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Annuities For The Middle Class?

By Eric Rasmussen

Since the market collapse last year, more investors have been turning to annuities—the ultimate chastity belt at a time when wild volatility in the stock market have reined in more promiscuous behavior and risk.

Given the widespread fear in the Great Recession, it's no surprise annuity sales have skyrocketed over the last year.

Year to date, fixed annuity sales (including immediate annuities and indexed annuities) rose to $62.56 billion for the first half of 2009 from $44.89 billion for the first half of '08, according to Beacon Research in Evanston, Ill. If you take the last 12 months from the third quarter of '08 through the second quarter of '09 the sales were $124.36 billion, which almost doubles the $66.6 billion in sales in '07, according to Beacon's president and CEO, Jeremy Alexander.

Amid the lofty new numbers, there is also new survey data from insurance companies that suggests the nonqualified annuity marketplace is not only booming but also has a remarkably pure ownership: middle-class retirees.

A survey of 1,003 U.S. annuity owners recently conducted by the Gallup Organization for the Committee of Annuity Insurers, a coalition of life insurance companies, has revealed that eight in ten annuity owners have household incomes of less than $100,000. Meanwhile, only 4% earn more than $200,000. Go down further in the income band, and you find that 42% of these annuity owners have household incomes of less than $50,000, says Gallup.

Most of those owners, 69% of them, are already retired, up from 58% in 2005. The average age of the annuity holder has risen to 70 from 66, says the poll.

"The average age when they bought these was 52," says Joe McKeever, a partner with the law firm Davis & Harman and counsel to the Committee of Annuity Insurers. "A significant number of them were working when they bought the contract. Most of them, their incomes come down after retirement. But the owners are clearly middle class. … If they're middle-class retirees, they were middle class when they were working."

The question is, should this be a middle-class product, even for security? It's important to keep the Gallup numbers in perspective, say financial advisors, especially for middle-class working people thinking of buying.

If these are pre-retirees considering an annuity, do they, as lower income people, really have extra money to stash away in an annuity after making mortgage payments, education payments, etc.? Have they already maxed out their 401(k)s and 403(b)s?

The numbers by themselves "don't tell you the average," says advisor Morris Armstrong of

Armstrong Financial Strategies in Danbury, Conn. If you're just talking about someone with only $50,000 of income who hasn't even retired yet, he says, "it's hard to get people to increase an IRA, let alone an annuity."

"Face it," he says. "If you have limited income, where are you putting your money in those situations? It costs a certain amount to keep a family or two or three or four. It seems like you should put $5,000 a year into a 401(k). And what is left over to invest?"

McKeever agrees that lower-income investors should probably be taking advantage of qualified plans first. However, he also says that according to the Gallup survey, 35% of the annuity owners surveyed never had access to a qualified plan when they were working.

If they are retirees, on the other hand, there are also reasons to ask whether an annuity is the right choice. Does the client mind the high commission you're paying out to the salesperson? If the clients decide they need their entire kitty back, could they part with the steep surrender charge? Or are they worried that the income for many annuities wouldn't keep up with inflation?

Sometimes, after an advisor has run through all these objections with clients, he or she might still see an annuity as a good deal.

"If you were in the distribution phase [of a qualified retirement plan] and 2008 scared you," says financial planner Rick Fingerman, the president and CEO of Financial Planning Solutions in Newton, Mass., "and you were in mutual funds and you had [a portion of] $250,000 in cash and you were frightened out of the market, it might make sense for you to put that in an annuity. So you can at least say I've got $1,000 a month guaranteed for the rest of my life, assuming the insurance company isn't going out of business."

In the retirement distribution phase, says Fingerman, it's a good idea to get a good handle on fixed expenses using Social Security and pension, and other money that's coming in. "If you've got a shortfall, you can put some of your savings in an annuity," he says. "That could make sense."

Putting *all* your money in it, though, might be a bad play, he says.