	11.5	8.3	6.6	2.9	104.6
2017	36.3	35.0	9.1	7.1	5.4	3.2	96.2
2018	35.9	38.2	8.8	6.9	6.1	3.3	99.2
2019	34.5	39.2	9.2	6.6	6.0	2.8	98.3
2020	32.5	40.4	9.1	5.9	5.5	2.4	95.8
2021	37.1	54.0	12.0	7.0	7.7	4.3	122.1
2022	35.6	42.4	8.5	4.1	6.0	2.1	98.7

Source: Morningstar, Inc.

Figure 15-17 Variable Annuity Total Sales by Distribution Channel by Quarter (dollars in billions)

Year	Captive Agents	Ind. NASD	Banks/ Credit Unions	New York Wirehouses	Regional Investment Firms	Direct Response	Total
Q1 2005	11.4	9.6	4.2	3.1	3.2	0.3	31.8
Q2 2005	12.1	10.1	4.3	3.5	3.3	0.2	33.5
Q3 2005	11.5	10.6	4.4	3.6	3.3	0.3	33.7
Q4 2005	12.0	10.6	4.4	3.7	3.2	0.5	34.4
Total 2005	47.0	40.9	17.3	13.9	13.0	1.3	133.4
Q1 2006	12.3	12.5	5.1	4.6	3.2	0.6	38.3
Q2 2006	13.1	14.3	5.7	4.4	3.5	0.8	41.8
Q3 2006	11.9	13.1	4.8	3.6	3.0	0.7	37.1
Q4 2006	12.5	14.0	5.3	4.4	3.4	0.8	40.4
Total 2006	49.8	53.9	20.9	17.0	13.1	2.9	157.6
Q1 2007	12.8	14.6	5.5	4.1	3.4	0.9	41.3
Q2 2007	13.9	17.0	6.5	5.2	3.9	1.0	47.5
Q3 2007	12.9	17.3	6.0	5.3	4.1	0.9	46.5
Q4 2007	13.9	16.7	6.1	6.4	4.0	1.0	48.1
Total 2007	53.5	65.6	24.1	21.0	15.4	3.8	183.4
Q1 2008	12.2	14.8	5.4	4.9	3.3	1.1	41.7
Q2 2008	12.8	14.7	5.3	4.9	3.5	0.8	42.0
Q3 2008	11.7	13.2	4.4	4.6	3.2	0.7	37.8
Q4 2008	11.2	11.9	3.4	3.6	2.6	0.6	33.3
Total 2008	47.9	54.6	18.5	18.0	12.6	3.2	154.8
Q1 2009	10.3	10.9	2.7	3.6	2.4	0.6	30.5
Q2 2009	10.7	11.6	3.3	3.5	2.4	0.4	31.9
Q3 2009	10.0	11.2	3.3	3.6	2.5	0.5	31.1
Q4 2009	10.8	11.1	3.3	3.3	2.9	0.7	32.1
Total 2009	41.8	44.8	12.6	14.0	10.2	2.2	125.6
Q1 2010	10.4	10.9	3.5	3.2	3.1	0.6	31.6
Q2 2010	11.0	11.7	4.0	3.4	3.6	0.6	34.2
Q3 2010	11.3	11.4	3.9	3.3	3.5	0.6	33.9
Q4 2010	11.9	12.6	4.3	3.9	4.0	0.8	37.3
Total 2010	44.5	46.5	15.5	13.7	14.1	2.6	136.9
Q1 2011	11.8	13.7	4.3	4.2	4.2	0.7	38.9
Q2 2011	12.1	13.4	4.8	4.1	4.6	0.8	39.8
Q3 2011	12.1	12.7	4.7	4.1	4.7	0.7	39.0
Q4 2011	12.0	12.0	4.1	4.1	4.4	0.4	37.0
Total 2011	48.1	51.9	17.8	16.4	17.8	2.6	154.6
Q1 2012	12.0	11.8	4.2	3.8	3.5	0.7	35.9
Q2 2012	12.3	12.6	4.6	4.0	3.7	0.7	37.8
Q3 2012	11.1	12.7	4.3	3.8	3.5	0.7	36.0
Q4 2012	11.5	10.7	4.2	3.6	3.4	0.8	34.1
Total 2012	46.9	47.8	17.2	15.1	14.0	2.9	143.9
Q1 2013	11.0	11.7	4.4	3.4	3.0	0.9	34.4
Q2 2013	11.6	12.7	4.9	3.8	3.2	0.9	37.1
Q3 2013	11.1	11.9	4.4	3.7	3.1	0.7	34.9
Q4 2013	12.0	11.9	4.1	3.9	2.9	0.8	35.6
Total 2013	45.9	48.4	17.7	14.7	12.1	3.3	142.1
Q1 2014	10.8	11.7	3.9	3.6	2.7	0.8	33.5
Q2 2014	11.2	12.7	4.3	3.8	2.8	0.8	35.6
Q3 2014	10.6	12.7	4.3	3.7	3.1	0.8	35.2
Q4 2014	10.7	11.7	3.9	3.6	2.9	0.8	33.6
Total 2014	43.3	48.8	16.4	14.7	11.5	3.2	137.8
Q1 2015	10.5	11.1	4.2	2.9	2.7	0.9	32.3
Q2 2015	11.5	12.1	4.6	3.2	3.0	1.0	35.4
Q3 2015	11.0	11.0	4.0	2.8	2.8	0.7	32.3
Q4 2015	11.3	10.3	3.6	2.7	2.5	0.8	31.2
Total 2015	44.1	44.3	16.5	11.7	11.1	3.4	131.1

Figure 15-17 Variable Annuity Total Sales by Distribution Channel by Quarter (dollars in billions)

Year	Captive Agents	Ind. NASD	Banks/ Credit Unions	New York Wirehouses	Regional Investment Firms	Direct Response	Total
Q1 2016	10.2	8.8	2.9	2.0	1.9	0.6	26.5
Q2 2016	10.8	8.7	3.1	2.2	1.6	0.7	27.0
Q3 2016	9.9	8.6	3.0	2.2	1.6	0.7	26.0
Q4 2016	9.9	8.4	2.6	1.9	1.3	0.8	25.0
Total 2016	40.9	34.5	11.5	8.3	6.6	2.9	104.6
Q1 2017	9.5	8.6	2.4	1.6	1.5	0.8	24.4
Q2 2017	9.4	8.9	2.5	1.9	1.3	0.8	24.8
Q3 2017	8.1	8.2	2.0	1.7	1.3	0.7	21.9
Q4 2017	9.2	9.3	2.2	2.0	1.5	0.8	25.0
Total 2017	36.3	35.0	9.1	7.1	5.4	3.2	96.2
Q1 2018	8.9	9.3	2.1	1.8	1.5	0.9	24.5
Q2 2018	9.7	9.6	2.2	1.8	1.5	0.9	25.7
Q3 2018	8.5	9.6	2.2	1.7	1.6	0.9	24.6
Q4 2018	8.8	9.7	2.1	1.6	1.5	0.7	24.5
Total 2018	35.9	38.2	8.8	6.9	6.1	3.3	99.2
Q1 2019	8.1	8.5	1.9	1.4	1.3	0.7	21.9
Q2 2019	8.7	9.8	2.4	1.7	1.5	0.8	24.9
Q3 2019	8.7	10.5	2.4	1.7	1.7	0.6	25.6
Q4 2019	9.0	10.4	2.5	1.8	1.5	0.7	25.9
Total 2019	34.5	39.2	9.2	6.6	6.0	2.8	98.3
Q1 2020	8.6	10.3	2.4	1.6	1.5	0.6	25.0
Q2 2020	7.6	8.4	1.7	1.1	1.1	0.5	20.4
Q3 2020	7.8	9.8	2.4	1.5	1.3	0.5	23.3
Q4 2020	8.5	11.9	2.6	1.7	1.6	0.8	27.1
Total 2020	32.5	40.4	9.1	5.9	5.5	2.4	95.8
Q1 2021	9.0	12.8	2.8	1.7	1.9	1.0	29.2
Q2 2021	9.5	14.2	3.0	1.7	2.1	1.0	31.5
Q3 2021	9.1	13.1	3.0	1.9	1.8	0.8	29.7
Q4 2021	9.5	13.9	3.2	1.7	1.9	1.5	31.7
Total 2021	37.1	54.0	12.0	7.0	7.7	4.3	122.1
Q1 2022	9.1	12.7	2.7	1.3	1.6	0.7	28.1
Q2 2022	9.6	11.1	2.4	1.1	1.5	0.5	26.2
Q3 2022	8.6	9.8	1.9	0.9	1.5	0.5	23.2
Q4 2022	8.3	8.8	1.5	0.8	1.4	0.4	21.2
Total 2022	35.6	42.4	8.5	4.1	6.0	2.1	98.7

Source: Morningstar, Inc.

