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## ANNUITY DISCLOSURE MODEL REGULATION

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### APPENDIX A—BUYER'S GUIDE TO FIXED DEFERRED ANNUITIES

**Drafting Note:** The language of the Fixed Deferred Annuity Buyer's Guide is limited to that contained in the following pages, or to language approved by the commissioner. Companies may purchase personalized brochures from the NAIC or may request permission to reproduce the Buyer's Guide in their own type style and format.

[The face page of the Fixed Deferred Annuity Buyer's Guide shall read as follows:]

*Prepared by the National Association of Insurance Commissioners*

The National Association of Insurance Commissioners is an association of state insurance regulatory officials. This association helps the various insurance departments to coordinate insurance laws for the benefit of all consumers.

This guide does not endorse any company or policy.

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It's important that you understand the differences among various annuities so you can choose the kind that best fits your needs. Annuities can be deferred or immediate but this Guide focuses on *fixed deferred* annuity contracts. There is, however, a brief description of two other types of deferred annuities, indexed and variable, as well as immediate annuities.

This Guide isn't meant to offer legal, financial or tax advice. You may want to consult independent advisors.

This Guide includes questions you should ask the company or your agent (a producer, broker, advisor or any other person or entity selling you the annuity). Make sure you're satisfied with the answers before you buy. If you don't understand the answers, ask again, ask the company or ask your state insurance department.

A list of common terms used with annuities and what each means starts on page \_\_\_\_\_. You may refer to that list as you read this Guide, the disclosure and your contract.

This Guide refers to a disclosure you'll receive with your annuity contract. The disclosure summarizes the terms of your contract and defines some of the words used in the contract. It will explain how your annuity increases in value and what charges are taken from your contract. Your agent should go through the disclosure with you so you understand it.

This Guide provides information that applies to all annuities on pages \_\_ to \_\_\_\_. Information about fixed annuities begins on page \_\_\_\_\_.

## BASIC INFORMATION ABOUT ANNUITIES

### What Is an Annuity?

An annuity is a contract with an insurance company. You pay for the annuity (in a single payment or multiple payments) and the insurer promises to pay out money from the annuity to you in a series of payments. Only an annuity can pay an income that can be guaranteed to last as long as you live. In some annuities, you don't receive income payments right away.

An annuity *is not* a savings account. If you buy an annuity, it should be to reach *long-term* financial goals.

All annuities have a *surrender charge* (also known as a withdrawal charge) which discourages you from taking money from your annuity or ending (surrendering) the contract before a certain point in time. The number of years you'll pay a surrender charge when you take money from your annuity and the amount of each year's surrender charge vary from one annuity to the next. The charge is usually a percentage of the premiums you've paid or of the value of the account when you make the withdrawal. The charge can be much more than the interest earned on the annuity in the first few years so it's possible to lose not only the interest, but also some of your principal (the amount of the premiums you've paid) if you make a withdrawal or surrender the annuity. Every fixed annuity offers you a way to access some of your money each year without paying a surrender charge. You can find this specific information in the annuity contract and it's summarized in the disclosure.

### What Are the Different Types of Annuities?

This Guide explains major differences among annuities to help you understand how each might meet your needs.

**This Buyer's Guide focuses on fixed deferred annuities.** If you're interested in a different type of annuity, ask your agent about that buyer's guide.

Annuities differ in several ways:

- How many premiums you pay
- When the company makes income payments to you
- How the money in the annuity earns interest

#### *How Many Premiums You Pay: Single Premium or Multiple Premium Annuities*

You pay the insurance company only one payment for a *single premium* annuity. You make a series of payments for a *multiple premium* annuity; for one type of multiple premium annuity, a *flexible premium* annuity, you pay whenever you want, within set limits.

#### *When the Company Makes Income Payments to You: Immediate or Deferred Annuities*

In an *immediate annuity*, income payments start no later than one year after you pay the premium. You usually pay for an immediate annuity with one payment.

