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TO BE HONEST, MR. JOBS, THE LAST TIME AN APPLE CAUSED SO MUCH EXCITEMENT AROUND HERE INVOLVED ADAM, EVE AND A SNAKE...

It's Open MIC Time!

9:00: AM Pacific Thursday 800 504-8071 Code is 5556463#

Words of Wisdom

. Over the years, I have learned that you never will be the person you can be if pressure, tension and discipline are taken out of your life.

- People always send flowers when someone dies. Give me my flowers now so we can appreciate the beauty together.*
- Our prayers are answered not when we are given what we ask but when we are challenged to be what we can be.*
- There are two words you need to ask yourself repeatedly: **What else?** What else can I do to help improve myself?*
- Yesterday, I made out a “**TICDAA**” list. It means things I cannot do anything about. Once you learn to factor out what you cannot change, you will find more time for the things you have control over. **(we could all learn from this TICDAA....BB)***

.....**James Watson** Football coach for the **North Pole Patriots** (High School, Alaska)

Current VA News, from Morningstar

Hartford continues to **reduce its exposure to variable annuities**, this time by re-allocating investment assets. In May the company filed a change requiring certain contract owners with the Lifetime Income Builder rider to reallocate their investments by October 4th, or face losing the living benefit. This requirement affects selected owners of the Director M lineup. Contract owners will be required to place a minimum 40% of assets in fixed income and a risk-based asset allocation model. This follows last quarter's cash buyout offer covering the same contracts and benefits.

That offer went to owners of the Lifetime Income Builder II rider, who were offered the greater of the contract value on the surrender date, or, if the account is under-water, the contract value plus 20% of the benefit base (capped at 90% of the benefit base). Contracts affected include the Director M series and the Leaders series.

Protective filed notice in that it will limit 1035 exchanges and rollovers from qualified accounts. The limitation went into effect May 20th.

AXA filed a buyback offer in July for owners of certain living benefits on their Accumulator series of contracts issued from 2004 and 2009. The buyback will be executed in September. The offer seeks to have the client terminate either their lifetime GMWB rider, enhanced earnings rider, or other death benefit in exchange for a credit to their account value. The calculation will factor in multiple values and credit an amount to the contract owner's account.

Principal plans to roll out a variable annuity called Principal Lifetime Income Solutions on Aug. 1. The fee is 1.40% and the contract carries an existing lifetime GMWB with a 5% withdrawal rate for a 65-year-old (4.5% joint life).

Spread between Social Security Benefit @ Age 62 and Age 70 (As a % of benefit at Full Retirement Age, by Year-of-Birth)			
Y-o-B	FRA	62	70
		%	%
1924	65	80	115
1925-26	65	80	117.5
1927-28	65	80	120
1929-30	65	80	122.5
1931-32	65	80	125
1933-34	65	80	127.5
1935-36	65	80	130
1937	65	80	132.5
1938	65, 2m	79	131.4
1939	65, 4m	78	132.7
1940	65, 6m	77	131.5
1941	65, 8m	76	132.5
1942	65, 10m	75	131.25
1943-54	66	75	132
1955	66, 2m	74	130.7
1956	66, 4m	73	129.3
1957	66, 6m	72	128
1958	66, 8m	71	126.7
1959	66, 10m	70	125.3
1960+	67	70	124
Source: Social Security Administration			

I was born in 1946, my FRA is 66, so if I take my SS at age 62, I would receive 75% of my FRA (full retirement benefit). At 66 I would receive the FRA and at 70 I would receive 132% of my (FRA) benefit. This simple chart could help you explain your prospects options.

Honor Copyrights



Here is a terrific guide to Social Security from Boston University, be sure and download it....email BU about copies to provide for your clients and prospects. “The Social Security Claiming Guide”

The ***Social Security Claiming Guide*** is available for \$2.15 each (10-99 copies) or \$1.50 each (100 or more copies), delivery included. The *Claiming Guide* brochure is available for \$1.55 each (10-99 copies) or \$0.95 each (100 or more copies), delivery included. To place an order, please contact Amy Grzybowski at amy.grzybowski@bc.edu or 617-552-1677.

http://crr.bc.edu/wp-content/uploads/2011/08/claiming-guide_-070713.pdf

The Baby Boomers are retiring, Social Security Information is hot! Use this fabulous piece as a marketing tool. ALWAYS respect copyrights, the guide is available CHEAP and freight is included.

One of the best handouts to come along in a long time.

BB



Correction

The article below from last week was indicated by me that this had been adopted as code status, not true. It is a PLR and has not gained code status. However, a PLR normally will be grounds for the change to permanent, although not always. It would be reasonable to assume that the PLR will become code status, but as of now it has not.....BB

The IRS recently allowed this change, once again providing benefits from owning an annuity.....BB

Can Changes be made to Your Annuity after Death?

A recent ruling by the IRS allows for the beneficiary of an annuity (specific case in regards to the PLR) to make changes to the inherited annuity.

Beneficiaries who inherit an annuity may now have options thanks to a recent private letter ruling from the IRS.

Rather than being bound by the terms of the original contract, beneficiaries may be able to **exchange inherited contracts** for newer, higher interest paying contracts, according to the IRS under Private Letter Ruling (PLR) 201330016. This indication of change by the IRS can benefit the beneficiary because newer contracts can have lower costs, higher interest or better features such as policy riders.

Prior to the PLR ruling beneficiaries could elect to annuitize the contract within a 12 month period or remove the funds over a 5 year period. Now many more options could possible exist.

If the PLR results in tax code changes, the beneficiary could use an IRS approved transfer (**1035 exchange**) and move the funds from one annuity to another without incurring tax liability. This allows for a wide range of new contracts to be considered and provides for a large array of investment options for the beneficiary.

Traditionally, a PLR is specific to a single question or request but it is not binding. What it indicates is how the IRS is thinking about a specific topic. Generally the PLR will lead the way to actual code changes.

This new PLR shows a clear benefit to owning an annuity; it would allow better management of the annuity by the beneficiaries and provide far more planning options.

Here is a link with more information: http://www.financial-planning.com/news/irs-approves-post-death-annuity-exchange-2686211-1.html?force_pg=/News/

Here is more information on the IRS ruling, see link

IRS Approves Post-Death Annuity Exchange

by: Donald Jay Korn

http://www.financial-planning.com/news/irs-approves-post-death-annuity-exchange-2686211-1.html?force_pg=/News/



Money: What is it good for?

What is more important, money or money as income? From our youth we all dreamed of being a millionaire, didn't we? I was raised in a small town in Idaho, we had 1 millionaire. People would always talk about her (yes, a her) about her cars, her vacations her house and especially the Christmas party she always hosted. My parents went to the party every year; it was all so grand, at least by our small town's standards. One year I got to park cars for the party and earned \$20, a really huge payday for me.

Now as I look back and wonder about being a millionaire I have realized that a big pile of money isn't really an answer, it is what the pile of money can do that is important. I am not speaking of helping our kids or charity; those are all very important things. I am speaking of the pile of money, what should we do with it to make sure it is enough?

Everyone wants to help you invest your pile of money, which will never change. Should we keep our money in the bank? The stock market? Where?

The first question is really simple, a simple question that is not EASY to answer. *What is the purpose of the "pile of money" and what do we want*

it to accomplish? If you can answer that, then you already know the answer.

For me, I made that decision years ago; I decided to forgo the pile in return for income. I bought annuities, lots of annuities. Now my pile of money isn't big but it is a big monthly income and guess what, it comes every month. I can spend every dollar every month if I choose because next month it comes again.

What was that you said? What about leaving funds for the kids, the church, the charities?

I have done that also, I have used a portion of my monthly income to create a large estate once I no longer need money, an estate which will be paid tax free to all of them. I have created a "life insurance" estate. When I die, my heirs will receive exactly what my "annuity money" represents, a big pile of money.

It was an easy decision because in choosing annuities as my investment choice, I removed all chances of risk and all chances of losing money. I also made sure we will have sufficient income for almost any contingency and still have the big pile ready for the heirs.

Smart aren't I? No, not really, what I am is informed, informed about the fabulous benefits annuities can provide. Income, safety, security and a whole lot of stress reduction.

So let's have a look at Income, Income Riders, Annuitization and other options.

What makes people inclined or disinclined to annuitize their 401(k) savings, their annuity or their defined benefit pensions? What features might make annuities more appealing? Does the mere manner of presentation of annuities bias people to purchase or not purchase one?

A team of Ivy League researchers and the **National Bureau of Economic Research** has been working on these questions for more than two years. A member of the team,

Brigitte Madrian of Harvard, presented the most recent iteration of their findings at the Retirement Research Consortium meeting in Washington, D.C. earlier this month.

In part, the [study \(PDF attached\)](#) reinforced what annuity marketers and defined benefit pension sponsors already know: that adding flexibility, such as partial annuitization and variable income streams, would be popular.