Figure 15-18 Variable Annuity Contracts

Year	# Unique Products Offered	# Cos. Selling Variable Annuities	# Contracts in Force (millions)	Average Individual Contract Value	Average # Funds Per Registered Contract
2002	667	55	27.7	\$29,376	34
2003	818	50	28.0	\$35,860	38
2004	941	48	21.5	\$52,200	39
2005	1,008	45	21.8	\$55,800	44
2006	1,150	42	22.5	\$61,400	44
2007	1,376	40	22.8	\$66,500	52
2008	1,491	40	22.7	\$49,200	51
2009	1,591	40	24.2	\$56,087	49
2010	1,694	40	24.3	\$61,973	50
2011	1,951	41	24.0	\$62,619	62
2012	2,051	37	23.3	\$70,382	63
2013	2,136	37	22.5	\$83,229	67
2014	2,181	35	20.0	\$93,988	69
2015	2,233	35	19.6	\$94,229	56
2016	2,297	34	19.1	\$94,711	57
2017	2,327	33	18.4	\$106,187	59
2018	2,343	33	17.9	\$113,053	60
2019	2,396	33	16.9	\$128,220	60
2020	2,514	33	16.8 ^o	\$125,345	60
2021	2,543	32	16.7	\$127,569	60
2022	2,565	31	16.6 ^o	\$102,590	58

Sources: Morningstar, Inc.; LIMRA Secure Retirement Institute
^oEstimated values, data not available at time of publication

Figure 15-19 Variable Annuity Net Assets by Asset Class

(dollars in billions)

Year	Equity	Fixed Accounts	Balanced	Bonds	Money Market	Total
2002	371.8	237.1	57.6	73.0	37.9	777.4
2003	524.5	264.1	74.4	83.0	26.6	972.6
2004	669.0	272.0	100.4	99.3	25.2	1,165.9
2005	691.0	270.7	104.5	96.2	24.9	1,187.3
2006	834.9	256.9	152.9	109.4	32.5	1,386.6
2007	887.9	255.6	189.1	125.7	41.0	1,499.3
2008	491.7	301.6	146.8	127.4	61.9	1,129.4
2009	642.5	294.3	216.8	158.0	42.9	1,354.5
2010	697.0	298.1	307.5	166.9	34.9	1,504.4
2011	616.5	324.7	348.1	177.9	35.1	1,502.3
2012	620.3	315.1	484.6	188.2	31.7	1,639.9
2013	769.6	321.8	576.5	171.6	29.0	1,868.5
2014	734.8	334.6	651.1	172.3	27.6	1,920.4
2015	677.4	344.6	652.9	166.8	29.9	1,871.6
2016	739.0	344.2	613.6	174.6	25.3	1,896.7
2017	676.0	341.6	775.1	171.2	21.8	1,985.7
2018	590.6	346.7	676.8	173.2	27.0	1,814.3
2019	635.3	352.7	827.8	178.7	23.5	2,018.0
2020	689.9	357.3	843.8	186.3	28.5	2,105.8
2021	746.8	358.6	823.2	178.2	23.6	2,130.4
2022	606.1	360.0	625.2	87.0	24.7	1,703.0

Source: Morningstar, Inc.

Figure 15-20 Variable Annuity Net Assets by Subaccount Investment Category

(dollars in billions)

Subaccounts	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
BALANCED/HYBRID:										
Aggressive Allocation	94.2	106.0	110.1	105.2	241.5	206.3	237.1	244.7	258.1	119.5
Conservative Allocation	138.4	167.0	144.5	113.2	113.2	116.2	104.2	89.1	85.0	10.1
Moderate Allocation	338.2	290.0	300.2		116.2	96.7	374.7	396.9	391.0	425.2
Tactical Allocation	N/A	N/A	24.0	357.1	389.6	345.4	20.1	18.3	19.0	14.5
World Allocation	66.9	81.3	66.1	30.0	22.1	18.5	78.5	77.1	56.7	36.1
Target Date	5.7	6.8	7.2	70.3	64.8	57.4	13.1	17.7	13.3	11.1
CORE BOND:										
				8.0	9.7	10.0				
Long-Term Corporate	3.1	4.6	2.7	13.3	14.1	15.6	19.5	21.6	20.3	14.4
Long-Term Government	0.5	1.9	0.5	0.5	0.4	0.4	0.4	0.5	0.5	0.3
Intermediate-Term Corporate	89.8	92.4	95.9	88.6	86.4	88.2	84.8	89.5	80.8	61.9
Intermediate-Term Government	8.0	4.4	5.3	7.0	6.2	5.5	5.9	6.9	6.2	4.7
Short-Term Corporate	9.2	10.4	11.2	12.6	10.4	11.0	10.6	12.6	13.9	10.6
Short-Term Government	1.2	0.5	0.4	0.4	0.4	0.3	0.3	0.7	0.7	3.0
Inflation-Protected	17.6	17.2	15.3	15.2	14.6	13.5	13.8	14.6	16.1	13.6
FIXED:										
Fixed	321.8	334.6	344.6	344.2	346.8	346.7	352.7	357.3	358.6	360.0
DOMESTIC STOCK:										
Bear Market	0.1	0.1	0.1	0.1	0.1	0.1	0.0	-	0	0.0
Large Cap	449.0	478.0	434.3	422.5	329.9	296.9	358.2	401.5	442.6	317.8
Mid Cap	61.3	63.2	57.1	58.8	61.2	51.2	62.5	66.3	68.8	51.7
Small Cap	38.8	36.7	33.7	38.0	38.3	33.7	39.7	43.5	45.2	32.8
Natural Resources	2.9	2.4	1.3	2.8	2.5	1.7	1.8	1.8	1.9	2.4
Real Estate	3.7	4.5	4.2	4.3	4.1	3.4	8.1	6.7	8.1	5.4
Specialty	32.8	39.1	42.9	45.6	50.6	49.7	57.2	56.8	66.3	59.7
Utility	3.2	3.2	2.5	2.6	2.8	2.5	2.9	2.5	2.6	2.9
HIGH YIELD/SPECIALTY BOND:										
Bank Loan	3.2	3.6	3.5	3.8	4.0	3.5	3.1	2.4	2.8	2.9
High Yield	19.1	17.8	15.6	16.4	15.9	13.1	16.1	13.8	14.0	11.0
Multi-Sector Bond	9.7	9.9	8.8	8.3	11.2	10.5	9.9	9.6	9.3	6.9
Ultra-Short Bond	-	-	-	-	2.1	3.0	3.0	3.3	3.2	3.8
INTERNATIONAL STOCK:										
Developed Markets Stock	100.9	97.4	100.1	93.8	107.4	93.8	95.0	99.9	102.0	76.4
Emerging Markets Stock	10.0	9.6	0.6	0.5	0.6	0.4	11.0	12.4	11.4	8.6
Japan	-	-	-	-	-	-	-	-	0.0	0.0
Pacific	0.5	0.6	0.1	-	-	-	0.2	0.2	0.0	0.0
INTERNATIONAL BOND:										
Developed Markets Bond	8.9	8.8	8.1	7.8	8.3	7.7	9.1	8.3	7.6	6.4
Emerging Markets Bond	0.8	0.8	0.7	0.5	0.6	0.6	0.7	0.8	0.8	0.6
MONEY MARKET:										
Money Market	29.0	27.6	29.9	25.3	22.9	27.0	23.6	28.5	23.6	28.7
TOTAL:	1,868.5	1,920.4	1,871.6	1,896.7	1,985.7	1,814.3	2,018.0	2,105.8	2,130.4	1,703.0

Source: Morningstar, Inc.

Figure 15-21 Variable Annuity Sales by State – 2020¹(dollars in millions)²

Rank	State	\$ Total	% of Total	Rank	State	\$ Total	% of Total
1	New York	8,080.5	9.6%	28	Kansas	756.9	0.9%
2	California	7,102.3	8.5%	29	Kentucky	743.2	0.9%
3	Florida	5,524.2	6.6%	30	Utah	673.2	0.8%
4	Texas	5,117.4	6.1%	31	Oregon	581.3	0.7%
5	Pennsylvania	4,761.5	5.7%	32	Nevada	527.5	0.6%
6	New Jersey	4,646.5	5.5%	33	Nebraska	525.1	0.6%
7	Michigan	3,737.2	4.5%	34	Oklahoma	488.1	0.6%
8	Ohio	3,629.7	4.3%	35	New Hampshire	484.3	0.6%
9	Illinois	3,262.7	3.9%	36	Hawaii	468.1	0.6%
10	Massachusetts	2,553.4	3.0%	37	Rhode Island	440.3	0.5%
11	Minnesota	2,193.4	2.6%	38	Arkansas	372.7	0.4%
12	North Carolina	2,126.6	2.5%	39	Mississippi	362.4	0.4%
13	Wisconsin	2,045.6	2.4%	40	West Virginia	332.7	0.4%
14	Virginia	2,004.0	2.4%	41	Maine	326.7	0.4%
15	Maryland	1,873.6	2.2%	42	Delaware	310.6	0.4%
16	Connecticut	1,623.6	1.9%	43	Idaho	281.0	0.3%
17	Colorado	1,565.7	1.9%	44	North Dakota	279.5	0.3%
18	Indiana	1,544.5	1.8%	45	New Mexico	279.2	0.3%
19	Georgia	1,426.7	1.7%	46	District of Columbia	254.4	0.3%
20	Arizona	1,419.7	1.7%	47	South Dakota	243.2	0.3%
21	Washington	1,418.3	1.7%	48	Vermont	227.8	0.3%
22	Tennessee	1,341.2	1.6%	49	Montana	157.2	0.2%
23	Missouri	1,224.5	1.5%	50	Wyoming	129.9	0.2%
24	Louisiana	1,146.6	1.4%	51	Puerto Rico	113.7	0.1%
25	Iowa	1,053.1	1.3%	52	Alaska	108.1	0.1%
26	South Carolina	995.5	1.2%	53	U.S. Virgin Islands	3.2	0.0%
27	Alabama	824.8	1.0%	54	Other	98.6	0.1%
Total						83,811.7	100%

Source: Morningstar, Inc.