The income payments from a *deferred annuity* often start many years later. Deferred annuities have an *accumulation period* and a *payment period*. During the *accumulation period*, the money you put into the annuity, less any charges, earns interest. The earnings grow tax deferred as long as you leave them in the annuity. After the *accumulation period* ends, the *payment period* (or the *annuitization period*) begins; in the *payment period*, the company pays income to you or to someone you choose.

#### *How the Money in an Annuity Earns Interest: Fixed, Variable and Indexed Annuities*

##### Fixed

During the *accumulation period* of a *fixed deferred* annuity, your money earns interest at rates set by the insurance company or in a way spelled out in the annuity contract. The company guarantees the contract will earn no less than a minimum rate of interest. During the *payment period*, the amount of each income payment to you is set when the payments start and won't change. This Guide describes fixed deferred annuities.

##### Variable

During the *accumulation period* of a *variable deferred* annuity, the insurance company puts your premiums into separate accounts. You choose the accounts, depending on how much risk you want to take. You may choose accounts with no guaranteed returns that are invested in bonds, money market funds or stocks or other equities. You also may have the option to put part of your premiums into a fixed account, with a minimum guaranteed interest rate. During the *payment period* of a *variable annuity*, the amount of each income payment to you may be fixed (set at the beginning) or variable (changing with the value of the separate accounts). If you want to consider a variable deferred annuity, please ask for that guide.

##### Indexed

During the *accumulation period* of an *indexed deferred* annuity, the return on your money depends on a market index. The index is a number that goes up and down as the market the index represents moves up and down. The company credits earnings to your annuity based on changes in the market index you select but guarantees the value of your annuity won't decrease as long as you don't withdraw the money. You also may have the option to put part of your premiums into a fixed account with a minimum guaranteed interest rate. Generally, during the *payment period* of an *indexed annuity*, the amount of each income payment to you is fixed. If you want to consider an indexed deferred annuity, please ask for that guide.

#### **How Do I Decide Which Annuity Is Best for Me?**

Your agent's recommendation of an annuity should be based on his/her knowledge of your current financial situation, tax status, investment objectives and needs. It's important that you discuss with your agent your total financial and life situation so you can decide whether an annuity is a good choice for you. You should ask your agent for a disclosure that's specific to the product you're considering.

The agent will suggest annuities that are suitable for your situation. If you aren't comfortable with the agent's suggestions, explain your concerns. It's important that any annuity you choose be consistent with the amount of risk that you're willing to accept.

Annuity contracts may be broadly categorized by the amount of risk involved. The types of annuities and the level of overall risk for each are:

- |                                |                      |
|--------------------------------|----------------------|
| ○ <b>Fixed Annuity</b>         | <b>Least Risk</b>    |
| ○ <b>Fixed Indexed Annuity</b> | <b>Moderate Risk</b> |
| ○ <b>Variable Annuity</b>      | <b>Most Risk</b>     |

As you think about the risk involved with each annuity type, ask yourself:

- Am I interested in a variable annuity with the potential for higher earnings that aren't guaranteed and willing to risk losing the premiums I've paid?
- Is the guaranteed interest rate of a fixed annuity more important to me, with little or no risk of losing my premiums, in exchange for less potential to earn interest?
- Or, am I somewhere between these two extremes and willing to take more risk in exchange for the opportunity to earn a higher return with an indexed annuity?

You may choose to add benefits known as *riders* to your annuity. Some riders offset some of the risks of owning certain annuities. There usually is an additional cost for riders. Also, some annuities have built-in features that may offset some of the risks of an annuity.

### **How Can I Access My Money?**

Each annuity offers more than one way to access your money: 1) by annuitizing the contract to receive income payments over time, 2) by taking a lump sum payment and *surrendering* your annuity, 3) by taking withdrawals and 4) as a death benefit paid to your *beneficiaries* if you die during the accumulation period. If you take money by making a withdrawal or surrendering your annuity, you'll likely pay fees and may not get back all of the premiums you've paid. The contract and the disclosure tell you how much you can take out without paying a charge and when the charges no longer apply.