It also discovers the concern over annuitization with two facts:

- 1. “will the money last as long as I do?”**
- 2. If the financial backstop (state guarantee funds) were allowed to be explained, more annuities would be chosen.**

In the conclusion of their paper, the authors write:

To increase annuity demand, annuity providers could design products that give beneficiaries more flexibility and control.

Another example is an annuity with **multiple annual bonuses**. Such bonuses could either be pre-selected at the time the annuity was purchased or selected at the beginning of each calendar year. In fact, the payout stream for a given year could be made completely flexible without creating a substantial adverse selection problem.

Other forms of personalization and flexibility could also be adopted, such as limited penalty-free early withdrawals and even asset allocation flexibility (adopting some features of the variable annuity market). Of course, there is a tradeoff between greater flexibility/control and greater complexity. Too much flexibility may drive some consumers away from annuities.

We also find that most consumers prefer **partial annuitization** of their retirement nest egg to either 0% or 100% annuitization. We find that the availability of partial annuitization raises the average fraction of wealth that ends up annuitized.

Framing changes may also increase the appeal of annuities, especially frames that make the option of partial annuitization salient. In addition, frames that downplay investment attributes of annuities may increase annuitization rates.

Finally, participants report that fears of counterparty risk play a large role in their annuitization choices. By adopting regulations that reduce this fear, policy makers may create moral hazard problems from consumers disregarding the financial stability of annuity providers, but they may also increase overall demand for annuities.

The full report is in your notes as an attached PDF.

The summary they concluded was about as expected and the product they silently recommend as near perfect is an **income rider**. Flexibility, knowing underlying guarantees and being able to adjust over time are the primary points.

This Barron's report is slightly dated but the message is current. The actual payout could be slightly different due to the reduction in interest rates this past year. The top two product illustrations are what I am looking at, the bottom is VA and I have no understanding of the numbers and how they coordinate.

BARRON'S COVER Top 50 Annuities By KAREN

HUBE | MORE ARTICLES BY AUTHOR

Americans are eager to lock in steady retirement income. We pick the best annuities from a dizzying array of choices.

FIXED INDEX ANNUITY WITH INCOME GUARANTEE: A portion of assets are pegged to the upside of an index with capped performance and downside protection. Payment is based on the account value or the principal plus the guaranteed rate, whichever is higher.

• Assumes \$200,000 investment by 55-year old male; payout begins at 65.

Company	Rating	Contract Name	10-Year Fixed Interest Rate	First-Year Bonus	Payout Rate	Annual Income Starting at Age 65
Great American Life	A	Valor 10	Simple 10.0%	2%	5.5%	\$22,440
Lincoln National	A+	OptiChoice	Compound 5.0	0	6.5	21,176
American Equity	A-	Bonus Gold	Compound 6.5	10	5.0	20,649
North American	A+	Charter 14	Compound 6.5	10	4.7	20,557
Aviva	A	Balanced Asset Allocation	Compound 6.5	6	5.0	19,898

• Assumes \$200,000 investment by 50-year old male; payout begins at 65.

Company	Rating	Contract Name	10-Year Fixed Interest Rate (Compound)	First-Year Bonus	Payout Rate	Annual Income Starting at Age 65
American Equity	A-	Bonus Gold	6.5%	10%	4.8%	\$28,290
North American	A+	Charter 14	6.5	10	4.7	27,838
Aviva	A	BAA 12	6.5	6	5.0	27,262
Lincoln	A+	OptiChoice	5.0	0	6.5	27,026
Aviva	A	Income Preferred Bonus	6.2	6	4.9	26,317

DEFERRED VARIABLE ANNUITY: Assets grow tax-deferred based on the performance of the underlying investments in stocks, bonds or other securities. Future payouts based on accumulated value. Assumes \$200,000 investment.

Company	Rating	Contract Name	Annual Insurance & Administrative Fees ¹	Surrender Charge	5-Year Avg. Annual Return For Best-Performing Growth Fund ²
Fidelity Investment Life	A+	Personal Retirement	0.25% ³	None	4.78%
Monumental Life	A+	Vanguard Variable Annuity	0.30	None	3.84
Allianz	A	Retirement Pro	0.30	None	3.00
Pacific Life Insurance	A+	Pacific Odyssey	0.40	None	1.73
TIAA-CREF Life Insurance	A++	Intelligent Variable Annuity	0.35	None	4.50
Prudential Life	A+	Premier Advisor	0.55 ⁴	None	4.34
Nationwide Life	A+	Schwab Income Choice	0.65	None	N.A.
Great-West Life & Annuity	A+	Schwab OneSource	0.65	None	2.64
Jackson National	A+	Elite Access	1.00	Yes ⁵	N.A.
Northwestern	A++	Select Variable	1.25 ⁶	Yes	3.82

¹Not including expense ratios on investment options. ²Returns through 4/30/12. ³Fees drop to 0.1% when assets reach \$1 mil. ⁴Insurance fee only. ⁵Waived for a .25% annual fee. ⁶Fee drops to .50% after 8 years. N.A.=Not applicable. Sources: AM Best, Capital Financial Advisory Group, Company reports, Insurance Technologies, Morningstar

Please welcome as our guest

Tom Bradley

Regional Vice President; First Annuity and Insurance Marketing

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888-758-7305 Toll Free

Tom is discussing income riders with us today.

<http://www.marketwatch.com/story/5-key-questions-on-annuity-income-riders-2013-09-03>

From Stan Haithcock

5 key questions on annuity income riders

In a little more than 10 years, income riders have taken the annuity world by storm. There are several key questions to ask before adding this benefit to your deferred annuity.

By definition, an annuity income rider is an attached benefit to a deferred annuity policy that solves for longevity risk by providing a lifetime income stream. Income riders typically have a guaranteed growth rate that can be used for income, and can be flexible from a planning standpoint. The bottom line is that these riders can be confusing, expensive, and should only be considered for income-later planning.

If you draw a line down the middle of a blank sheet of paper, the left hand side would represent the investment side of a deferred annuity. This is typically the separate accounts (aka mutual funds) with a variable annuity or the index option strategy with an indexed annuity. For the record, I don't

care about this side because the choices are limited and you should own an annuity for the contractual guarantees only.

On the right hand side of the ledger is the income rider benefit that is a transfer of risk to the annuity company to pay you a lifetime income stream that starts at your discretion. This amount can only be used for income, and cannot be accessed lump sum. With a few riders your beneficiaries can use this amount as a death benefit, but for this discussion, let's look at this benefit from an income standpoint. Just to confuse things more, income riders vary from carrier to carrier, and product to product. Below are the main questions you need to ask concerning income riders.

1. What is the roll-up rate?

Example: the rollup rate might be 6%, that means the income rider guaranteed account will grow at 6% per year, interest can be simple or compound, \$100,000 growing at 6% each year until accessed for income. The income rider account is NOT the accumulated account value, that account can be more or less based on market conditions.....BB

This is the guaranteed rate that the right hand or guaranteed side of the ledger grows by as long as you are deferring. As soon as you turn on the lifetime income stream, the rate stops. This roll-up rate can be either compound interest or simple interest, and some **annuities offer** upfront bonuses that can be applied to the income rider side as well. Just because a roll-up rate is high doesn't mean that the income payout will be greater than a lower roll-up rate.

These vary greatly but can be for a high as 20 years, at the end of the guaranteed interest period, the interest can go down of years following. The time chosen should match the needs of your prospect.....BB

2. How long is roll-up rate guarantee period?

Some income riders guarantee the roll-up rate for a specific period of time, but can change the rate after that. For example, an income rider could guarantee a 6% annual rate for the first nine years of deferral, but then the guarantee can renew at different rate that cannot go lower than 3%.

Some riders have a guaranteed rate for the life of the contract or to a certain age, and once the policy is issued the terms don't change. For example, one carrier offers a 6% simple interest income rider that allows you to defer until income is turned on, or up to age 95.

Some income riders restrict when the income can start. For example, you can be required to defer for as short as two years and as long as 10 years before you can turn on your income stream. There can also be limitations on when during the year that you can turn the income stream on. Some require you to wait until the contract anniversary date, while others have no restrictions. This is very important to know, and could really cost you if the rules aren't followed.

This factor also varies based on the age of the prospect and time the funds have been on deposit in the annuity.....BB

3. What is the actuarial payout?

This is a very important part of the income rider payout calculation. The actuarial payout is the percentage that is applied to the income rider total dollar amount that determines your lifetime income stream. For example, if your income rider value has grown to \$200,000, and the actuarial percentage is 6 when you turn on the income, then you will receive \$12,000 a year for the rest of your life. All annuity lifetime income payments are based on your life expectancy at the time you decide to receive payments. The actuarial rate is often more important than the roll up rate in determining the highest contractual payout.