¹2020 is the most recent data available.²\$83.8 billion total sales by state represents 87.4% of 2020 total variable annuity sales of \$95.8 billion.

Figure 15-22 2022 Variable Annuity Total Sales by Top 25 Issuers

Company	Total Flow (\$MM)	Rank	% Share	Cumulative % Share
Jackson National	14,694.1	1	14.9%	14.9%
Equitable	13,880.5	2	14.1%	29.0%
Lincoln National	8,770.2	3	8.9%	37.9%
TIAA	7,563.1	4	7.7%	45.5%
Brighthouse Financial	7,081.4	5	7.2%	52.7%
New York Life	6,715.0	6	6.8%	59.5%
Allianz Life	5,931.9	7	6.0%	65.5%
Corebridge Financial	5,562.8	8	5.6%	71.2%
Nationwide	5,366.5	9	5.4%	76.6%
Prudential	5,296.9	10	5.4%	82.0%
Pacific Life	3,308.8	11	3.4%	85.3%
RiverSource	2,808.2	12	2.8%	88.2%
Thrivent Financial	2,207.8	13	2.2%	90.4%
CUNA Mutual	1,384.1	14	1.4%	91.8%
Fidelity Investments Life	1,228.2	15	1.2%	93.1%
Massachusetts Mutual	1,167.6	16	1.2%	94.2%
Northwestern Mutual	988.9	17	1.0%	95.2%
Athene	903.0	18	0.9%	96.2%
AEGON/Transamerica	882.5	19	0.9%	97.0%
Protective	857.8	20	0.9%	97.9%
Symetra Financial	687.4	21	0.7%	98.6%
Mutual Of America	322.9	22	0.3%	98.9%
Horace Mann	311.5	23	0.3%	99.3%
Sammons Financial Group	293.1	24	0.3%	99.6%
Security Benefit	187.3	25	0.2%	99.7%

Source: Morningstar, Inc

Fixed Annuity Market

(Excludes Structured Settlements)

Figure 15-23 Fixed Annuity Sales and Net Assets

(dollars in billions)

Year	Sales	Net Assets
2002	103.3	421.0
2003	84.1	490.0
2004	86.7	510.0
2005	76.5	534.0
2006	74.0	519.0
2007	66.6	511.0
2008	106.7	556.0
2009	104.2	620.2
2010	76.4	658.6
2011	75.6	676.0
2012	67.0	691.6
2013	78.1	721.2
2014	91.5	747.1
2015	98.4	782.0
2016	108.0	827.5
2017	97.8	861.5
2018	125.0	902.3
2019	129.5	946.6
2020	111.7	983.5
2021	114.1	1,030.9
2022	203.5	1,122.7

Sources: Beacon Research and LIMRA Secure Retirement Institute

Figure 15-24 Fixed Annuity Sales by Quarter

(dollars in billions)

Year	Sales
Q1 2006	17.4
Q2 2006	18.8
Q3 2006	20.5
4 2006	17.3
Total 2006	74.0
Q1 2007	14.1
Q2 2007	16.4
Q3 2007	18.1
Q4 2007	18.0
Total 2007	66.6
Q1 2008	19.6
Q2 2008	25.3
Q3 2008	27.7
Q4 2008	34.1
Total 2008	106.7
Q1 2009	34.8
Q2 2009	27.8
Q3 2009	22.1
Q4 2009	19.5
Total 2009	104.2
Q1 2010	17.9
Q2 2010	20.4
Q3 2010	20.5
Q4 2010	17.6
Total 2010	76.4
Q1 2011	18.6
Q2 2011	20.7
Q3 2011	19.0
Q4 2011	17.3
Total 2011	75.6
Q1 2012	17.0
Q2 2012	17.2
Q3 2012	16.6
Q4 2012	16.2
Total 2012	67.0
Q1 2013	15.0
Q2 2013	17.1
Q3 2013	22.5
Q4 2013	23.5
Total 2013	78.1

Figure 15-24 Fixed Annuity Sales by Quarter

(dollars in billions)

Year	Sales
Q1 2014	22.5
Q2 2014	24.3
Q3 2014	21.7
Q4 2014	23.0
Total 2014	91.5
Q1 2015	20.9
Q2 2015	22.8
Q3 2015	26.5
Q4 2015	28.2
Total 2015	98.4
Q1 2016	29.6
Q2 2016	29.1
Q3 2016	25.8
Q4 2016	23.5
Total 2016	108.0
Q1 2017	25.2
Q2 2017	26.1
Q3 2017	22.6
Q4 2017	23.9
Total 2017	97.8
Q1 2018	25.5
Q2 2018	31.8
Q3 2018	31.9
Q4 2018	35.8
Total 2018	125.0
Q1 2019	35.9
Q2 2019	35.8
Q3 2019	30.1
Q4 2019	27.7
Total 2019	129.5
Q1 2020	27.6
Q2 2020	26.5
Q3 2020	30.2
Q4 2020	27.4
Total 2020	111.7
Q1 2021	27.5
Q2 2021	30.8
Q3 2021	28.0
Q4 2021	27.8
Total 2021	114.1
Q1 2022	33.9
Q2 2022	50.6
Q3 2022	54.3
Q4 2022	64.7
Total 2022	203.5

Source: Beacon Research

Figure 15-25 Fixed Annuity Assets – Qualified Versus Non-Qualified

(dollars in billions)

Year	Qualified	Non-Qualified	Total
2002	167.0	254.0	421.0
2003	201.0	289.0	490.0
2004	208.0	302.0	510.0
2005	214.0	320.0	534.0
2006	207.0	312.0	519.0
2007	211.0	300.0	511.0
2008	242.0	314.0	556.0
2009	272.2	348.0	620.2
2010	300.6	358.0	658.6
2011	313.0	363.0	676.0
2012	324.6	367.0	691.6
2013	344.2	377.0	721.2
2014	365.1	382.0	747.1
2015	388.0	394.0	782.0
2016	428.5	399.0	827.5
2017	453.5	408.0	861.5
2018	484.9	417.4	902.3
2019	530.1	416.5	946.6
2020	759.6	223.9	983.5
2021	784.2	246.7	1,030.9
2022	617.5	505.2	1,122.7

Source: LIMRA Secure Retirement Institute

Figure 15-26 Fixed Annuity Sales – Qualified Versus Non-Qualified

(dollars in billions)

Year	Qualified	Non-Qualified	Total
2003	29.9	54.2	84.1
2004	31.1	55.6	86.7
2005	28.6	47.9	76.5
2006	27.6	46.4	74.0
2007	22.0	44.6	66.6
2008	41.6	65.1	106.7
2009	43.7	60.5	104.2
2010	34.2	42.2	76.4
2011	33.6	42.0	75.6
2012	34.8	32.2	67.0
2013	39.2	38.9	78.1
2014	50.9	40.6	91.5
2015	56.7	41.7	98.4
2016	61.9	46.1	108.0
2017	53.9	43.9	97.8
2018	69.7	55.3	125.0
2019	75.7	53.8	129.5
2020	58.9	52.8	111.7
2021	59.0	55.1	114.1
2022	111.9	91.6	203.5

Source: Beacon Research

Figure 15-27 Fixed Annuity Sales – Product Type

(dollars in billions)

Year	Book Value	Market Value	Indexed	Income Annuities	Total
2003	59.0	9.0	11.0	5.0	84.0
2004	51.0	9.0	21.0	6.0	87.0
2005	38.0	6.0	27.0	6.0	77.0
2006	33.0	10.0	25.0	6.0	74.0
2007	27.0	8.0	25.0	7.0	67.0
2008	54.0	18.0	27.0	9.0	108.0
2009	52.0	15.0	30.0	8.0	105.0
2010	29.0	6.3	33.1	8.0	76.4
2011	28.1	6.0	33.0	8.5	75.6
2012	18.8	4.8	34.2	9.2	67.0
2013	21.7	6.7	38.7	11.0	78.1
2014	20.8	9.8	47.9	13.0	91.5
2015	20.2	11.1	54.6	12.5	98.4
2016	20.9	16.0	58.8	12.3	108.0
2017	20.6	12.4	54.3	10.5	97.8
2018	27.9	15.9	69.8	11.4	125.0
2019	25.2	19.9	72.5	11.9	129.5
2020	24.4	24.5	55.4	7.4	111.7
2021	24.5	22.4	60.2	7.0	114.1
2022	59.5	53.0	79.7	11.3	203.5