One of the most important benefits of deferred annuities is your ability to use the value built up during the accumulation period to receive multiple income payments. After you *annuitize*, you receive income payments for life. Payments are usually made monthly but you may choose to receive them less often. The size of income payments is based on the *accumulation value* in your annuity and the *benefit rate* when income payments start. The benefit rate usually depends on your age and sex as well as the annuity payment option you choose. Payment options usually include payments that continue as long as you live, as long as you and your spouse live or for a set number of years.

There's a table of guaranteed benefit rates in each annuity contract. Some companies have current benefit rates which are greater than the guaranteed benefit rates. A company can change the current benefit rates *at any time*, but the current benefit rates can never be less than the guaranteed benefit rates. When income payments start, the insurance company uses the benefit rate in effect at that time to figure the amount of your income payment.

Another option may be to take a *lump sum payment* from your annuity and surrender or terminate it. If a lump sum payment is a choice, ask when it would be available and how much the payment would be. If it's an option, think about whether a lump sum payment may be a better choice for you than payments over time. In some annuities, there's no charge if you surrender your contract when the company's current interest rate falls below a certain level. This may be called a *bailout option*.

You can make *withdrawals* from your annuity before income payments begin, but you may pay a fee (often a surrender charge). The contract and the disclosure tell you how much you can take out without paying a charge and when the charges no longer apply. Most annuities let you withdraw a percentage of your annuity's value annually (typically 10%) without paying a fee. You may lose any interest on the amount withdrawn, and you may lose part of your principal. After you've owned an annuity for a certain length of time (typically 7 to 14 years), the surrender charge period may end and you'll be able to take money out without paying a surrender charge. Many annuities let you withdraw part of the accumulation value without paying a surrender charge if certain events, such as nursing home confinement or terminal illness, occur.

Annuities have stated maturity dates. When an annuity reaches its maturity date, the contract may automatically expire or renew. You're usually given a short period of time, called a *window*, to decide if you want to renew or surrender the annuity. If you surrender during the window, you won't have to pay surrender charges. If you renew, the surrender or withdrawal charges may start over.

Some annuities have a Market Value Adjustment (MVA) feature. An MVA could increase or reduce your annuity's value if you withdraw more than the penalty-free amount. In general, if interest rates are lower at the time of withdrawal

than at the time the contract was issued, your annuity's value will be increased. If interest rates are higher at the time of withdrawal than at the time of issue, your annuity's value will be reduced. Every MVA calculation is different, however, so check your contract and disclosure for details.

In some flexible premium annuities, a new surrender charge may apply to each premium paid. This may be called a rolling surrender charge.

Finally, if you die during the accumulation period, your *beneficiaries* will receive some or all of the money in your annuity. In some annuities, there's a charge that reduces what your beneficiaries receive. Check your contract and disclosure.

### **Will I Pay Income Tax on My Annuity?**

Below is a general discussion about taxes and annuities. You should consult a professional tax advisor about your individual tax situation.

Under current federal law, annuities receive special tax treatment. Income tax on annuities is deferred, which means you aren't taxed on the interest your money earns while it stays in the annuity. The interest isn't tax free, however; you will pay taxes when you withdraw money. You also may have to pay a 10% tax penalty if you withdraw money before age 59 1/2. Most states' tax laws on annuities follow the federal law.

You also can use annuities to fund traditional and Roth IRAs. If you buy an annuity to fund an IRA, you'll receive a disclosure statement describing the tax treatment. You're unlikely to gain any additional tax advantage by funding an IRA or a qualified retirement plan with an annuity, as an IRA and a qualified retirement plan both are tax deferred regardless of how they're funded.