Fees are important to understand, but they are not a factor if the account is accessed for income. ...BB

4. What are the fees?

Most riders have a guaranteed roll-up rate for a specific period of time and at certain contractual fee. For example, a 6.5% income rider rate can be guaranteed for 10 years of deferral for a fee of 0.95% per year. **It's important to know that the rider fee is taken out of the accumulation value (investment side), not the rider side.**

Some riders will then offer an option to renew or restart if you want to continue to delay turning on the income stream. For example, a 6.25% income rider with a guaranteed annual rate for 10 years of deferral at 0.95% annual fee, might have an option to renew for another 10 years of deferral at 6.25% with the fee not to go above 1.25%. It's important to know these details because your agent might not be reachable in 10 years, and the home office might not effectively remind you. If you don't tell the annuity company that you want to renew or restart the income rider, it won't happen automatically. Also, there are a few income riders that actually grow at a smaller rate like 4.5% during the deferrals years, and charge no fee at all.

Ratings can depend on your state of residence, Washington (\$500,000) has higher guarantees than does Idaho (\$300,000) etc....BB

5. What are the carrier ratings?

Annuity guarantees, including income riders, are only as good as the company backing them up. It's also important to know that the state guarantee funds that protect policies to a specific level, don't cover income rider valuations. That coverage only guarantees, to a specific dollar amount, the accumulation or investment side of the calculation.

You can visit to nolhga.com to see your state's specific limits.





Big Truck Partners



**Anthony and Chad Owen own *Annuity Income
Illustrator***

<http://www.annuityis.net/Products/AnnuityIncomeIllustrator>

Annuity Income Illustrator



The Annuity Income Illustrator is an innovative annuity illustration and income calculator that displays Fixed Indexed Annuity Income Rider Payouts side-by-side from multiple insurance carriers. The Annuity Income Illustrator is entirely web based and is accessible for licensed Annuity Agents 24/7. Illustrations can also be sent to PDF for later printing or viewing.

View our Product Demo Video and then click Get Started to begin a FREE 15 day trial.

Core Product Features

- ✓ **Highest and Second Highest Income** - Quickly identify the highest and second highest Income Rider income payouts for each deferred year of the annuity contract. Our Income Illustrator displays calculated income and highlights the highest and second highest payouts by carrier product.
- ✓ **Illustrate Multiple Scenarios** - Easily change parameters such as premium, premium qualification, payout type and age to illustrate different scenarios
- ✓ **Illustrate Index Stacking** - For products that allow stacking, you can easily illustrate hypothetical index growth applied to the Income Rider and the associated income payouts.
- ✓ **Support for Multiple States and Carriers** - The Annuity Income Illustrator compares income payouts from multiple carriers and products for 49 states (NY excluded). We update our carriers and products on a regular basis.
- ✓ **Product Variations Included** - Our unique illustration takes into account state, premium, deferral years and age availability related product variations that affect the way bonus, roll up period and roll up rate are applied to the account balance and eventual income payout for each income rider.
- ✓ **Flexibility** - Easily save the Annuity Income Illustration to PDF for later viewing. **View SAMPLE PDF**

Key Benefits

- ✓ **Product Variations Included** - Our unique illustration takes into account state, premium, deferral years and age availability related product variations that affect the way bonus, roll up period and roll up rate are applied to the account balance and eventual income payout for each income rider.
- ✓ **Flexibility** - Easily save the Annuity Income Illustration to PDF for later viewing. **View SAMPLE PDF**

Key Benefits

- ✓ **Save Time and Money!** - Our very competitive monthly subscription cost is a small price to pay compared to the many hours spent manually comparing annuity income rider payouts. As an annuity professional, you are keenly aware of how many annuity products exist and how time consuming it is to look up carrier illustrations for each product in order to determine the highest income payouts. The Annuity Income Illustrator does all the research for you and gives you instant results.
- ✓ **Find the Right Product and Increase Sales!** - Whether you are new to annuity sales or a seasoned professional, every good salesman knows that making the sale is about putting the right product, in front of the right customer, at the right time. The Annuity Income Illustrator helps you by giving you a powerful tool to find just the right product for each customer scenario.

Product Demo Video:



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- Forethought
- Great American
- National Western
- Phoenix
- Security Benefit
- Sentinel Security

Annuity Income Illustrator for state of CO

		Allianz	Allianz Pref	AEL	AIL	ET	FT	GALIC		NWL	NAC			Phoenix			
FIA bonus		MasterDex X 5.0%	366 5.0%	Retirement Gold 8.0%	Income Preferred Bonus 4.0%	Market Twelve Bonus 6.0+2.0+2.0+2.0%	Income 125+ 0%	American Valor 10 2.0%		Ultra Future 9.0%	Charter 10 3.0%			Personal Income Annuity 0.0%			
LIBR bonus		Simple Income Option 1 FIA%	Income Maximizer Option 1 FIA%	LIBR 6.5% FIA%	LIBR 7% FIA%	Income Edge Plus FIA%	Income For Life FIA%	125+ GLWB FIA + 25.0%	Income Secure FIA%	Income Sustainer Plus FIA%	Income Outlook FIA%	Income Outlook Plus & FIA + 5.0%	Income Pay Option 1 FIA%	Income Pay Option 2 FIA%	Income Pay Option 3 FIA%	Income Today FIA + 30.0%	Income Tomorrow 0.0%
Yrs	Age	Income	Income	Income	Income	Income	Income	Income	Income	Income	Income	Income	Income	Income	Income	Income	Income
0	80	\$5,250	\$5,250	Deferral	Deferral	\$4,680	Deferral	\$8,625	\$4,590	Deferral	Deferral	Deferral	Deferral	Deferral	Deferral	\$6,285	\$3,830
1	81	\$5,565	\$5,512	\$5,176	\$5,200	\$4,961	Deferral	\$5,906	\$5,161	\$5,067	\$5,781	\$5,828	\$4,618	\$4,862	\$4,651	\$6,826	\$4,480
2	82	\$5,880	\$5,775	\$5,512	\$5,564	\$5,258	\$5,629	\$8,202	\$5,753	\$5,561	\$6,131	\$6,186	\$4,872	\$4,965	\$4,942	\$6,051	\$5,299
3	83	\$6,195	\$6,038	\$5,871	\$5,954	\$5,574	\$6,115	\$8,612	\$6,365	\$6,071	\$6,498	\$6,412	\$5,140	\$5,288	\$5,251	\$6,218	\$6,632
4	84	\$6,510	\$6,300	\$6,252	\$6,370	\$5,908	\$6,512	\$6,837	\$6,897	\$6,597	\$6,888	\$6,668	\$5,423	\$5,632	\$5,579	\$6,385	\$6,864
5	85	\$6,825	\$6,562	\$7,398	\$7,574	\$6,959	\$7,706	\$7,179	\$7,650	\$7,140	\$7,294	\$7,628	\$6,394	\$6,703	\$6,625	\$7,041	\$7,718
6	86	\$7,140	\$6,825	\$7,879	\$8,104	\$7,376	\$8,207	\$7,538	\$8,328	\$7,699	\$7,724	\$7,934	\$6,746	\$7,139	\$7,039	\$7,221	\$8,226
7	87	\$7,455	\$7,088	\$8,392	\$8,671	\$7,819	\$8,740	\$7,915	\$8,917	\$8,274	\$8,176	\$8,251	\$7,117	\$7,603	\$7,479	\$7,400	\$8,861
8	88	\$7,770	\$7,350	\$8,937	\$9,278	\$8,288	\$9,808	\$8,311	\$9,190	\$8,866	\$8,652	\$8,581	\$7,508	\$8,097	\$7,946	\$7,580	\$9,328
9	89	\$8,085	\$7,612	\$9,518	\$9,898	\$8,785	\$9,913	\$8,725	\$9,364	\$9,474	\$9,153	\$8,924	\$7,921	\$8,623	\$8,443	\$7,894	\$9,844
10	90	\$9,240	\$8,662	\$11,150	\$11,685	\$9,778	\$11,814	\$9,163	\$9,537	\$10,098	\$9,681	\$10,125	\$9,237	\$10,151	\$9,915	\$8,663	\$11,084
11	91	\$9,586	\$8,951	\$11,876	\$11,685	\$10,365	\$12,388	\$9,163	\$9,710	\$10,739	\$10,236	\$10,530	\$9,745	\$10,151	\$10,535	\$8,859	\$11,229
12	92	\$9,933	\$9,240	\$12,647	\$11,685	\$10,987	\$13,172	\$9,163	\$9,884	\$11,395	\$10,820	\$10,951	\$10,281	\$10,151	\$11,193	\$9,289	\$11,374
13	93	\$10,280	\$9,529	\$13,489	\$11,685	\$11,546	\$14,029	\$9,163	\$10,057	\$11,595	\$11,434	\$11,389	\$10,846	\$10,151	\$11,892	\$9,582	\$11,900
14	94	\$10,626	\$9,818	\$14,344	\$11,685	\$12,345	\$14,840	\$9,163	\$10,231	\$11,795	\$12,080	\$11,845	\$11,443	\$10,151	\$12,636	\$9,785	\$12,050
15	95	\$10,972	\$10,106	\$15,200	\$12,747	\$13,708	\$15,768	\$9,163	\$10,404	\$11,995	\$12,760	\$13,345	\$13,222	\$11,117	\$14,704	\$10,449	\$12,932
16	96	\$11,319	\$10,395	\$16,048	\$12,747	\$14,531	\$16,868	\$11,199	\$10,577	\$12,195	\$13,474	\$13,879	\$13,949	\$11,117	\$15,623	\$10,661	\$13,091
17	97	\$11,666	\$10,684	\$16,902	\$12,747	\$15,403	\$17,868	\$11,199	\$10,751	\$12,395	\$14,226	\$14,434	\$14,716	\$11,117	\$16,600	\$10,873	\$13,750
18	98	\$12,012	\$10,972	\$17,751	\$12,747	\$16,327	\$18,868	\$11,199	\$10,924	\$12,595	\$15,011	\$15,526	\$11,117	\$17,897	\$11,310	\$14,168	
19	99	\$12,358	\$11,261	\$18,600	\$12,747	\$17,306	\$19,868	\$11,199	\$11,098	\$12,795	\$16,142	\$16,612	\$11,117	\$18,798	\$11,530	\$14,592	
20	80	\$13,860	\$12,600	\$24,798	\$13,809	\$20,013	\$18,805	\$11,199	\$11,271	\$12,995	\$16,718	\$17,485	\$18,783	\$12,084	\$21,842	\$12,652	\$14,892
21	81	\$14,238	\$12,915	\$24,798	\$13,809	\$20,013	\$18,805	\$11,199	\$11,444	\$13,195	\$17,635	\$18,185	\$19,816	\$12,084	\$21,842	\$12,652	\$14,892
22	82	\$14,616	\$13,230	\$24,798	\$13,809	\$20,013	\$18,805	\$11,199	\$11,618	\$13,395	\$18,599	\$18,912	\$20,506	\$12,084	\$21,842	\$12,800	\$14,892
23	83	\$14,994	\$13,545	\$24,798	\$13,809	\$20,013	\$18,805	\$11,199	\$11,791	\$13,595	\$19,612	\$19,668	\$22,068	\$12,084	\$21,642	\$12,800	\$14,892
24	84	\$15,372	\$13,860	\$24,798	\$13,809	\$20,013	\$18,805	\$11,199	\$11,965	\$13,794	\$20,676	\$20,455	\$23,288	\$12,084	\$21,642	\$12,906	\$14,892
25	85	\$15,750	\$14,175	\$24,798	\$13,809	\$20,846	\$20,251	\$11,199	\$12,138	\$13,994	\$21,793	\$22,793	\$24,648	\$12,084	\$21,642	\$13,435	\$15,281