Source: Beacon Research

Figure 15-28 Fixed Annuity Sales – Deferred Versus Immediate

(dollars in billions)

Year	Deferred	Immediate	Deferred Income	Total
2003	79.4	4.8	-	84.1
2004	80.6	6.1	-	86.6
2005	70.2	6.3	-	76.5
2006	67.7	6.3	-	74.0
2007	60.0	6.7	-	66.6
2008	98.0	8.6	-	106.7
2009	96.3	7.8	-	104.1
2010	68.4	8.0	-	76.4
2011	67.1	8.5	-	75.6
2012	58.0	8.0	1.0	67.0
2013	67.0	8.9	2.2	78.1
2014	78.5	10.4	2.6	91.5
2015	85.9	9.9	2.6	98.4
2016	95.6	9.8	2.6	108.0
2017	87.3	8.8	1.7	97.8
2018	113.6	10.0	1.4	125.0
2019	117.6	10.2	1.7	129.5
2020	104.3	6.4	1.0	111.7
2021	107.1	6.0	1.0	114.1
2022	192.2	10.3	1.0	203.5

Source: Beacon Research (Prior to 2012, Deferred Income Annuities were included in Immediate)

Figure 15-29 Fixed Annuity Sales Percentages by Distribution Channel

(dollars in billions)

Year	Captive Agents	Independent Producers	Wirehouses	Large/regional B-Ds	Independent B-Ds	Banks & S&Ls	Direct/Third Party	Total Sales
2003	11.6%	34.2%	1.7%	3.7%	2.6%	43.8%	2.4%	84.1
2004	12.0%	39.7%	1.3%	3.5%	2.0%	39.1%	2.5%	86.7
2005	12.6%	46.1%	1.4%	3.0%	2.2%	31.9%	2.9%	76.5
2006	13.5%	46.3%	2.4%	3.0%	3.3%	29.2%	2.4%	74.0
2007	11.9%	49.8%	2.2%	2.7%	3.6%	27.2%	2.6%	66.6
2008	13.7%	38.0%	2.5%	4.3%	5.2%	32.9%	3.4%	106.7
2009	15.3%	36.6%	2.0%	5.9%	5.5%	31.9%	2.8%	104.2
2010	12.7%	51.1%	1.2%	4.4%	3.3%	23.9%	3.5%	76.4
2011	11.5%	47.4%	1.6%	5.2%	4.6%	26.7%	2.9%	75.6
2012	12.4%	53.3%	1.3%	4.9%	4.2%	19.7%	4.2%	66.8
2013	12.7%	47.4%	1.1%	7.3%	4.1%	23.4%	4.0%	78.1
2014	11.9%	42.4%	1.4%	7.5%	9.5%	24.3%	3.1%	91.5
2015	12.9%	40.2%	1.8%	8.6%	10.2%	24.7%	1.7%	98.4
2016	11.0%	38.3%	2.2%	10.2%	11.8%	24.8%	1.7%	109.3
2017	9.5%	36.9%	2.6%	11.5%	11.6%	26.2%	1.7%	100.4
2018	9.5%	34.8%	2.9%	11.0%	13.1%	26.3%	2.4%	128.3
2019	9.3%	35.6%	3.2%	11.5%	12.9%	24.7%	2.8%	129.5
2020	7.4%	34.3%	2.8%	13.5%	12.0%	25.7%	4.3%	111.7
2021	6.6%	36.9%	2.5%	12.4%	10.8%	25.3%	5.5%	114.1
2022	8.4%	29.0%	2.1%	13.4%	9.7%	31.1%	6.4%	203.5

Source: Beacon Research

Figure 15-30 Fixed Indexed Annuity Assets and Sales

(dollars in billions)

Year	Total Fixed Indexed Assets	Total Fixed Indexed Sales	Sales as a % of Total FIA Sales
2002	35.0	11.8	11%
2003	47.0	11.3	13%
2004	71.0	21.1	24%
2005	93.0	26.8	35%
2006	103.0	25.0	34%
2007	125.0	25.1	38%
2008	137.0	26.7	25%
2009	157.0	29.5	28%
2010	185.1	33.1	43%
2011	205.0	33.0	44%
2012	224.6	34.2	51%
2013	256.7	38.7	50%
2014	295.1	47.9	52%
2015	334.2	54.6	55%
2016	374.3	58.8	54%
2017	407.8	54.3	56%
2018	453.6	69.8	56%
2019	495.4	72.5	56%
2020	517.0	55.4	50%
2021	559.4	60.2	53%
2022	585.2	79.7	39%

Sources: Beacon Research; LIMRA Secure Retirement Institute

Figure 15-31 2022 Fixed Annuity Total Sales by Top 25 Issuers

Company	Total Flow (\$MM)	Rank	% Share	Cumulative % Share
Athene	19,505.6	1	9.6%	9.6%
Massachusetts Mutual	18,987.1	2	9.3%	18.9%
New York Life	17,678.9	3	8.7%	27.6%
Corebridge Financial	13,087.4	4	6.4%	34.0%
Global Atlantic	9,393.7	5	4.6%	38.6%
F & G Life	8,294.8	6	4.1%	42.7%
Allianz Life	8,208.7	7	4.0%	46.8%
Sammons Financial Group	7,968.3	8	3.9%	50.7%
Pacific Life	6,489.3	9	3.2%	53.9%
Western Southern	6,249.5	10	3.1%	56.9%
Nassau	5,940.9	11	2.9%	59.9%
Symetra Financial	5,437.3	12	2.7%	62.5%
USAA	5,236.9	13	2.6%	65.1%
Security Benefit	4,309.9	14	2.1%	67.2%
Brighthouse Financial	3,861.7	15	1.9%	69.1%
Lincoln National	3,327.3	16	1.6%	70.8%
American Equity	3,321.1	17	1.6%	72.4%
Delaware Life	2,488.0	18	1.2%	73.6%
EquiTrust Life	1,939.1	19	1.0%	74.6%
Reliance Standard Life	1,848.8	20	0.9%	75.5%
Bankers Life	1,576.2	21	0.8%	76.2%
American National Insurance Company	1,464.3	22	0.7%	77.0%
Integrity Life	1,395.0	23	0.7%	77.6%
Oceanview Life	1,241.3	24	0.6%	78.3%
The Standard	1,115.9	25	0.5%	78.8%

Source: Beacon Research

Glossary of Annuity Product Terms

A

A-SHARE VARIABLE ANNUITIES Annuity contracts in which sales charges are incurred at time of investment or premium payment. A-share contracts typically have no surrender charges.

ACCUMULATION PHASE The period in an annuity contract prior to annuitization when annuity owners can add money and accumulate tax-deferred assets.

ACCUMULATION UNIT VALUE (AUV) A variable annuity subaccount price per share during the accumulation phase. An AUV is the net asset value after income and capital gains have been included and subaccount management expenses have been subtracted.

ANNUAL CONTRACT FEE An annual fee paid to the insurance company for administering the contract. The fee is often waived for contracts with high account values.

ANNUITANT The person, frequently the contract owner, to whom an annuity is payable and whose life expectancy is used to calculate the income payment.

ANNUITIZATION The conversion of the annuity accumulation value to a fixed or variable income stream for the life of the annuitant(s) or for a specified period.

ANNUITY A periodic income payable for the lifetime of one or more persons, or for a specified period. A contract in which an insurance company agrees to pay an income for life or for a specified number of years.

ANNUITY COMMENCEMENT DATE The date income payments begin, also known as the annuity start date.

ANNUITY CONTRACT A legal agreement between the contract owner and the insurance company.

ANNUITY OWNER The person or entity that has the rights to the contract, including withdrawals, surrender, change of beneficiary, or other specified terms.

ANNUITY INCOME PAYMENTS or **PAYOUTS** A series of payments made over a specific period of time with the duration guaranteed by the life insurance company at the beginning of the period.

ANNUITY START DATE The beginning date of the series of annuity payments.

ANNUITY PURCHASE RATE The cost of an annuity based on insurance company tables, which take into account various factors such as age and gender.

ANNUITY UNIT Annuity units (variable) are the units in the separate account after the maturity date that is used to determine the amount of the annuity payment. The amount of the payment is the number of annuity units times the annuity unit value.

ANNUITY UNIT VALUE The number of annuity units in an account remains constant during the annuitant's lifetime. Each annuity unit value changes each payment period based on the following factors:

- The investment performance of the account
- The assumed investment returns (AIR)
- Contract expenses during the period

APPLICATION A form supplied by a life insurance company on the basis of information received from the applicant. The form is signed by the applicant and is part of the insurance or annuity contract.

ASSET ALLOCATION In a variable annuity, distribution of assets across multiple classes, e.g., stocks, bonds, and cash, in order to meet an individual's financial goals. The objective of asset allocation is to reduce investment risk.

ASSET ALLOCATION PROGRAMS A system of assigning variable annuity purchase payments to subaccounts based on a contract owner's financial goals and risk tolerance. Portfolio rebalancing programs redistribute the amount of money allocated to each subaccount when the target percentages move out of alignment over time as the value of some subaccounts changes faster than others.

ASSET-BASED EXPENSES Variable annuity expenses, such as investment management fees and annual insurance charges, that are based on the value of the assets held in the insurance company's separate account.