### **What Is a "Free Look" Provision?**

Many states have laws which give you a set number of days to look at the annuity contract after you buy it. If you decide during that time that you don't want the annuity, you can contact the insurance company, return the contract and get all of your money back. This is often referred to as a *free look* or *right to return* period. The free look period should be prominently stated in your contract and disclosure. Be sure to read your contract carefully during the free look period.

## **FIXED DEFERRED ANNUITIES**

With this basic information about annuities in mind, this section describes the type of annuity you're considering, the *fixed deferred* annuity. First, here's a reminder about what a fixed annuity is. During the *accumulation period* of a *fixed deferred* annuity, your money earns interest at rates set by the insurance company or in a way spelled out in the annuity contract. The company guarantees the contract will earn no less than a minimum rate of interest. During the *payment period*, the amount of each income payment to you is set when the payments start and won't change. While fixed immediate annuities may be available, this Guide describes fixed deferred annuities.

### **How Are Interest Rates Set?**

During the *accumulation period*, your money earns interest. Several different interest rates apply to most fixed deferred annuities. **The insurance company sets the interest rates, which can change.**

#### *Minimum Guaranteed Rate*

Look for the *minimum guaranteed interest rate*. This is the **lowest** rate your annuity can earn. This rate is stated in the contract.

#### *Current Interest Rate*

Interest on your annuity is credited based on the *current interest rate*. If at any time the minimum guaranteed interest rate is higher than the current interest rate, then the company uses the guaranteed rate.

- The current interest rate when you first buy your annuity is called the *initial interest rate*. Ask how long the company promises to pay this initial interest rate; in many annuities, the initial interest rate only applies to the first year you own the annuity. When the rate changes, **it may be lower**.
- Once the initial interest rate period ends, the company credits interest to your annuity based on the *renewal interest rate*. The disclosure tells how the company will set the renewal rate and how often it can change. **The renewal interest rate may be lower than the initial interest rate.**

#### *Bonus Interest Rate*

As an incentive to buy an annuity and to keep it, some companies promise a *bonus interest rate*. A bonus interest rate is higher than the current interest rate, **but the company will only use the bonus interest rate if you meet certain conditions**. For example, if you take a lump sum at maturity or take your money out early, you may lose the bonus interest rate.

#### *Multiple Interest Rates*

*Multiple interest rates* apply to flexible premium annuities. These contracts may apply different interest rates to each premium you pay.

### **What Charges May Be Subtracted from My Annuity?**

Annuities have charges related to the cost of selling and management. These charges may be subtracted directly from the contract value or they may be reflected in lower interest rates. See the disclosure and ask your agent or the company to describe the charges that apply to your annuity. Some examples of charges, fees and taxes are:

- A *contract fee* is a flat dollar amount charged either once or annually.
- A *transaction fee* is a charge for each premium payment or other transaction.
- A *percentage of premium charge* is a charge deducted from each premium paid. The percentage may vary over time.
- Some states charge a *premium tax* on annuities. The insurance company pays this tax to the state. The company may subtract the amount of the tax when you pay your premium, when you withdraw your contract value, when you start to receive income payments or when it pays a death benefit to your beneficiary.

#### *Surrender Charges*

You may take out all or part of the money in your annuity at any time during the accumulation period but you'll likely pay a *surrender charge*. The contract and the disclosure tell you how much you can take out without paying a charge and if the charge no longer applies after you've had the annuity a while. For more information about surrender charges, review the *How Can I Access My Money?* section of this publication.

### **HOW DO I KNOW IF A FIXED DEFERRED ANNUITY IS RIGHT FOR ME?**

The questions listed below may help you decide. You should think about what your goals are for the money you put into the annuity. You also need to think about how much risk you're willing to take.

**These are the questions you should ask yourself.**

How comfortable am I with risk?

How long can I leave my money in the annuity?

Does the annuity let me get money when I need it?

How much retirement income will I need in addition to what I will get elsewhere?

