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Seasonal Musings

September 2007

Musings In This Issue

Annuity Acuity

**Save Some Trees and
Make the Mailman
Smile**

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Hi Paul,

Welcome to another issue of "Seasonal Musings", the online newsletter from Five Seasons Financial Planning (FSFP). In this issue, we'll be discussing whether there's a place for annuities in your portfolio, and ways to reduce the clutter in your life. As usual, if there are financial planning or investment topics you'd like us to cover in future issues, please drop us a line.

Annuity Acuity

Do Annuities Have a Role to Play?

If there's one investment vehicle that causes more controversy than any other, it has to be the annuity. Opinions among financial professionals are usually divided along the lines of compensation model.

Commission-based brokers and insurance salespeople tend to think more highly of them, and to recommend them more frequently, than Fee-Only financial planners. There's no mystery to this relationship:

annuities typically pay out some of the largest commissions of all financial products.



The vast majority of our clients are still accumulating investment assets rather than drawing down on them. So, I haven't dealt with a client yet where I thought that annuities would help them achieve their financial objectives better than other investment vehicles. The tax deferral and downside protection frequently used to justify the recommendation of an annuity in a taxable account can often be replicated at lower cost. And the negatives of annuities (poor tax treatment on withdrawal, higher expenses, and loss of liquidity) usually overwhelm the positives. Using annuities in tax-deferred accounts before retirement is just plain silly.

But having said all this, I also fully expect in the future to be confronted with client circumstances in which annuities will fit the bill nicely. After all, annuities are unique among investment vehicles in offering a stream of cash flow guaranteed to last a lifetime. With traditional pensions on the decline, the Social Security program looking wobbly, and life expectancies rising, this feature is becoming more scarce and valuable.

So it's when you're starting to think about the distribution phase of your financial life rather than the accumulation phase that annuities may have a role to play. And when I say annuities here, I mean immediate annuities, in which you pay a lump sum in return for a lifetime stream of income starting immediately (as opposed to deferred annuities). There are some academic studies that suggest that new retirees stand a better chance of successfully funding their retirements by allocating 25-50% of their nest egg to an immediate annuity.

As with any financial product, there are well-designed, cost-effective annuities available and there are really expensive, inflexible, and overly complicated annuities out there. Unfortunately, the general investing public gets a lot more exposure to the latter since again that's where commissions are the fattest. To make matters worse, many financial salespeople don't have a very good understanding themselves of the annuities they're pushing ([check this out](#)). This survey probably overestimates their level of competence given the "[Lake Wobegon effect](#)"

A surprisingly large percentage of our client engagements include trying to extricate clients as cost- and tax-efficiently as possible from inappropriate or sub-optimal annuities. If you feel you may fall in this category, or if you'd like to explore how cost-efficient, immediate annuities can replace income in retirement, please drop us a line.

[Save Some Trees and Make the Mailman Smile](#)

[Unclutter Your Lives](#)

Check out [these tips](#) to unclutter your lives.

Five Seasons Financial Planning is a Fee-Only financial planning and investment advisory firm registered with the state of Utah. Five Seasons offers financial planning services on an hourly basis, as well as discretionary investment management. To view past issues of "Seasonal Musings", click [here](#).

One of the benefits of working with a Fee-Only investment advisory firm is full disclosure. To receive a copy of our Form ADV, which details a variety of information about Five Seasons, or our Privacy Policy, please use the contact information below.

Best wishes,

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