ASSUMED INVESTMENT RETURN (AIR) Variable annuity payments increase or decrease based on the net performance (returns after fees and expenses) of the underlying investments in relation to a benchmark assumed investment return. If the total investment return minus expenses exceeds the AIR, the payment increases. If the return minus expenses is less than the AIR, the payment decreases. If the return minus expenses equals the AIR, payments remain the same.

B

B-SHARE VARIABLE ANNUITIES Variable annuity contracts characterized by deferred sales charges, which typically range from 5% to 7% in the first year, and subsequently decline to zero after five to seven years. B-shares are the most common form of annuity contracts sold.

BAILOUT PROVISION If a fixed annuity's interest rate falls below a rate specified in the annuity contract, this feature assures the free withdrawal of all funds from an annuity account.

BENEFICIARY A person, persons, or trust designated under the contract to receive any payments due in the event of the death of the owner or the annuitant.

BONUS RATE Extra interest accumulated in the first year of a deferred annuity that is added to the sum upon which interest is calculated in later years, also called a first-year bonus rate.

BONUS SHARE (X-SHARE) VARIABLE ANNUITIES A bonus amount, typically defined in the prospectus as a percentage of purchase payments, is allocated to the annuity accumulation value early in the contract period. This type of annuity typically has higher expenses to pay for the cost of the bonus.

BREAKPOINT PRICING A system whereby the cost of up-front sales charges decreases depending on the cumulative amount of purchase payments made.

C

C-SHARE VARIABLE ANNUITIES Variable annuity contracts with no up-front or contingent deferred sales charges, which offer full liquidity to contract holders at any time

CASH REFUND ANNUITY An annuity settlement payment, which provides that upon the death of the annuitant before payments totaling the purchase price have been made, the excess will be paid in one sum to designated beneficiaries.

CASH SURRENDER VALUE The amount that can be withdrawn from the contract after the deduction of any surrender charge. It is equal to the contract value (the sum of premiums and earnings minus contract charges and withdrawals) minus the surrender charge.

CASH VALUE (SURRENDER VALUE) The amount available to the owner when a policy is surrendered. During the early policy years, in some contracts, the cash value equals the account value less a “surrender charge.”

CHARITABLE ANNUITY (GIFT ANNUITY) A charitable gift annuity is a contract between a donor and a foundation, under which the foundation guarantees payment of an annuity.

COMMUTATION A process provided under some annuities that allows annuity payments to be terminated and the remaining value to be withdrawn from the contract.

CONTINGENT ANNUITANT In the case of the death of an annuitant prior to the beginning of annuity payments, the person who is designated to receive the payments in the original annuitant’s stead.

CONTINGENT BENEFICIARY A person or persons named to receive contract benefits if the primary beneficiary is deceased.

CONTINGENT DEFERRED ANNUITY A retirement product option that provides for lifetime income payments, typically composed of a balanced mutual fund coupled with a lifetime income feature that, subject to certain conditions, continues to make payments to an insured in the event systematic withdrawals from the fund reduce its value to zero.

CONTINGENT DEFERRED SALES CHARGE Costs imposed on the withdrawal of proceeds or liquidation of a variable annuity, which typically range from 5% to 7% in the first year, and subsequently decline to zero.

CONTRACT DATE The date an annuity contract becomes effective.

CONTRACT OWNER The purchaser of an annuity contract, and holder of all rights pertaining to the contract.

COST BASIS The initial payment/premium(s) paid to a non-qualified annuity is known as the cost basis in the contract. Since it was previously taxed, cost basis is not taxed upon withdrawal.

D

DEATH BENEFITS The payment the investor's estate or beneficiaries receive if the contract holder dies prior to the annuity starting date. Types of death benefits: Greater of account value or premiums less withdrawals; rising floor, in which the insurance company guarantees a minimum return on premium deposits; ratchet, a benefit equal to the greater of (a) the contract value, (b) premiums less withdrawals, or (c) the contract value on a specified prior date.

DEFERRED ANNUITY The annuity contract during the time period prior to annuitization. The contract owner determines the point at which accumulated principal and earnings are converted into a stream of income.

DEFERRED INCOME ANNUITY An annuity product designed to make lifetime payments to an insured beginning 5 to 40 years in the future.

DEFINED BENEFIT PLAN An employer-administered pension plan that qualifies for special tax treatment under the Internal Revenue Code. With a deferred benefit plan, the retired employee receives lifetime payments based on salary, years of service, and age at retirement. The employer bears the investment risk. The plan provides lifetime income through a group or individual annuity contract.

DEFINED CONTRIBUTION PLAN An employer-administered retirement plan in which the contribution, rather than the benefit, is defined. Under a 401(k) type of defined contribution plan, the employee is allowed to channel part of his/her income into the plan on a pre-tax basis. A percentage of employee contributions may be matched by the employer but the employee bears the investment risk. The final benefit consists solely of assets (including investment returns) that have accumulated in these individual accounts. Depending on the type of defined contribution plan, contributions may be made either by the company, the participant, or both. In some DC plans, distribution options in the form of life annuities are available.

DISTRIBUTION A payout made from a retirement plan or annuity contract. See also Lump-Sum Distribution and Annuity.

DOLLAR COST AVERAGING A program for investing a fixed amount of money at set intervals with the goal of purchasing more shares at low values and fewer shares at high values. Variable annuity dollar cost averaging programs involve allocating a certain amount to one investment subaccount, such as a money market fund, and then having portions of that payment periodically transferred to other subaccounts. Dollar cost averaging does not guarantee a profit or prevent a loss in declining markets.

E

EARLY WITHDRAWAL PENALTY A 10% penalty tax for withdrawal of assets from a qualified retirement plan prior to age 59 ½. This 10% penalty tax is in addition to regular federal and (if applicable) state tax. Exceptions to the penalty, such as death and disability, may apply.

EFFECTIVE ANNUAL YIELD In a fixed deferred annuity, the annualized return based on the daily compounding and crediting of the annuity's interest.

EFFECTIVE INTEREST RATE The actual annual interest rate that accrues, including the effects of compounding.

ENHANCED DEATH BENEFIT A death benefit that goes beyond the guaranteed minimum death benefit by periodically locking in investment gains or paying a minimum stated interest rate on purchase payments.

ENHANCED EARNINGS BENEFIT A feature of some variable annuity contracts that provides beneficiaries with an additional death benefit amount, usually equal to a percentage of earnings.

ERISA A federal law requiring plan sponsors to design and administer their plans in accordance with the Employee Retirement Income Security Act of 1974 (ERISA). Among its statutes, ERISA calls for proper plan reporting and disclosure to participants. Non-qualified annuities are not covered by ERISA.

EXCESS INTEREST Interest credited to a fixed annuity contract beyond the minimum guaranteed by the insurance company.

EXCHANGE TRADED FUNDS (ETFs) An investment fund traded on stock exchanges, much like stocks. An ETF holds assets such as stocks, commodities, or bonds, and trades close to its net asset value over the course of the trading day.

EXCLUSION RATIO The formula that determines which portion of an annuity payment is considered taxable and which is a tax-free return of principal. For variable annuities, this formula is similar, however, due to the fluctuating nature of variable payouts, this is recalculated annually and is reported as an exclusion amount.

EXPENSE RATIO The percentage of a fund's assets used to pay its annual expenses.

F

FIDUCIARY A person who has undertaken to act for and on behalf of another in a relationship of trust and confidence.

FIXED ACCOUNT An investment option in the issuing insurance company's general account that is offered in some variable annuity contracts. A minimum rate of interest is guaranteed, usually for a period of one year.

FIXED ANNUITIZATION A series of guaranteed income payments of a specified amount payable for the life of the annuitant(s) or a specified number of years.

FIXED ANNUITY A contract providing a specified rate of interest paid on the amount invested during the accumulation phase and a specified payment amount during the annuitization phase. The issuing company assumes the investment risk.

FIXED INDEXED ANNUITY An annuity on which credited interest is based upon the performance of an equity market index, such as the S&P 500. The principal investment is protected from losses in the equity market, while gains add to the annuity's returns.

FIXED PERIOD ANNUITY Payout option for a specified number of years instead of for a lifetime.

FLEXIBLE PREMIUM ANNUITY Contracts purchased with a series of payments over a period of time. The owner is usually allowed to change the amount or frequency of payments, subject to minimum annual amounts.

FREE-LOOK PERIOD A specified number of days (e.g., 10 days) during which an annuity contract owner may revoke the purchase of the contract.

FRONT-END LOAD A percent of premium fee insurance companies charge at contract inception and each subsequent premium payment to cover the costs of establishing new accounts. Referred to as A- share pricing.

G

GENERAL ACCOUNT The assets and liabilities of the insurance company not allocated to separate accounts.

GUARANTEE PERIOD The period during which the level of interest credited under a fixed annuity is guaranteed.

GUARANTEED INTEREST RATE The minimum rate of interest the insurance company agrees to pay each year on a fixed annuity.

GUARANTEED INVESTMENT CONTRACTS (GICS) Group contracts with an insurance company at a fixed rate of interest.