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Nice pro annuity article (UK)...BB

Shopping around is normal – it should be for annuities too

<http://www.everyinvestor.co.uk/analysis/2013/09/05/shopping-around-is-normal-it-should-be-for-annuities-too-5806/>

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I added highlighting in red and notes...BB

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Annuities Find Favor With More Advisors

SEPTEMBER 4, 2013 • BRUCE W. FRASER

When it comes to financial planning, **it's difficult to find guarantees**. Still, that's exactly what lots of **baby boomers are hoping** for today. Though the stock market has made a spectacular rebound since the depths of the economic crisis in 2009, the effects of the crash linger and many baby boomers remain fearful, seeking out steady income.

Those who witnessed their **retirement nest eggs implode** are still viewing annuities and the income guarantees they provide in a more **favorable** light. As they leave the accumulative phase of their lives and put more stress on financial planning, they have more regard for safety and some form of guaranteed income. It's not so much return on their investment as return of their investment, or at least a minimum amount of it, advisors point out.

"Baby boomers are no longer willing to gamble in the market," says Elizabeth Ruch, a CFP licensee and a veteran advisor with Waddell & Reed in San Diego. "They are looking for **guarantees**. At the same time, they like the flexibility and growth in the market and want to participate."

Annuities are filling some gaps in retirement planning, playing a more pension-like role today, providing needed supplemental income for Social Security and dwindling pension programs.

Fixed And Variable Annuities

Structures for both of the primary types of annuities, fixed and variable, have been upended by the post-financial crisis world. **With fixed annuities, guaranteed payments to the owner are set in advance, eliminating most investment risk.** But ultra-low interest rates have forced insurers to offer meager returns.

With a variable annuity contract, however, some of the **risk shifts** to the buyer, and payments vary according to the performance of the underlying assets. The stock market has rebounded since 2009, but that does not calm people's memories of a decade that witnessed two 50% corrections. Before the financial crisis, many insurers offered principal protection guarantees and automatic increases in the value of clients' original investments over time that forced the companies to absorb huge losses and raise additional capital in 2008 and 2009.

Many leading insurers, including **The Hartford and Sun Life, have exited** the business entirely, while others have placed strict dollar-value limits on the amount of variable annuities they sell. The upshot is that today's guarantees are much less attractive to clients than the previous generation of annuities.

This changing environment is forcing advisors to find annuities that must be right for the clients. "Just like any other financial instrument, an annuity should be a proper fit for a client's portfolio, based on their age, net worth, retirement needs and their financial goals," says planner Philip H. Miller, vice president of Asset Marketplace LLC in Wilton, Conn.

Annuities have their proponents and detractors. "It's easy to get burned," warns Larry Luxenberg, a financial advisor at Lexington Avenue Capital Management in New City, N.Y., who has largely avoided annuities for his clients.

(VA here....BB) "Some have high costs," he says. "Some have a **lack of flexibility**. You may have to stay in them for seven years or more before redemption fees totally go away. You can also have less-than-optimum tax consequences. In some cases, you're converting capital gains to ordinary income tax rates."

Up until recently, many advisors have held back recommending annuities to clients, citing their **complexity and high costs**. Variable annuity providers in particular have been pummeled for imposing high fees while curtailing benefits to stay profitable.

Lately, sales have bounced all over the place. Variable annuity sales totaled \$147.4 billion in 2012—down 7% from 2011—while sales of fixed annuities totaled \$72 billion in 2012, off 11% from the previous year, according to Limra, an insurance industry research firm.

Yet in an environment where fewer clients are retiring with pensions and the bond market offers miniscule returns and potential losses, advisors aren't turning their backs

anymore. In a 2011 Limra study, the number of advisors who thought that a guaranteed income product was an important part of a retirement plan grew by 25% over a two-year period.

By 2020, Limra estimates that Americans age 55 and older will have \$22 trillion in investable assets for retirement income products.

Ruch has stayed an enthusiast through the good times and the bad. “There’s not an annuity I don’t like, but not all annuities are right for all clients,” she says. “The majority of my clients nearing retirement have an annuity in their investment portfolios.”

Catherine Theroux, a spokesperson for Limra, says annuities are a lot more flexible now than they have been in the past in letting clients get access to their assets and income.

“Insurers are recognizing there has been some reticence by consumers in investing their money in a situation where they’d be unable to access it,” she says. “So depending on the contracts, there is more flexibility if you decide to annuitize the process.

“Based on our consumer research,” Theroux adds, “people are very interested in that guaranteed income.”

Retooling Annuities

Insurance companies almost on cue have widened product lines and are rolling out different variations of annuities. AnnuityAdvantage.com, an online service that allows investors to compare annuity products, says they can get a five-year contract whose rates are higher than those of current bank CDs. Investors can also get, guaranteed, a lifetime of income, to be used now or deferred into their retirement. Or they can use annuities to create a tax-deferred account that mimics their IRA or 401(k) to create a nest egg for retirement. There are also multiyear fixed annuity products.

Among the more popular products today are deferred-income annuities and single-premium immediate annuities. Fixed-indexed annuities are also growing in popularity.

One reason fixed annuity products might be more attractive is that their rates have recently crept up. That rise has followed the increase in U.S. Treasury yields after they bottomed out earlier this year, according to wealth manager Gregory L. Olsen, a partner at Lenox Advisors in New York. “This has given deferred income products even a more attractive rate of return,” he says. Many investors are using single-premium immediate annuities to fund life insurance and long-term care insurance, Olsen says.

But it’s not all peaches and cream. **Recently, variable annuities have come under close scrutiny by state insurance regulators.** The **cost of hedging** the downside protection, commonly known as “the floor,” has become more expensive for the annuity

issuers than actuaries originally calculated, says Miller, prompting restrictions to most product lines.

“The variable annuities that had allowed 100% participation for an indexed strategy with downside protection greatly shifts the risk of profitability of that annuity to the insurer issuing the annuity,” he says.

