LM Federal Credit Union
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Wealth Management & Financial Planning Services

What is an annuity?

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Answer:

An annuity is a contract between you (the purchaser or owner) and an insurance company. In its simplest form, you pay money to an annuity issuer, and the issuer then pays an income stream back to you or to a named beneficiary. Annuities are generally used to provide income in retirement.

In an annuity, your money is tax deferred until you withdraw it. The tradeoff is that if you take your money out before age 59½, you'll usually have to pay a 10 percent early withdrawal penalty to the IRS, unless an exception applies.

Most life insurance companies sell annuities. You pay the insurance company a sum of money, either all at once or incrementally. The type of annuity you own determines whether your money earns a fixed amount or an amount that depends on the equities in which the annuity is invested. At a designated time chosen by you, the insurance company generally begins to send you regular distributions from the annuity's account. Or, you may be able to withdraw the money over time or in one lump sum.

There are many different kinds of annuities. Four of the most common are the following:

- Single premium immediate annuity: You pay the insurance company a lump sum now and begin to receive withdrawal distributions for a period of time you specify. The amount you receive will vary according to the length of time the payments are to last and whether anyone will receive the remaining balance at your death.
- Single premium deferred annuity: You pay the insurance company a lump sum now and defer receiving withdrawals until later. The amount of those distributions will depend on the value of your account at the time your payments begin, the length of time the payments are to last, and whether anyone will receive the remaining balance at your death.
- Additional premium deferred annuity: You send money to the insurance company usually monthly, quarterly, or annually. You defer your withdrawals to a later date.
- Variable annuity: This type of contract is a vehicle for equity investments. You can do a one-time deposit or contribute throughout the life of the contract. You have choices as to how your money is invested in an offering of investment portfolios, and you may invest conservatively or aggressively. The growth of your account value will vary, depending on your choice of investments.

Variable annuities are long-term investments suitable for retirement funding and are subject to market fluctuations and investment risk including the possibility of loss of principal. Variable annuities contain fees and charges including, but not limited to mortality and expense risk charges, sales and surrender (early withdrawal) charges, administrative fees and charges for optional benefits and riders. Variable annuities are sold by prospectus. You should consider the investment objectives, risk, charges and expenses carefully before investing. The prospectus, which contains this and other information about the variable annuity, can be obtained from the insurance company issuing the variable annuity, or from your financial professional. You should read the prospectus carefully before you invest.

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