GUARANTEED LIFETIME WITHDRAWAL BENEFIT (GLWB) An annuity option that provides a specified percentage of a guaranteed benefit base that can be withdrawn each year for the life of the contract holder, regardless of market performance or the actual account balance.

GUARANTEED MINIMUM ACCUMULATION BENEFIT (GMAB) A guarantee that ensures that the contract value of a variable annuity will be, at least, equal to a stated minimum amount after a specified number of years.

GUARANTEED MINIMUM DEATH BENEFIT (GMDB) The basic death benefit offered under variable annuity contracts, which specifies that if the owner, or in some contracts the annuitant, dies before annuity income payments begin, the beneficiary will receive a payment equal to (a) the greater of the contract value or (b) purchase payments less withdrawals.

GUARANTEED MINIMUM INCOME BENEFIT (GMIB) An annuity option guaranteeing that the owner may annuitize the contract at a stated future date, based on the greater of (a) the actual account value or (b) an amount equal to premiums credited with a defined interest rate or the maximum anniversary value of the account prior to annuitization.

GUARANTEED MINIMUM LIVING BENEFIT (GMLB) A benefit that protects against investment risks by guaranteeing the level of account values or annuity payments. There are three types—guaranteed minimum income benefits, guaranteed minimum accumulation benefits, and guaranteed minimum withdrawal benefits.

GUARANTEED MINIMUM WITHDRAWAL BENEFIT (GMWB) A guarantee that promises a certain percentage (usually 5% to 7%) of a guaranteed benefit base (often paid premiums) can be withdrawn annually until the base is completely recovered, regardless of market performance or the actual account balance.

I-SHARE VARIABLE ANNUITY Also known as fee-based variable annuities in which an investor pays one fee to have the portfolio managed by an investment advisor. I-shares do not offer a sales commission to the advisor. However, the advisor assesses fees for the services, including the I-share contract, which is agreed upon by the client.

IMMEDIATE ANNUITY An annuity purchased with a single premium on which income payments begin within one year of the contract date. With fixed immediate annuities, the payment is based on a specified interest rate. With variable immediate annuities, payments are based on the value of the underlying investments. Payments are made for the life of the annuitant(s), for a specified period, or both (e.g., 10 years certain and life).

INCOME FLOOR GUARANTEE Annuity feature that guarantees payments will never be less than a given percentage of the original payment, such as 80%, regardless of the performance of the underlying investments.

INCOME OR PAYOUT OPTIONS Methods by which a contract owner can receive income from an annuity. These include a lump-sum payment, systematic withdrawals, living benefits, and annuitization.

INDEXED ANNUITY (See Fixed Indexed Annuity.)

INDIVIDUAL RETIREMENT ACCOUNT (IRA) IRC Sec 408(a) defines an IRA as an Individual Retirement Account. Sec 408(b) defines an IRA as an Individual Retirement Annuity. With either definition, an IRA is a tax-advantaged personal savings plan that allows an individual to set aside money for retirement. All or part of the participant's contributions may be tax deductible, depending on the type of IRA chosen and the investor's personal financial circumstances. Distributions from most employer-sponsored retirement plans may be eligible to be rolled into an IRA to continue tax-deferred growth until the funds are needed. Generally, distributions are required to begin at age 70 ½.

INITIAL INTEREST RATE The rate of interest set by the insurance company each policy year based on the prevailing market rates.

INSURANCE CHARGES Costs which cover administrative expenses and the mortality and expense (M&E) risk.

INVESTMENT MANAGEMENT FEE The fee paid in connection with the professional management of the assets of the investment funds underlying variable annuities.

INVESTMENT ONLY VARIABLE ANNUITY A variable annuity that does not offer any death or living benefits, or offers them only for an additional fee. Such product typically offer a wide range of subaccount investment options and/or pre-designed, outcome oriented investment strategies (e.g. inflation protection).

ISSUER The insurance company that issues the annuity contract.

J

JOINT AND SURVIVOR ANNUITY A life annuity in which there are two annuitants, usually spouses, known as joint annuitants. Annuity payments continue as long as either annuitant is alive.

L

L-SHARE VARIABLE ANNUITIES Variable annuity contracts that typically have shorter surrender periods, such as three or four years. L-share variable annuities typically have higher mortality and expense (M&E) charges than B-share annuities.

LEVELIZED ANNUITY PAYMENTS Payments under a variable annuity contract that remain the same for a period of time, such as 12 months, and then change to reflect investment performance. Once changed, the payments remain the same for the next 12 months.

LIFE ANNUITY Annuity payments that are guaranteed to continue for the life of the annuitant.

LIFE EXPECTANCY The average duration of the life remaining to a number of persons of a given age (cohort), according to a selected mortality table.

LIFETIME INCOME Income payments that continue throughout a person's life, irrespective of the duration.

LIVING BENEFITS The term applied to a series of annuity options that protect against investment risk by guaranteeing either withdrawal payments, account values, or annuity payments. There are three primary types—guaranteed minimum income benefits, guaranteed minimum accumulation benefits, and guaranteed minimum withdrawal benefits.

LONGEVITY RISK The risk of outliving one's assets.

LUMP-SUM DISTRIBUTION The distribution at retirement of a participant's entire account balance within one calendar year due to retirement, death, or disability.

LUMP-SUM OPTION A withdrawal option in which the annuity is surrendered and all assets are withdrawn in a single payment.

M

MARKET RISK The risk of losing portfolio value due to the volatility of the stock market.

MARKET VALUE ADJUSTMENT (MVA) A feature included in some annuity contracts which imposes an adjustment or fee upon the surrender of a fixed annuity or the fixed account of a variable annuity. The adjustment is based on the relationship of market interest rates at the time of surrender and the interest rate guaranteed in the annuity.

MINIMUM CREDITED INTEREST RATE The minimum rate of interest that is guaranteed on a fixed annuity.

MONEY MARKET FUND A mutual fund seeking to generate income for participants through investments in short-term fixed income securities.

MONEY-PURCHASE PLAN A type of defined contribution plan in which the employer's contributions are determined by a specific formula, usually as a percentage of pay. Contributions are not dependent on company profits.

MONTE CARLO SIMULATION A computerized analytical model that considers thousands of scenarios, using multiple data points such as inflation, interest rates, and market returns, and presents a range of probabilities that various outcomes might actually occur.

MORTALITY AND EXPENSE RISK CHARGE (M&E) A fee charged in variable annuities for insurance guarantees, including the death benefit, the guaranteed lifetime income options, and the guarantee that contract charges will not increase.

MORTALITY TABLE A table showing the incidence of death at specified ages that is used to determine average life expectancy.

N

NET ASSET VALUE (NAV) The market value of all securities owned by a mutual fund, minus its total liabilities, divided by the number of shares issued.

NET SALES or **NET FLOWS** Total variable annuity sales minus surrenders, withdrawals, inter- and intra-company exchanges, and benefit payments.

NON-QUALIFIED ANNUITY An annuity in which purchase payments are made with after-tax dollars. Earnings accumulate on a tax-deferred basis until withdrawn.

O

O-SHARE VARIABLE ANNUITIES Annuity contracts which do not impose up-front sales charges, while, typically, possessing surrender charge periods similar to B-shares. Mortality and expense charges are assessed, and progressively decline throughout the surrender period.

P

PARTIAL WITHDRAWAL The withdrawal of an amount less than the total contract value of an annuity. Many contracts permit annual withdrawals of a certain amount free of a surrender charge.

PARTY-AT-INTEREST An individual or group having direct interest in a contract, including the issuer, the contract owner, and the annuitant.

PAYOUT PHASE or **PAYOUT PERIOD** The period during which the money accumulated in an annuity is paid out as regular income payments.

PENSION ANNUITIES An annuity incorporated in a pension or other qualified retirement plan set up by a corporation, labor union, government, or other organization for its employees, including profit-sharing plans, stock bonus and employee stock ownership plans, thrift plans, target benefit plans, money purchase plans, and defined benefit plans.

PENSION BENEFIT GUARANTY CORPORATION (PBGC) A federal agency established by Title IV of ERISA for the insurance of defined benefit pension plans. The PBGC provides payment of limited pension benefits if a plan terminates and is unable to cover all required benefits.

PERIOD CERTAIN A type of refund annuity guaranteeing that if the annuitant dies before payments have been made for a minimum number of years, payments to the beneficiary will continue until the end of the stated period.

PERSISTENCY BONUS An enhancement to the policy's benefits, usually in the form of additional interest credits and/or reduced charges, for policies that remain in force for a certain period. The bonus may or may not be guaranteed in the contract.

PORTFOLIO REBALANCING A type of asset allocation program that periodically reallocates contract assets among investment options within a variable annuity contract.

PREMATURE DISTRIBUTION OR WITHDRAWAL (PREMATURE DISTRIBUTION PENALTY) Withdrawals made from deferred annuities and certain other tax-favored plans may be subject to an additional 10% federal income tax if the withdrawal is made before the contract owner reaches age 59 1/2. Certain exemptions apply. The contract owner should seek legal and tax advice before making withdrawals prior to age 59 1/2.

PREMIUM BONUS A premium bonus is an additional amount credited to the accumulation account of an annuity policy under certain conditions.