“Margins for variable annuities are tight in a low-return world,” says Luxenberg. **“People are craving guarantees**, but with many annuities they give up a lot of flexibility for that.”

FIAs

Another product starting to make inroads with consumers is **fixed-indexed annuities**.

Adherents speak of these products in the same breath as single-premium immediate annuities and deferred income annuities. Fixed-index annuities, which are tied to different benchmarks, produce high levels of guaranteed income like their fixed siblings, but some people say they have the **advantage of better liquidity** and that investors have more control over their income than they do with other vehicles.

Doug Wolff, president of Security Benefit Life, says **more advisors** are purchasing fixed-index annuities for clients today. These products can be offered with a guaranteed lifetime withdrawal benefit and then coupled with a mutual fund spend-down strategy, and this “can allow for both market participation and security,” Wolff says. He adds that the account values in fixed-indexed annuities are less volatile, so they can be ideal for those who need income growth potential but can’t afford to sacrifice principal protection.

Miller says the majority of his clients are looking at indexed annuities with a 0% to 2% floor and a 4% to 6% participation in an indexed strategy with locked-in annual gains.

Olsen says the annuities he has put clients into, especially in the years before the stock market meltdown, “were an **absolute home run for clients**, so much so that companies are either offering to buy clients out for more than their existing account balance or contemplating doing so in the future.” Indeed, they were such big home runs that those structures and guarantees are no longer available.

But don’t be fooled. Annuities are complex and an ever-changing species of the investment world. “You need to understand their restrictions, the impact of additional fees, surrender charges and other contract restrictions,” says Ruch.

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What Makes Annuitization More Appealing?

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David Laibson

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Brigitte C. Madrian

Harvard University and NBER

Stephen P. Zeldes

Graduate School of Business, Columbia University, and NBER

Latest revision: May 11, 2013

Abstract: We conduct and analyze two large surveys of hypothetical annuitization choices. We find that allowing individuals to annuitize a fraction of their wealth increases annuitization relative to a situation where annuitization is an “all or nothing” decision. Very few respondents choose declining real payout streams over flat or increasing real payout streams of equivalent expected present value. Highlighting the effects of inflation increases demand for cost of living adjustments. Frames that highlight flexibility, control, and investment significantly reduce annuitization. A majority of respondents prefer to receive an extra “bonus” payment during one month of the year that is funded by slightly lower payments in the remaining months. Concerns about later-life income, spending flexibility, and counterparty risk are the most important self-reported motives that influence the annuitization decision.

Keywords: annuity, pension, retirement income, framing

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I. Introduction

Many households resist annuitization. In U.S. defined benefit (DB) pension plans that offer a lump-sum option, between 50% and 75% of eligible DB benefits are taken as a lump sum, even though the annuity is the default option and opting out requires time-consuming paperwork (Mottola and Utkus, 2007; Benartzi, Previtro, and Thaler, 2011; Previtro, 2012; Banerjee 2013). In defined contribution (DC) savings plans, only 10% of participants who leave their job after age 65 annuitize their assets (Johnson, Burman, and Kobes, 2004). This resistance to annuitization is referred to as the “annuitization puzzle” (Modigliani, 1986), since the benefit of buying insurance against outliving one’s savings should create strong demand for annuities (Yaari, 1965; Davidoff, Brown, and Diamond, 2005).

Researchers have explored a variety of rational motives that could explain the low demand for annuities, such as adverse selection (Mitchell et al., 1999; Finkelstein and Poterba, 2004), bequest motives (Friedman and Warshawsky, 1990; Brown, 2001; Inkmann, Lopes, and Michaelides, 2011; Ameriks et al., 2011; Lockwood, 2012), uncertain healthcare expenses (Pang and Warshawsky, 2010; Ameriks et al., 2011; Poterba, Venti, and Wise, 2011), annuity prices (Warner and Pleeter, 2001; Fitzpatrick, 2012), means-tested government benefits (Pashchenko, 2010; Büttler, Peijnenburg, and Staubli, 2011), and the annuity embedded in Social Security and defined-benefit pension plans (Bernheim, 1991; Dushi and Webb, 2004; Beshears, Choi, Laibson, and Madrian, 2011).

In this paper, we take no stand on how much of the annuitization puzzle remains after accounting for these rational motives. We instead focus on the elasticity of annuity demand with respect to annuity product design and choice architecture.¹ To study these issues, we fielded two large surveys in which we elicited hypothetical annuitization choices from individuals aged 50 to 75. We examine 1) what factors people say are important to their annuitization choices, 2) how offering “partial annuitization,” rather than an all-or-nothing choice, influences outcomes, 3) individual preferences over the intertemporal slope of annuity payouts, 4) whether altering the

¹ Other authors have also studied the role of behavioral factors in annuity choice such as recent stock market returns (Chalmers and Reuter, 2012; Previtro, 2012) and framing (Brown, 2008; Brown et al., 2008; Agnew et al., 2008; Brown, Kapteyn, and Mitchell, 2012).

framing² used to describe options influences annuitization choices, and 5) whether there is demand for an annuity product that makes an extra “bonus” payment during one month of the year that is funded by slightly lower payments in the remaining months.

The use of surveys such as these has advantages and disadvantages. On the positive side, we can ask questions that directly measure specific preferences, including preferences for products not available on the market. We can also examine choices in economic environments that differ from the current one. On the negative side, the choices people make do not influence their actual life outcomes, so the results may not correspond to the choices people would make in real-life settings. Surveys like ours provide a starting point for designing field experiments with larger stakes.³

Five findings emerge from our surveys. First, there are three considerations that respondents report being most important for their decision about whether or not to annuitize: a desire to “make sure I have enough income later in life,” a desire for “flexibility in the timing of my spending,” and being “worried about [the] company not being able to pay me in the future.” Current regulations ban insurance companies from mentioning back-stop state funds in their marketing of annuity products. While such bans may reduce moral hazard problems by encouraging consumers to be selective, they may also have the perverse effect of decreasing annuity demand. We provide new evidence that this latter effect is important.

Second, we find that a substantial fraction of people choose partial annuitization when it is offered, and that offering partial annuitization rather than an “all-or-nothing” annuitization choice increases both the percentage of people choosing any annuitization and the average percentage of pension balances that are annuitized. Many DB pension plans offer individuals the choice between taking a lump sum and an annuity.⁴ The U.S. Treasury Department recently

² We abuse the “framing” terminology slightly by using it to describe some treatments that not only present the choice in a different way, but also provide additional information.

³ Arguably, survey responses from those who are more likely to be in a position to purchase annuities would correspond more closely to real-life choices. All of our results on framing treatment effects and demand for alternative annuity products are similar when restricting the sample to those who have net worth above the sample median.

⁴ A 2011 Aon Hewitt survey of 227 DB plan sponsors found that over 40% offered a lump sum option, and over 20% more responded that they were “very likely to implement” or “somewhat likely to implement” a lump sum payment option in the future (Aon Hewitt, 2011). It is thought that many employees perceive the annuitization versus lump sum choice as being an “all-or-nothing” choice (<http://www.treasury.gov/press-center/press-releases/Documents/020212%20Retirement%20Security%20Factsheet.pdf>).

proposed a new regulation to make it easier for DB plans to offer a combination of an annuity and a lump sum (Federal Register, 2012). Our findings suggest this proposal will increase annuitization in plans that already offer a lump sum withdrawal option.

Third, we find that holding the present value of expected payments fixed, very few respondents choose declining real income paths. Our respondents prefer flat or rising real income paths. This result underscores how puzzling the dearth of inflation-indexed annuities in the marketplace is. This result also contrasts with the empirical fact that holding household composition fixed, real consumption declines by about 2% per year during retirement (Hurd and Rohwedder, 2011). We also find that making salient the effects of inflation on real payout values increases the demand for cost of living adjustments (COLAs).

Fourth, we find that two framing changes significantly reduce demand for annuitization relative to a neutral frame: one that focuses on flexibility and control, and a second that focuses on investment attributes. Four other framing changes do not have a significant effect on annuitization: explaining that the annuity being offered is a better deal than what could be purchased on the open market, presenting the total expected undiscounted lifetime payments from the annuity, explaining that the annuity provides insurance against outliving one's savings, and explaining that the annuity transfers money from states where one is dead and the value of money is low to states where one is alive and the value of money is high.

Finally, we find that 60% of our subjects prefer a product that pays an annual bonus in a month of their choosing over a product with a traditional uniform monthly payout. Annual bonuses expand annuitants' control over their high-frequency payout streams without jeopardizing the low-frequency withdrawal restrictions that make longevity insurance possible. The preference for such a product is consistent with subjects' responses that wanting "flexibility in the timing of my spending" is an important factor in their annuitization decision. Allowing more customization of payout streams may increase annuity demand. Other customization schemes are easy to imagine, such as multiple intra-year bonuses or age-contingent payout patterns.

