Is Outliving Your Retirement Money a Worry?

Houston, Texas
Safe Money Advisory
For Immediate Release

You can now buy insurance to protect you and your spouse against *outliving your money*. This coverage is for the retirement-minded whose biggest fear is living longer than their money. You simply deposit with an insurance company part or all of your retirement money, and they guarantee you, and your spouse, a lifetime annual income. Let's see how this works.

Let's assume you're age 62 and retirement is heavy on your mind. You've been saving money during your working years, and let's say you now have $500,000 to pay for your retirement years. You've determined that you'll need at least $50,000 in guaranteed annual income when you retire at age 66. How could you arrange this lifetime guaranteed income now that will be ready for you in four years?

Let's make this easy by assuming your only other source of income will be Social Security. By using the calculators at www.ssa.gov you've estimated your Social Security benefits will be $25,803 per year. You are interested in getting a guarantee from an insurance company to pay you the remaining $24,197, so you'll have the $50,000 annually you have decided is adequate. The insurance company offers you a fixed index-linked annuity which guarantees that your money will grow by at least 7% annually until you turn it into an income (yes, there are annuities from top-quality insurance companies that will do this). The annuity you have chosen will also pay a 10% bonus when you open the account. Yes, such bonuses are available if you shop. At age 66, the annuity you have selected will guarantee you a lifetime annual income equal to 5.5% of the present amount in your account. Also, some annuities offer protection against inflation.

Since you'll need $24,197 in four years, which will be 5.5% of your annuity's account value, we know that $439,945 will be needed four years hence ($24,197 divided by 5.5%). This is where the math gets complicated, so call your financial advisor. If you invested $305,120 of your $500,000 retirement money with the insurance company today, and they credited you with a 10% bonus and guarantee that your account would grow by at least 7% annually over the next four years, you'd have the needed $439,945 when you retire at age 66. You and your spouse are now guaranteed to never run out of money during your lifetime, plus you have about $200,000 left, and growing, to cover emergencies.

But, what happens if you die too soon? The bad news is that your worries about money are over, but the good news is that your spouse continues getting the income if you chose the joint life option. If you chose the single life coverage, the remainder of your account value goes to your beneficiary. The account value is based on the market index to which your annuity is linked so that you avoid all market loses but participate in the gains. Additionally, you're guaranteed a minimum rate of return by the insurance company even if the market loses every year. You've got upside opportunity without downside risk!

You're set for life because the insurance company must pay you until you die, and Social Security is an entitlement for your lifetime. What's more, you can start, stop and store the annuity income if your circumstances change (win the lottery or get an inheritance) AND there are no current taxes on the earnings until you actually start your income. You've covered your longevity risk without giving up control of your money. Your income is guaranteed for life, but you still have all your other options.

Are these policies fair to the policyholders? Insurance companies are successful because they spread the risk over a large population and price for the "average" outcome. This "average" outcome allows them to make a profit and simultaneously deliver a valuable service by protecting their policyholders against losses they can't afford. In our longevity case, some live too long and benefit greatly while others die prematurely and benefit less. But, if you and your spouse have longevity insurance, you'll have peace of mind knowing you can't outlive your retirement money. Call your financial advisor and talk to him/her about insuring against this risk.

Shelby J. Smith, Ph.D.
March 2008