PREMIUMS The amounts of money paid into an annuity contract. Also known as purchase payments.

PREMIUM TAXES Some states charge a tax on the contributions made to an annuity, typically upon annuitization. The issuing company generally charges the annuity contract for any premium tax and other taxes based on premium it pays to the state.

PRIMARY BENEFICIARY The person or entity named as first in line to receive proceeds or benefits from a contract following the death of the contract holder or, in some contracts, the death of the annuitant.

PRIVATE ANNUITY A private annuity is an arrangement in which the client transfers property to an individual or entity in return for a promise of fixed periodic payments for the rest of the client's life. In private annuities, the person or entity assuming the payment obligation is not in the business of selling annuities.

PROCEEDS The net amount of money payable by the company at the death of the insured or at the maturity of a contract.

Q

QUALIFIED ANNUITIES Qualified annuities are annuities purchased for funding an IRA, 403(b) tax-deferred annuity, or other type of tax-benefited retirement arrangements. An IRA or qualified retirement plan provides tax deferral. An annuity contract should be used to fund an IRA or qualified retirement plan to benefit from annuity features including lifetime income, living benefits, and the guaranteed minimum death benefit.

QUALIFYING LONGEVITY ANNUITY CONTRACT (QLAC) A deferred income annuity intended for purchase within a qualified plan (e.g. 401(k) or IRA) that meets IRS requirements that it a) provide distributions that begin at an advanced age, but not later than age 85; b) not be a variable contract under section 817, or an equity-indexed contract; and c) may include a return of premium death benefit, but may not include commutation rights, cash surrender value, or other similar feature.

R

RATCHET GUARANTEED MINIMUM DEATH BENEFIT A type of enhanced death benefit that is equal to the greater of (a) the contract value, (b) premium payments less prior withdrawals, or (c) the contract value on a specified prior date.

REFUND ANNUITY A contract that provides a lump sum at the death of the annuitant, which when added to total annuity payments equals the purchase price.

RENEWAL RATE INTEREST Rate at time of annuity contract anniversary set at the end of each policy year.

RESERVE Actuarially determined amounts held by insurance companies, which are required to meet future contract obligations.

RETIREMENT INCOME PERIOD OR PHASE The period during which the money accumulated in a deferred annuity contract, or the purchase payment for an immediate annuity, is paid out as income payments.

REVERSE ANNUITY MORTGAGE A reverse annuity mortgage is an arrangement in which a homeowner borrows against home equity and receives lifetime monthly payments from the lender.

RISING FLOOR GUARANTEED MINIMUM DEATH BENEFIT A type of enhanced death benefit that is equal to the greater of (1) the contract value or (2) premium payments less prior withdrawals increased annually at a specified rate of interest.

RISK POOLING The spreading (in the case of annuities) of longevity risk among a large group of individuals, some of whom die sooner than expected, some of whom will live longer than expected.

ROLLOVER The action of moving plan assets from one qualified plan to another or to an IRA within sixty days of distributions, while retaining the tax benefits of a qualified plan.

S

SAVINGS PERIOD OR PHASE The period in which the owner of a deferred annuity makes payments and accumulates assets.

SECTION 1035 EXCHANGE or **1035 EXCHANGE** A tax-free exchange of:

- An existing life insurance policy for a new life insurance policy, or
- An existing life insurance policy for a new annuity policy, or
- An existing annuity policy for a new annuity policy.

A requirement in a 1035 exchange is that the owner is not in constructive receipt of the surrendered contract value. In cases in which the old and new carriers are different companies, this is accomplished by the owner assigning the contract to the new carrier, which takes delivery of the surrender proceeds, which are then applied to the new contract.

SEPARATE ACCOUNT The insurance company's investment portfolio that supports variable life and annuity contracts. It is an element of added protection to the investor that variable annuity assets are held in a separate account protected from the claims of insurance company creditors.

SERVICE PROVIDER A company that provides any type of service to the plan, including managing assets, recordkeeping, providing plan education, and plan administration.

SIMPLIFIED EMPLOYEE-PENSION PLAN (SEP) A defined contribution plan in which employers make contributions to individual employee accounts (similar to IRAs).

SINGLE PREMIUM ANNUITY An annuity contract that is purchased with a single payment. All immediate annuities and some deferred non-qualified annuities are in this category.

SPLIT ANNUITIES A split annuity is the combination of a single premium deferred annuity and a single premium immediate annuity. The immediate annuity pays a sum each month over a specified period. The deferred annuity accumulates on a fixed interest basis. The objective is that when the immediate annuity is depleted, the deferred annuity has reestablished the starting principal.

STANDALONE LIFETIME BENEFIT (SALB) A living benefit product that provides protection similar to that provided by the GLWB, while adding flexibility with the various types of assets that can be protected.

STEPPED-UP DEATH BENEFIT A death benefit that is increased periodically to protect investment gains.

STRAIGHT LIFE ANNUITY An annuity income option that pays during the lifetime of the annuitant(s) and ceases at the death of the last surviving annuitant.

STRUCTURED ANNUITY A structured annuity, also called a Registered Index-Linked Annuity (RILA), is a variable annuity that credits interest based on the change in price of one or more market indexes. Call options are used to provide the investor with some upside potential and some downside protection. Generally, these products use a “buffer” strategy, where the investor is protected against the first x% of loss, or a “floor” strategy, where the investor is protected from losses after the first x%. Gains are capped based on the level of protection selected by the contract owner; the higher the level of protection, the lower the cap.

SUBACCOUNT The investment funds offered in variable annuity contracts are often called subaccounts. The term refers to their position as accounts held within the separate account of the insurance company offering the variable annuity.

SUBACCOUNT INVESTMENT OBJECTIVE The category of securities representing the principal investment in a given subaccount, for example, aggressive growth, international, money market, or corporate bond.

SURRENDER CHARGE The cost to a contract owner for withdrawals from the contract before the end of the surrender charge period. The surrender charge period typically is five to seven years.

SURRENDER VALUE The surrender value is the amount that is available for withdrawals or contract liquidation.

SYSTEMATIC WITHDRAWAL PLAN A distribution method that allows a variable annuity contract owner to periodically receive a specified amount as a partial withdrawal from the annuity contract value prior to the annuity starting date. Unlike lifetime annuity payments, systematic withdrawals continue until the contract value is exhausted. Systematic withdrawals are taxable to the extent they represent investment gain in the contract.

T

TAX-QUALIFIED RETIREMENT PLAN A retirement plan, such as an IRA, 401(k), or 403(b), that meets specific requirements of the Internal Revenue Code as well as stipulations in various laws, such as the Employee Retirement Income Security Act of 1974 (ERISA), the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), and the Pension Protection Act of 2006 (PPA). In some cases, funding of such plans is through fixed or variable annuities.

TAX-SHELTERED ANNUITIES A type of retirement plan for employees of tax-exempt organizations or schools, which are covered under Section 403(b) of the IRC. Tax-sheltered annuities are funded by pre-tax contributions made through salary reduction agreements. Employers may also make direct contributions on behalf of employees.

TERM CERTAIN ANNUITY An annuity that provides income payments for a specified number of years.

TOTAL SALES or **TOTAL PREMIUM FLOWS** The sum of new sales (all first-time buyers of a contract, including inter- and intra-company exchanges) and additional premiums from existing contract owners.

TRANSFER The movement of assets from one subaccount to another.

TRANSFER FEE The charge for transferring assets from one subaccount to another.

TRUSTEE The individual, group of individuals, bank, or trust company having fiduciary responsibility for holding plan assets.

U

UNBUNDLED CONTRACTS Annuity contracts that permit purchasers to choose and pay for certain optional features they want in their contracts.

UNIT VALUE A measurement of the performance of the underlying funds in a variable annuity, similar to the share value of a stock. Each investment subaccount has a separate unit value. The unit value increases with positive investment performance in the subaccount and decreases with negative investment performance and with asset management and insurance charges.

V

VARIABLE ANNUITIZATION A stream of income payments that vary based on the investment performance of underlying subaccounts.

VARIABLE ANNUITY An insurance company contract into which the buyer makes a lump-sum payment or series of payments. In return, the insurer agrees to make periodic payments beginning immediately or at some future date. Purchase payments are directed to a range of investment options, which may be mutual funds, or directly into the separate account of the insurance company that manages the portfolios. The value of the account during accumulation, and the income payments after annuitization vary, depending on the performance of the investment options chosen.

VARIABLE ANNUITY PAYMENT FLOOR A guaranteed minimum amount for each annuity payment.

VARIABLE ANNUITY UNIT VALUE A measurement of the performance of the underlying funds in a variable annuity, similar to the share value of a stock. Each investment subaccount has a separate unit value. The unit value increases with positive investment performance in the subaccount, and decreases with negative investment performance and with asset management and insurance charges.

VARIABLE INVESTMENT OPTIONS The investment choices available to a variable annuity contract owner. These choices typically include stock, bond, and money market funds.

X

X-SHARE (BONUS) VARIABLE ANNUITIES X-share variable annuity contracts credit an additional amount or bonus to the contract value, which is calculated as a percentage of purchase payments added to the contract at, or subsequent to, contract issue. Contract charges may be higher in X-share products.