The remainder of the paper is structured as follows. In Section II, we describe our two surveys. In Section III, we present summary statistics on our sample, and in Section IV, we present our empirical results. Section V concludes by discussing the implications of our findings for the design of pensions and annuity products.

II. Survey design

We designed two surveys and retained the online survey firm Toluna to administer them to 1,000 (Survey 1) and 4,130 (Survey 2) U.S. residents ages 50-75 in August 2011 and June 2012, respectively.⁵ U.S. macroeconomic conditions were similar in both periods, characterized by a tepid recovery from a deep recession. The seasonally adjusted trailing one-year GDP growth rate was 1.6% in the third quarter of 2011 and 2.1% in the second quarter of 2012. The unemployment rate was 9.0 % in August 2011 and 8.2% in June 2012. The trailing one-year S&P 500 total return was higher at the beginning of August 2011 than at the beginning of June 2012 (19.7% versus -0.4%).⁶ The median times taken to complete the surveys were 13 minutes (Survey 1) and 8 minutes (Survey 2). Participants in both surveys made hypothetical choices about pension income in retirement. They then ranked the importance of different reasons for their choices and answered a set of demographic questions during the same online session. The full surveys are available in an online appendix.

A. Survey 1

Survey 1 asked participants to make choices under the following hypothetical scenario: “Just before you retire at age 65, you are working for a company that will give you pension payments every month for the rest of your life after you retire. This income is guaranteed, but the payments will stop when you die. You will also receive Social Security benefits every month for the rest of your life after you retire.” Note that this scenario is like that of a traditional DB pension plan.

Because one of the main issues we wished to explore in this survey was preferences over real annuity payment growth rates, we told respondents to assume that inflation would be 2% for the rest of their lives. We described inflation as follows: “With inflation, prices rise, so you get less for your money than you used to. For example, suppose a basket of groceries costs you \$100 today. A year later, the same groceries will cost you \$102. The price of the groceries has gone up

⁵ Participants were part of a large panel maintained by Toluna who are paid for their participation in each survey. We ran two separate surveys because our research program evolved over time.

⁶ Based on the evidence of Previtro (2012), it is possible our respondents’ baseline desire to annuitize was lower in Survey 1 than in Survey 2 because of the higher prior stock market return in August 2011.

because there has been inflation.” They were also told that “the interest rate will be 5% for the rest of your life.”

Participants made choices about the intertemporal slope of their annuity payouts, whether to receive intra-year “bonus” payments, and how much of their pension stream to cash out and receive as a lump sum. In each case, the present value of the options’ expected payouts was \$330,000, based on the stated interest rate and Social Security mortality tables (averaging male and female mortalities together).⁷ In calculating annuity payouts, we included no fees or markups for costs. In order to avoid having responses be influenced by any negative association participants might have with existing annuities, nowhere in the survey did we use the word “annuity” or “annuitization.”⁸

Slope of annuity payouts

In the first question, participants were told: “Suppose the company lets you choose between the following two retirement income options. The total cost to the company of providing these lifetime payments to you is expected to be *the same* under either option.” The two options were the following:

A) Match-Inflation Income: “Your first year of monthly payments will sum to \$24,200. Your monthly payments will rise by 2% each year for the rest of your life. The increase in your payments will match the increase in prices (inflation).”

B) Steady Income: “Your first year of monthly payments will sum to \$29,000. Your monthly payments will stay the same for the rest of your life. Because inflation is 2% each year, the amount you can buy with your income will fall by 2% each year.”

Below these descriptions and before participants were asked to make their choice, subjects were shown three graphs. The first (see Figure 1) was a graph depicting the likelihood that a person aged 65 today will live to at least age 70, 75, 80, 85, 90, 95, and 100. The graph’s mortality probabilities were the average of male and female mortalities. The second was a graph

⁷ The mortality data came from “Life Tables for the United States Social Security Area 1900-2100,” Actuarial Study No. 120, which can be found at <http://www.socialsecurity.gov/OACT/NOTES/as120/TOC.html>.

⁸ The cost of not using the terms “annuity” and “annuitization” is the risk that participants who were familiar with the terms could have become confused about whether our failure to use them implied that the product being offered was something different from an annuity.

showing how much something that costs \$1 today would cost in the future, from ages 65 to 100 (see Figure 2). The third graph (see Figure 3) showed the yearly nominal amount received under each option from ages 65 to 100.

Participants were then asked to make another choice between two options:

A) Match-Inflation Income, as described in the previous question

B) High-Growth Income: “Your first year of monthly payments will sum to \$19,900.

Your monthly payments will grow by 4% every year. The increase in these payments will be larger than the increase in prices (inflation).”

Between the description of the options and where participants were to indicate their choice, we showed a graph depicting the yearly nominal amount received under each option from age 65 to 100, and we provided hyperlinks to the previously shown graphs of mortality probabilities and inflation in case participants wished to review them.

Bonus payments

Participants were asked two questions about the addition of bonus payments to their income options. The first question asked participants to choose between the following two options:

A) Match-Inflation Income: “In the first year, you will receive \$2,000 every month. This monthly payment will grow by 2% every year for the rest of your life, matching the increase in prices.”

B) Match-Inflation Income with Bonuses: “In the first year, you will receive \$1,900 in every month except for one, when you will get \$1,900 plus an extra \$1,200. You can choose in which month the \$1,200 bonus is paid. This month might be a time when you often want to spend extra. For example, you might like to travel somewhere warm or spend extra money during the December holiday season. The regular monthly payments and the bonus will each grow by 2% every year for the rest of your life.”

Participants were told, “The total cost to the company of providing these lifetime payments to you is expected to be *the same* under either option.” Participants who chose Match-Inflation Income with Bonuses were asked to choose in which month they would like the bonus to be paid.

Participants were then asked to choose between the Match-Inflation Income plan and an income stream with an annual bonus that declined at the end of each decade of life. Again, both payment paths had the same expected present value. We wished to see whether a declining intertemporal payout slope would be more appealing if the decline were justified as a declining travel bonus. The description of the declining bonus was as follows:

B) Match-Inflation Income with Travel Bonuses: “You will receive \$1,800 every month in the first year. These monthly payments will grow 2% each year for the rest of your life. From age 65 to 69, you will receive an extra \$3,000 every June to use for traveling (or whatever else you want). During your 70s, you will receive an extra \$2,000 every June. During your 80s, you will receive an extra \$1,000 every June. Because you probably won’t be doing much traveling in your 90s, there is no travel bonus after age 89.”

Lifetime income stream versus a lump sum

We included three questions asking participants to choose what percent of their annuity benefit to cash out as a lump sum. The first question asked participants about the Match-Inflation income stream, offering three cash-out options: A) “0% Cash Out,” which gave participants monthly payments that summed to \$24,200 in the first year and increased 2% annually, but no lump sum payout, B) “50% Cash Out,” which gave participants \$165,000 immediately plus monthly payments that summed to \$12,100 in the first year and increased 2% annually, and C) “100% Cash Out,” which gave participants \$330,000 immediately and no other payment for the rest of their lives. Participants were told the three options had the same expected costs to the company. Participants were shown a graph (see Figure 4) of the nominal annual payouts they would receive (excluding any lump-sum payment) under each option, from ages 65 to 100.

The second and third questions asked about cash-out rates for the Steady Income and High-Growth Income annuities described above, letting participants choose in each case among “0% Cash Out,” “50% Cash Out,” and “100% Cash Out” options after seeing a graph of the

nominal yearly payout amounts (excluding any lump sum) they would receive from ages 65 to 100 under each option.

Exit questions

After answering all of the annuity choice questions, participants were asked to rate on a six-point Likert scale (0 for not important, 5 for very important) the importance of eleven potential reasons for their cash-out choices. Participants were also asked about their life expectancy relative to the average person of their age and a set of demographic questions. The survey concluded with two questions related to the clarity of the survey. The first asked whether respondents thought the questions were clear or confusing on a scale between 0 (completely clear) and 5 (completely confusing). The second question had an open-response box for respondents to explain what, if anything, they found unclear or confusing. Eighty-seven percent of Survey 1 participants reported that the survey was “clear” or “mostly clear,” whereas less than 1% reported the survey to be “mostly confusing” or “completely confusing” (see Table 1).

B. Survey 2

In Survey 2, participants were also asked to make annuitization choices based on a hypothetical retirement scenario. This scenario, which is different than the one presented in Survey 1, was described in the first page of the survey:

“Suppose that you are 65 years old. You are about to retire and have accumulated \$500,000 in the pension plan at your current employer. Your employer wants to know whether you prefer to receive this balance as a lump sum payment right now (in other words, a single \$500,000 payment) or as a stream of fixed payments over your lifetime, which your employer calls the guaranteed lifetime income option. This stream of fixed payments is based on current market interest rates. The fixed payments won’t change in the future even if market interest rates do change.”