After I buy the annuity, how much money do I need to have available to cover major expenses and emergencies? How much would I have for these expected expenses?

Will I need income payments only for myself or for myself and someone else?

How soon will I need income payments? How much retirement income will I need in addition to what I'll get elsewhere?

If the annuity only earns the minimum guaranteed interest rate, will that be enough income to meet my needs?

Am I comfortable with the length of time that I'll pay surrender charges if I withdraw money from the annuity?

**These are questions you should ask the agent or the insurance company.**

Is this a single premium or flexible premium contract?

What is the guaranteed minimum interest rate?

What is the initial interest rate and how long is it guaranteed?

Does the initial rate include a bonus rate and how much is the bonus?

If there's a bonus, when is it credited and on what amount?

Do I lose any bonus if I take a lump sum rather than annuitize my accumulation value? Are there other ways I could lose the bonus?

What renewal rate is the company crediting on annuity contracts sold last year?

How much are the withdrawal charges, surrender charges and other penalties? How long do they apply?

When is the earliest I can get money out of the annuity and how much can I get?

How much can I withdraw without paying surrender charges or losing interest?

Is there a Market Value Adjustment (MVA) feature in my annuity?

What other charges may be deducted from my premium or contract value?

If I take a lump sum and surrender the annuity, will the accumulated value or the way interest is credited change before I do this?

What happens to the money in my annuity if I die?

How long is the free look or right to return period?

### **FINAL POINTS TO CONSIDER**

Before you decide to buy an annuity, you should review the contract. Terms and conditions of each annuity contract will vary.

Ask yourself if, depending on your needs or age, an annuity and *this type* of annuity are right for you. Taking money out of an annuity may mean you'll pay taxes and/or penalties. If you're exchanging annuities, the new annuity may have new expenses you must pay directly or indirectly. Also, you may pay surrender charges on the old annuity. If you're selling another asset, are there penalties associated with the sale? Will you have to pay taxes on the sale?

Annuities are intended to be a long-term product. Generally, you should keep it long enough to avoid penalties.

If you're buying an annuity to fund an IRA or other tax-deferred retirement program, ask what the advantages are of this approach.

When you receive your annuity contract, **READ IT CAREFULLY!!** Also, read the disclosure the company provides. Ask the agent and company for an explanation of anything you don't understand. Do this **before** any free look period ends.

If you can't get the answers you need from the agent or company, contact your state insurance department.

## ANNUITY TERMS

*Accumulation Period:* The time when the money you put into the annuity, less any applicable charges, earns interest.

*Accumulation Value:* The sum of your premiums plus any interest credited less any charges deducted.

*Annuitize:* Converting the lump sum of the accumulated value of your annuity to a series of payments.

*Annuity:* A contract with an insurance company that pays income to you, usually over time.

*Bailout Option:* A feature in some annuities where there's no charge if you surrender your contract when the company's current interest rate falls below a certain level.

*Beneficiary:* A person who receives part or all of the money in the annuity if the annuitant dies. May also be an organization such as a charity.

*Benefit Rate:* The rate used to determine the size of the income payments you'll receive when the accumulation period ends. Varies by age, gender, and the payment option chosen.

*Bonus Interest Rate:* An interest rate that's higher than the current interest rate and is credited to your accumulation value as an incentive for you to buy an annuity and to keep it. The company may only pay the bonus interest rate if you meet certain conditions, such as annuitizing the accumulated value or not taking money out.

*Contract Fee:* A flat dollar amount that's charged either once at purchase or annually during the annuity.

*Current Interest Rate:* An interest rate set by the company during the accumulation period; can never be less than the guaranteed interest rate.

*Death Benefit:* The annuity benefits paid to the beneficiary upon the death of the contract owner or annuitant.

*Deferred Annuity:* An annuity where your money earns interest for a period of time before it's converted into one or more payments back to you.