W

WITHDRAWAL FEE An administrative fee charged on withdrawals.

WRAP-FEE A comprehensive charge levied by an investment manager or investment advisor to a client for providing a bundle of services, such as investment advice, investment research and brokerage services. Wrap fees allow an investment advisor to charge one straightforward fee to their clients, simplifying the process for both the advisor and the customer.

The Evolution of Annuities

- 225** Roman jurist Gnaeus Domitius Annius Ulpianus produces the first known mortality table for an “annua,” which provided lifetime stipends made once per year in exchange for a lump-sum payment.
- 1600s** Tontines become popular with European governments to pay for wars and public works projects. A tontine gave each participant income for life, with the payments to the survivors increasing as the other participants passed away. Payments ceased upon the death of all the participants.
- 1700s** The British Parliament authorizes annuity sales. Annuities became popular among European “high society” as a form of prevention from a fall from grace, unavailable in other more risky investments.
- 1759** Pennsylvania charters the Corporation for the Relief of Poor and Distressed Presbyterian Ministers and Distressed Widows and Children of Ministers.
- 1776** The National Pension Program for Soldiers was passed in America prior to the signing of the Declaration of Independence. It provided annuity payments to soldiers and their families.
- 1812** The Pennsylvania Company for Insurance on Lives and Granting Annuities is the first American company to offer annuities to the general public.
- 1905** Andrew Carnegie establishes the Teacher’s Pension Fund. This eventually became the Teacher’s Insurance and Annuity Association (TIAA) in 1918 to provide annuities to educators.
- 1930s** Annuities become popular, as concerns about the overall health of the financial markets prompt many to purchase products from insurance companies, which are seen as stable institutions.
- 1930s** New Deal programs encourage individuals to save for their own retirement. The group annuity market for corporate pension plans begins to develop.
- 1952** The first variable annuity is issued by TIAA-CREF for use in college- and university-qualified retirement plans.
- 1959** In *SEC v. Variable Annuity Life Insurance Company*, the Supreme Court holds that variable annuities are subject to federal securities regulation.
- 1960** The first non-qualified variable annuity policy becomes available through the Variable Annuity Life Insurance Company (VALIC).
- 1977** Revenue Ruling 77-85 is issued stating that individual investments in an annuity cannot be directed by the owner.

- 1979** Revenue Ruling 79-335 is issued eliminating the tax-free step-up in basis at death for variable annuity contracts.
- 1980** Revenue Ruling 80-274 is issued ruling that bank CDs cannot be wrapped in an annuity.
- 1980** The guaranteed minimum death benefit (GMDB) is introduced.
- 1981** Revenue Ruling 81-225 is issued stating that publicly traded mutual funds cannot be the underlying investments in a non-qualified annuity.
- 1982** The Tax Equity and Fiscal Responsibility Act of 1982 allows annuities to keep their valuable tax-deferred status, retains the exclusion ratio, which treats annuitization payments as part return of principal and part return of taxable earnings, and changes the taxation of withdrawals from principal first to income first.
- 1984** The Tax Reform Act of 1984 eliminates the double taxation of realized capital gains of separate accounts at the insurance company level.
- 1986** The Tax Reform Act of 1986 disallows non-natural owners of annuities unless they are held by a trust acting as agent for an individual. The capital gain preference tax is eliminated and tax shelter investments are greatly curtailed.
- 1991** The National Association for Variable Annuities (NAVA) is formed.
- 1995** Indexed annuities and the maximum anniversary value (ratchet) death benefit are introduced.
- 1995** Annuity industry sales top \$100 billion.
- 1996** The guaranteed minimum income benefit (GMIB) is introduced.
- 1997** Total annuity assets top \$1 trillion.
- 1998** Bonus variable annuities are introduced.
- 1999** Variable annuity sales top \$100 billion a year for the first time.
- 2000** Variable annuity assets top \$1 trillion.
- 2000** Enhanced earnings benefits (EEBs) and L-share variable annuities are introduced.
- 2002** The guaranteed minimum withdrawal benefit (GMWB) is introduced.
- 2002** The guaranteed minimum accumulation benefit (GMAB) is introduced.
- 2002** The variable annuity industry standardizes net flows (net sales) reporting.
- 2002** Fixed annuity sales top \$100 billion a year for the first time.
- 2004** The guaranteed lifetime withdrawal benefit (GLWB) is introduced.

- 2005** Indexed annuity sales top \$25 billion for the year.
- 2006** The Pension Protection Act of 2006 overhauls the federal pension plan and tax laws, which, among other provisions, allows annuities to include long-term care riders and makes it easier for traditional defined contribution plans to offer annuities to workers by clarifying the “safest available annuity” standard under ERISA.
- 2008** The standalone lifetime benefit (SALB) is introduced.
- 2009** NAVA becomes the Insured Retirement Institute (IRI).
- 2010** IRI membership tops 30,000 financial professionals
- IRI launches first-ever, industry-wide data reporting – uniting Morningstar variable annuity data and Beacon Research fixed annuity data.
- Total annuity assets top \$2 trillion.
- 2011** Variable Annuity assets reach all-time high of \$1.6 trillion.
- IRI research shows that 92% of annuity owners feel well prepared for retirement.
- IRI celebrates its 20th anniversary.
- 2012** Fixed Indexed Annuity sales surpass traditional Fixed Annuity sales for the first time.
- With roughly \$1 billion in sales, 2012 marks the first year of significant sales for Deferred Income Annuities.
- The NAIC endorses the National Association of Registered Agents and Brokers Reform Act of 2012 (NARAB II).
- The NAIC determines that contingent deferred annuities (CDAs) are best written by life insurance companies and subject to existing state laws and regulations applicable to annuities.
- 2013** Deferred Income Annuity sales more than double, reaching \$2.2 billion.
- Total annuity assets top \$2.5 trillion.
- Fixed Indexed Annuities become available through Wirehouses, top \$38 billion in sales.
- 2014** Record Fixed Indexed Annuity sales of \$48 billion propel the industry to growth.
- Deferred Income Annuity sales grow 18% to \$2.6 billion.
- Total annuity assets reach a new all-time high of \$2.7 trillion.
- The U.S. Treasury issues final rules regarding Qualifying Longevity Annuity Contracts (QLACS).

2015 Fixed indexed annuity sales reach 60 percent of fixed annuity sales, and 24 percent of overall annuity sales.

The Department of Labor publishes its final Conflict of Interest Rule – Retirement Investment Advice, defining the term “Fiduciary” under the Employment Retirement Income Security Act of 1974 (ERISA). The rule is effective June 7, 2016 with an applicability date of April 10, 2017.

2016 Fixed annuity sales surpass variable annuity sales for the first time, accounting for 51.7 percent of total annuity sales in 2016.

Fee-based variable annuities are developed at a brisk pace in an effort to provide guaranteed income solutions workable within the DOL fiduciary rule framework.

The Department of Labor Rule faces an uncertain future as President Donald Trump’s administration compels Federal agencies to review regulations, with an eye toward eliminating regulations that are unnecessarily burdensome.

2017 Fixed and variable annuities see sales drop due to uncertainty created by the DOL fiduciary rule.

The industry awaited a decision by the United States Court of Appeals for the Fifth Circuit on the decision by the United States District Court for the Northern District of Texas to uphold the rule. Fifth Circuit Court vacated the rule on March 15, 2018.

2018 The United State Court of Appeals for the Fifth Circuit vacates the DOL Fiduciary Rule.

Annuity sales rise, led by fixed indexed products, as business processes normalize in the wake of the DOL vacatur.

Structured annuities begin to stake out a larger market presence, with sales increasing 22 percent in 2018, to \$11.1 billion from 2017 sales of \$9.1 billion.

2019 The SECURE Act becomes law in December 2019, paving the way for broader inclusion of annuities and guaranteed lifetime income benefits in employer-sponsored defined contribution plans.

Low interest rates create a difficult environment for annuity product development, capacity and profitability, but this also spurs innovation. Structured annuities continue gaining market share, closing the year with \$17.2 billion in sales, a 56 percent gain over 2018.

2020 Sales of Registered Index-Linked Annuities (RILAs, also called “structured annuities”) continue to surge in 2020, growing 26.5 percent from 2019 to hit \$22 billion and 10.6 percent of all annuities sold.

“SECURE 2.0,” officially the Securing a Strong Retirement Act, was introduced by House of Representatives Ways and Means Committee Chairman Richard E. Neal (D-MA) and Ranking Member Kevin Brady (R-TX) in October 2020.

- 2021** RILAs continue to increase in market share as consumers seek yield and protection from market volatility. RILA sales grow 75% over 2020, to over \$38 billion and 16% of total annuity sales. “Defined Outcome” subaccounts are also introduced, embedding the RILA structure in traditional variable annuities within a broader menu of investment options.
- 2022** SECURE 2.0 is signed into law on December 29, 2022, adding additional flexibility and accessibility to help American workers save for a secure retirement. Provisions include expansion of automatic enrollment and escalation, further extension of the Required Minimum Distribution (RMD) age, employer matches for student loan payments, and enabling the creation of ROTH emergency savings accounts within defined contribution plans.

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