This wording describes the pension benefit as a dollar accumulation rather than as an accrued income stream. Thus, Survey 2 puts the respondent in a setting more like that of a cash balance or DC pension plan, rather than the traditional DB setting of Survey 1. We also put respondents in their current macroeconomic environment, with all its uncertainties, instead of fixing the future inflation and interest rates as in Survey 1. We made this choice because we wished to

study the demand for COLAs, and a significant benefit of a COLA is the hedge it provides against inflation risk.

In Survey 1, we provided only single life annuities, regardless of marital status. In Survey 2, we offered single life annuities to unmarried respondents, and joint and 100% survivor annuities to married respondents. As in Survey 1, nowhere in Survey 2 was the word “annuity” or “annuitization” used. The annuity option was described throughout the survey as a “guaranteed lifetime income option.”

We based Survey 2’s annuity payouts on actual price quotes from Western National Life Insurance as of March 1, 2012 for a \$500,000 annuity.⁹ For participants who were single, we averaged the monthly payout for the male single life annuity (\$2,790.74) and the female single life annuity (\$2,627.87) and multiplied the average by 110%. For participants who were married, we multiplied the joint and 100% survivor annuity monthly payout of \$2,378.20 by 110%. We multiplied the monthly payouts by 110% to account for the likelihood that an annuity purchased through an employer charges lower fees and to ensure that the annuity we were offering would be more generous than anything available on the open market—a feature necessary for the Good Deal treatment described below. The final monthly payout offered for somebody annuitizing 100% of his or her balances was \$2,981 per month for single survey participants and \$2,616 for married participants.

Participants were randomly assigned to one of eight different treatment arms¹⁰:

- *Minimal Framing baseline*: Participants could choose to take 0%, 25%, 50%, 75%, or 100% of their \$500,000 balance as a lump sum. They indicated their annuitization choice by clicking one of five buttons that were ordered from 0% cash-out on the far left to 100% cash-out on the far right. A horizontal axis with an arrow on each end was shown above the buttons. The left end of the axis was labeled “Lower lump sum/More guaranteed income” and the right end of the axis was labeled “Higher lump sum/Less guaranteed income.” (See Figure 5.) The remaining treatments were identical to the Minimal Framing baseline except in the ways described below.

⁹ At that time, this was the most competitive quote on the Hueler Income Solutions website, incomesolutions.com.

¹⁰ One treatment we did not implement is making salient to respondents that Social Security provides a real annuity. We suspect that such a treatment would have reduced annuity demand, although we have no empirical evidence on this matter.

- *All or Nothing treatment*: Participants were only allowed to choose to annuitize their entire \$500,000 balance or receive a \$500,000 lump-sum payment. This treatment showed no horizontal axis.
- *Good Deal treatment*: This treatment was designed to overcome any reluctance to annuitize due to the fear of foregoing a better deal elsewhere. The following text was added to the description of the annuity: “The guaranteed lifetime income option gives you higher payments than you would get by buying an identical product from an insurance company because your employer will not charge you fees.”
- *Total Payments treatment*: The motivation for this treatment was the hypothesis that the reluctance to annuitize may partly be due to the contrast between the large size of the lump sum and the small size of the monthly annuity payment. If this is the case, highlighting the undiscounted expected total payments from complete annuitization, which are larger than the \$500,000 lump sum amount, may increase annuitization. We added the text, “The average individual who chooses 100% guaranteed income will receive total lifetime payments of \$ x .” The number x was the expected undiscounted total lifetime payments of a 100% annuitization choice, which was \$695,765 for single participants and \$775,382 for married participants.¹¹
- *Investment Framing treatment*: Brown et al. (2008) find that an investment frame discourages annuitization relative to a consumption frame. In this treatment, we included a discussion of how the rate of return would vary with longevity: “Under the guaranteed income option, you get a higher return on your \$500,000 investment if you die old and a lower return if you die young. Under the lump sum, you get the same return whether you die young or old.” We relabeled the axis to show “Higher return if you die old/Lower return if you die young” on the left side, and “Same return whether you die young or old,” on the right side. This frames the annuity as risky, rather than emphasizing its role in providing insurance.

¹¹ We used the average of male and female mortality rates to calculate this expectation for singles, and assumed that married spouses were both 65 years old.

- *Flexibility and Control treatment*: Annuities may be unattractive because they require giving up control of one’s investments and the timing of one’s spending. We added the following language about flexibility and control: “Choosing a bigger lump sum gives you more control over your investments and more flexibility over the timing of your spending.” We changed the axis labels to “You have less control and less flexibility” on the left side and “You have more control and more flexibility” on the right side.
- *Longevity Insurance treatment*: The Investment Framing treatment framed annuities as a risky choice. The Longevity Insurance treatment framed annuities as a risk-reducing choice. We added the following text: “Choosing more guaranteed income gives you more assurance that you will not outlive your savings, since the monthly payments will continue as long as you live.” We changed the axis labels to “Less risk of outliving your savings” on the left side and “Greater risk of outliving your savings” on the right side.
- *Mortality Credits treatment*: Reluctance to annuitize may be driven by a failure to realize that annuities have the attractive property of transferring money from low marginal utility states to high marginal utility states. We added the following language to explain this: “The monthly payment from the guaranteed lifetime income option is much higher than the interest you would receive from investing the lump sum. The guaranteed income option stops payments when you are no longer alive. In return, the guaranteed income option delivers very high pay-outs as long as you live. You are giving up payments when you are no longer alive (and don’t need the money) and receiving extra-large payments as long as you are alive (and need the money).”

After making an annuitization choice, participants were shown a graph of the likelihood that a person aged 65 today would live to at least age 70, 75, 80, 85, 90, 95, and 100. They were asked to again elect how to receive their pension payment, with the qualification that it was fine to give the same answer as the previous question. The purpose of this second elicitation was to see whether unrealistic longevity expectations were affecting the annuitization choice.

Participants in every treatment arm were then asked about a cost-of-living-adjustment provision. We presented the following scenario: “Now suppose that your employer only offers a guaranteed lifetime income option. But you can choose whether you want a cost-of-living

adjustment (COLA) to your payments.” Each participant was randomly assigned (independent of their assignment to the previous treatments) to one of three versions of the COLA question:

- *Minimal Inflation Information baseline*: Unmarried participants were told, “If you don’t choose a cost-of-living adjustment, then your monthly pension payment will be \$2,981 a month for the rest of your life. If you do choose a cost-of-living adjustment, then your first monthly pension payment will be \$2,033 a month, but this amount will increase over time at a rate equal to the inflation rate (as measured by the Consumer Price Index).” Married participants had the two dollar figures replaced with \$2,616 and \$1,784. Participants were then asked whether they preferred a COLA over no COLA.
- *Inflation Compounding treatment*: Some people may not fully understand what inflation is. In addition, many people underestimate how quickly exponential series grow (Eisenstein and Hoch, 2005). Therefore, they may be unaware how much low levels of annual inflation will erode the purchasing power of a dollar over long horizons. In this treatment, we added to the Minimal Inflation Information baseline text a slightly fuller explanation of inflation and a calculation illustrating the long-run power of inflation. The following text was appended to the description of the no-COLA option for unmarried participants: “This means that as the cost of living increases, \$2,981 per month will buy fewer goods and services. For example, if the cost of living increases by 2% per year for the rest of your life and you don’t have a cost-of-living adjustment, your monthly pension payment will buy 33% fewer goods and services at age 85 than it does at age 65.” The text for married participants was analogous. The COLA option description had the following additional sentence: “So your monthly payment will buy about the same amount of goods and services at every age in the future as it does at age 65.”
- *Inflation Compounding With Graph treatment*: This treatment was identical to the Inflation Compounding treatment, except we also included a graph of what nominal payments would be from age 65 to 100 for the annuity with and without the COLA.

We set the initial monthly payment amount for the annuity with a COLA in the above questions to be 68.2% of the non-COLA annuity’s monthly payment. We computed this ratio using June 6, 2012 quotes from the Principal Life Insurance Company for a \$500,000 joint and

100% survivor annuity with and without an inflation adjustment based on changes in the Consumer Price Index for All-Urban Consumers (CPI-U).¹²

After answering the annuity choice questions, Survey 2 participants were asked to rate the importance on a six-point Likert scale (0 for not important, 5 for very important) of ten reasons for their lump sum versus annuity choices. These reasons mostly overlapped with those in Survey 1. Participants were also asked questions about their life expectancy, demographics, and the clarity of the survey that were identical to the Survey 1 questions. As with Survey 1, the vast majority (93%) of Survey 2 participants reported that the questions were understandable and clear, and less than 1% found the survey to be “mostly confusing” or “completely confusing” (Table 1).