*Disclosure:* A document the insurance company is required to give you when it delivers the annuity contract; summarizes the annuity contract, specifies how interest is earned and how all charges are calculated and summarizes

what happens if you take money out before it's scheduled to be paid and how much money you'll lose if you do this.

*Fixed Annuity:* An annuity where your money earns interest at rates set by the insurance company or in a way spelled out in the annuity contract. The company guarantees that it will pay no less than a minimum rate of interest.

*Fixed Indexed Annuity:* An annuity in which the return on your money depends on the market index you choose. The company guarantees the value of your annuity won't decrease as long as you don't withdraw the money.

*Flexible Premium Contract:* A type of multiple premium annuity where, within set limits, you pay as much premium as you want, whenever you want.

*Free Look or Right to Return Period:* A set number of days to look at the annuity contract after you buy it and return the contract to get all of your money back. The number of days is set by state law.

*Immediate Annuity:* An annuity where income payments start no later than one year after you pay the premium.

*Initial Interest Rate:* The current interest rate when you buy your annuity.

*Limited Withdrawal:* A feature that lets you make one or more withdrawals up to a set amount without a charge.

*Market Value Adjustment (MVA):* A feature in some annuities that adjusts the market value if you withdraw more than the penalty-free amount; the adjustment increases your annuity's market value if interest rates are lower at time of withdrawal than when the contract was issued and decreases the market value if interest rates are higher.

*Maturity Date:* The date at the end of your accumulation period in a deferred annuity where you must decide to reinvest, withdraw or annuitize the proceeds. Many guarantees in the contract are tied to this date. If you remove your money before this date you may lose money or receive less money than if you had left your money in.

*Minimum Guaranteed Interest Rate:* The lowest interest rate your annuity will earn.

*Multiple Interest Rates:* Different interest rates apply to each premium you pay; applies only to a flexible premium annuity.

*Multiple Premium Annuity:* A deferred annuity where a series of premium payments are made over a period of time.

*Partial Surrender Charge:* A charge paid if you take out part of the annuity value. (See Withdrawal Charge)

*Payment Period:* The time when the company pays income to you or to someone you choose.

*Percentage Of Premium Charge:* A charge deducted from each premium you pay; may be lower after the contract has been in force for a certain number of years or after all total premiums paid have reached a certain amount.

*Premium Tax:* A tax on annuities that some states charge.

*Renewal Interest Rate:* The interest rate the company uses to credit interest to your annuity after the initial interest rate period ends.

*Required Minimum Distribution (RMD):* IRAs and qualified plans have certain "required" distributions. For IRAs, you must begin to withdraw funds by April 1st of the year following the calendar year you reach age 70 1/2. For qualified plans, withdrawals must begin by April 1st of the year following the later of (a) the year you reach age 70 1/2 or (b) the year you retire.

*Rider:* A benefit added to an annuity contract; changes the annuity's terms or conditions.

*Rolling Surrender or Withdrawal Charge:* A charge in a multiple premium annuity that may apply to each premium paid rather than to the entire accumulated value.

*Scheduled Premium Annuity:* A type of multiple premium annuity where the contract spells out your payments and how often you'll make them.

*Single Premium Annuity:* An annuity bought with only one payment to the insurance company.

*Suitability Review:* A review by your agent to recommend the amount of risk you should take if you buy an annuity and if the product you're buying is appropriate.

*Surrender:* To take all of the money from an annuity and terminate the contract.

*Surrender Charge:* A charge paid if you take out part or all of the annuity value.

*Transaction Fee:* A charge to you for each premium payment or other transaction you make.

*Variable Deferred Annuity:* An annuity where the insurance company puts your money into separate accounts. You decide how the company will invest the money in the accounts, depending on how much risk you want to take.

*Window:* A short period of time to decide if you want to renew or surrender the annuity. If you surrender during the window, you won't have to pay surrender charges. If you renew, the surrender or withdrawal charges may start over.

*Withdrawal Charge:* A charge paid if you take out some of the annuity value. (See Surrender Charge).