Episode #182: How to Maximize Your Income Using an Index Annuity

Video Transcription

Hello, and welcome to another episode of "Money Script Monday." My name is Adam Reyna, and I want to thank you for attending today. Our topic for today is how to maximize your income using an indexed annuity. What we'll talk about today is kind of broadly what an annuity is. We'll get into some of the mechanics of an annuity. We'll look somewhat product-specific and talk about two of the separate accounts and kind of the inner workings of an annuity. Before we get started, I wanted to do just a quick analogy. If you are considering the purchase of an annuity, chances are you're getting close to retirement. What we do is compare your working career in retirement to scaling Mount Everest. When you're scaling Mount Everest- you're preparing, you're doing everything you can to reach the summit, but that's not where your climb ends. Your climb ends when you safely reach the bottom and you've made it. You've then scaled Mount Everest and you made it down safely. Retirement is just like that.

Your working years, you're striving to get to that peak, the pinnacle of your working life, then eventually you stop at the very top, you enjoy retirement, but then you must get down through the rest of your life with the amount of income that you need. If you can't get down that mountain safely or through retirement with the right amount of income that you need, you may not make it and you could run out of money. We're going to show you how to maximize your different sources of income using an annuity. What is an annuity? An annuity can be a promise, a promise to you or your spouse that you'll never run out of money. That your essential expenses are covered. Your mortgage, your healthcare costs, whatever those things that you can't outlive, you want to make sure that that is protected and that you have enough income to get through retirement. That would give you peace of mind. One way we do that is we transfer the risk out of the stock market, out of some sort of investment portfolio and we take away the risk and we get that money over to an insurance company for a promise of income or peace of mind.

The mechanics of an annuity. Let's talk about the relationship between you and the insurance company. When we're using an annuity for a stream of income for retirement, we need that to last 35, 30, 25 years. As long as you're alive, we need you to have that stream of income. What the insurance company is going to do is incentivize you to transfer some assets over, set that income floor, and keep it there for the rest of your life. That's how you get the most value from an annuity policy.

The insurance company incentivizes you to keep your money there over and above a stream of income that you'll never outlive. If your account balance goes to zero, you'll never run out of income. Typically, it's funded with a lump sum from a stock portfolio, 401(k), or IRA. We move that money over in a lump sum. The money you've already accumulated, we transfer the risk to the insurance company, and then we give you that income. There are two phases to an annuity. We have our deferral or accumulation phase and then we have our distribution or income phase. You move that money over five, six years before retirement, you let it defer, and eventually, you start your distribution. You take income from this annuity. It's deferral; you let it park, you earn interest, and have a lot of gains and bonuses. When you're ready to retire or whenever you want that income stream, we tell the insurance company, and they go ahead and provide that for the rest of your life.

Let's talk about the accumulation value versus the income account value. Your accumulation value and your income account value are two simultaneous accounts within one annuity typically. This is somewhat specific but work with your insurance professional on the ins and outs of each annuity that you're looking at. For today, we're going to talk about an indexed annuity with two accounts. Your accumulation value is your walkaway value. I surrender this contract. I don't want it anymore. Go ahead and give me all my money back minus any withdraws or any surrender charges that may be on there. That's your walkaway lump sum. It's typically credited annually, so you have a starting point and an ending point at the beginning of the end of the year. The difference between the growth within the contract provides a percentage of interest and that's what you'd be credited. We usually average about 3% to 5%. It can be used as a death benefit. Whatever's left over that you have not used for your income can be provided as a death benefit to your beneficiary. As we'll see, it's somewhat irrelevant. Your accumulation value typically does go to zero because even if your account balance goes to zero, you'll never run out of income. If you run out of money, you'll never run out of income. If that account balance goes to zero, that's a good thing because then you're living off the insurance company and that stream of income goes for the rest of your life.

Let's talk about the income account value. This is the fun part. The income account value we want to get this as large as possible. The bigger your account value, the more income you'll get. With the account value, when you decide to tell the insurance company that you want to start your income, there's going to be an associated withdrawal rate. For example, you transfer over $750,000, 5 years later your income account balance or income account value is $1 million. They may give you 4.5% of that as a starting point as your annual income. Work with your insurance professional on the exact rates and the ins and outs. That's just a quick example for you there. They want to incentivize you to keep your money there and grow this income account value as big as possible. Many companies will give an upfront bonus, so you'll see an 18% premium bonus.

That means you move over $1 million, instantly, you would get a $180,000 bonus to that income account. While you're deferring during that deferral stage, they'll often offer an interest rate bonus. 250% multiplier. Let's say you got a 5% return from your indexed account; they would credit that two and a half times or you would earn 12.5% on your income account value. You want that to grow as large as possible. That's how you get the most amount of income.

You want to find a product or an insurance company that's going to give you these different bells and whistles to help that grow. Whatever's leftover can also be used as a death benefit account and your income account's typically going to be quite a bit bigger than your accumulation value. Your beneficiary has to make a choice. Do I want the lump sum, or do I want the income account value? The only caveat is they typically have to spread it out over an amount of time, in this case, about five years. One very important thing is you want to have an annuity or a product that has an increasing income because inflation is a real thing, and we want to see growth in your income. Otherwise, a level of income loses purchasing power every year that we realize inflation. Work with your insurance professional on the ins and outs of the annuity, but just know that it's peace of mind. It's that protection that even if you run out of money, you'll never run out of income. Thank you for attending. That’s how we want to maximize your income using an indexed annuity. Thank you.