III. Summary statistics

Table 2 presents summary statistics on participant demographics and relative life expectancy in Surveys 1 and 2. The two survey populations are very similar.¹³ The mean age is 59.5 years for Survey 1 and 59.6 years for Survey 2. In both surveys, 50% of participants are male, 55% are married, and the average number of children is 2. Somewhat more Survey 2 respondents are retired than Survey 1 respondents: 40% versus 36%. Almost 40% of participants have a DB pension, and about 70% own a home. The median net worth for participants, which we measure with considerable noise and for only about three-quarters of our sample, is \$162,500 in Survey 1 and \$150,000 in Survey 2, and the respective means are \$298,217 and \$286,594.¹⁴ College graduates comprise about 40% of both samples, and 12 to 13% of the sample have a post-graduate degree.

¹² The annuity monthly payouts (obtained via the Hueler Income Solutions web site) were \$2,232.42 per month with no COLA and \$1,524.44 per month with a COLA, giving a ratio of 68.2%. The CPI-U rider had no cap on the increase, and the monthly payment would be adjusted annually on the contract anniversary date. If the CPI-U were negative, the periodic benefit would not decrease. Future years' monthly payments would not increase until CPI-U exceeded its previous high.

¹³ There is no overlap in the individuals included in Survey 1 and Survey 2.

¹⁴ Out of the 1,000 participants in Survey 1 and 4,130 participants in Survey 2, there were 752 and 3,169, respectively, who responded to all of the questions necessary to calculate net worth. The surveys had participants give interval responses for the components of net worth. To calculate total net worth, we map each interval to its midpoint except in the case of intervals without an upper bound, which we map to a value equal to 150% of the lower bound of the upper interval.

We asked respondents how much longer they expected to live relative to others their age. In Survey 1, 36% of participants said they expected to live longer than the average person their age, 54% said they expected to live about the same amount of time as the average person their age, and 10% said they expected to die sooner than the average person their age. Responses to Survey 2 were similar: 34% of participants anticipated a relatively long life, 54% anticipated a life about as long as that of an average person of the same age, and 12% anticipated a relatively short life. The greater number of people anticipating a relatively long life is not necessarily evidence of optimistic bias, since our sample is more educated than the typical American in this age bracket, and longevity is positively correlated with education (Meara, Richard, and Cutler, 2008). The U.S. Census reports that among all 45 to 64 year olds in the U.S. in 2007, only 29% were college graduates.

Consistent with the importance of adverse selection in annuity markets, the average percent of balances annuitized was significantly lower for respondents with lower self-reported life expectancy. Averaging the five lump sum versus annuity decisions in the two surveys, those who expected to die sooner annuitized 47% of their balances, those who expected to live about the average length annuitized 56%, and those who expected to live longer than average annuitized 57% (not shown in tables). The difference between the lowest life expectancy group and the others is significant at the 1% level.

IV. Results

We present six sets of findings: 1) demographic correlates of annuitization, 2) obstacles to and motivations for annuitization, 3) the effect of offering partial annuitization, 4) the desired intertemporal slope of retirement income and the demand for COLAs, 5) framing effects, and 6) the demand for “bonuses” (uneven intra-year payments).

A. Demographic correlates of annuitization

Table 3 shows the results of regressing the fraction of balances annuitized in each of the five annuity versus lump sum decisions in our surveys on age, number of children, and dummies for being male, a college graduate, married, retired, and a homeowner. In Survey 1, the three decisions involved tradeoffs between the lump sum and the Steady Income, Match-Inflation, or High-Growth annuity. In Survey 2, the two decisions involved tradeoffs between the flat nominal

annuity and the lump sum before seeing the mortality graph and after seeing the mortality graph. We pool all of the treatment arms in each Survey 2 regression.

We find that collectively, the demographic variables explain very little of the variation in annuitization choices (the R^2 s are all very low); in addition, very few of the demographic variables are significantly correlated with annuity demand. In Survey 1, being a homeowner is associated with a 5.8 percentage point lower fraction of balances invested in the Steady Income annuity. In Survey 2, being married is associated with a 3.9 percentage point higher fraction of balances invested in the flat nominal annuity before seeing the mortality graph. After seeing the mortality graph, being retired is associated with a 3.0 percentage point higher fraction of balances annuitized, and each child is associated with a 0.7 percentage point lower fraction of balances annuitized. In untabulated results, we additionally control for net worth, which reduces our sample sizes because of non-response. Net worth is negatively correlated with the fraction invested in the Steady Income annuity in Survey 1. This additional control also causes the homeowner dummy to lose significance in the Steady Income regression and the number of children variable to lose significance in the Survey 2 regression of annuitization percentage after seeing the mortality chart.

It is difficult to compare these results to others in the literature on the demographic correlates of annuitization because the hypothetical situations in which our respondents made their decisions differ from the real or hypothetical situations in which individuals in other studies made their annuitization decisions. In addition, other studies control for a different set of covariates than we do, so the coefficient on a given variable has a different interpretation in our analysis than in others. Brown (2001) finds that among older U.S. adults in the Health and Retirement Survey, self-reported intentions to annuitize DC plan assets in the future are higher for single individuals and those with less wealth, but do not vary with current age, gender, education, and the presence of children when a model-estimated value of annuitizing is controlled for. Mottola and Utkus (2007) examine actual annuitization choices at two large U.S. firms and report that lower wealth, female gender, and being unmarried are associated with more annuitization.¹⁵

¹⁵ For evidence on demographic correlates of annuity demand outside the U.S., see Bütler and Teppa (2007) and Inkmann, Lopes, and Michaelides (2011).

B. Obstacles to and motivations for annuitization

In Figure 6, we present the average importance individuals reported placing on various factors when making their lump sum versus annuitization choices. Ratings are similar across the two surveys on factors whose importance rating was elicited on both surveys. The factor with the highest average importance is the desire to “make sure I have enough income later in life,” with an average rating of 3.9 to 4.0 out of 5. The next highest category is “flexibility in the timing of my spending,” with an average rating of 3.5 in both surveys, closely followed by “worried about company not being able to pay me,” with an average rating of 3.4 in both surveys. The desire for flexibility manifests itself in the 3.2 rating placed on “I might have a big spending need sometime during retirement” (asked only on Survey 2). The low rating of 1.6 on “I have a big spending need right after retirement” (asked only on Survey 1) suggests that respondents do not have a specific spending need in mind.

Worries about inflation (average rating of 3.0 to 3.3), the desire to invest the money on one’s own (average rating of 3.0 to 3.1), and the desire to prevent overspending (average rating of 2.7 to 3.0) are intermediate-level concerns. In contrast, two other motives that are commonly discussed in the annuities literature are reported to have little absolute importance by our survey participants. The desire to give money to children or others garners an average rating of 2.1 to 2.4, and worries about dying early receive an average rating of 2.3. The factor rated least important is the desire to keep money away from children or others, which has an average rating of 1.4. In Survey 1, the annuity offered did not have a survivor benefit, and the fact that lifetime payments would not provide for one’s spouse after one’s death has a 3.5 importance rating among married participants in this survey.

How do these factor ratings correlate with annuitization choices? Table 4 shows results from regressing the percent of balances subjects choose to annuitize in Survey 2 before seeing the mortality chart on the subjects’ factor ratings, pooling together all the treatment arms.¹⁶ All of the factor ratings except “want to keep money from children or others” (which had the lowest absolute importance rating in Survey 2) and “I might have a big spending need sometime during

¹⁶ The regression results from using Survey 1 annuity choices are broadly similar. Additionally controlling for Survey 2 treatment dummies and demographic characteristics does not qualitatively alter the coefficients on the factor importance ratings.

retirement” are significantly correlated with the fraction of balances annuitized. Annuitization is increasing in the importance placed on having enough income later in life, worries about inflation, and the desire to prevent overspending, while it is decreasing in the importance placed on flexibility in the timing of spending, worries about counterparty risk, the desire to invest money on one’s own, the desire to give money to one’s children or others, and worries about dying early. The insignificance of “I might have a big spending need sometime during retirement” is initially puzzling given that factor’s high absolute importance rating, but the factor’s coefficient becomes negative and significant if the “Want flexibility in the timing of my spending” rating is excluded from the regression, indicating that the former rating captures a strict subset of the motives measured by the latter rating.

From the perspective of product design, it is not obvious whether the levels (Figure 6) or the sensitivities (Table 4) are the most relevant statistics. In Appendix 2, we sketch a model that analyzes this issue (without resolving it one way or the other).

C. Partial annuitization

Mark Iwry, senior adviser to the Secretary of the Treasury and deputy assistant secretary for retirement and health policy, has stated that the U.S. Treasury Department would like to see DB plans move away from offering an “all-or-nothing” choice between an annuity and a lump sum to offering a variety of choices combining annuity and lump-sum payouts (Steverman, 2012). To assess the effect of such a change, we compare annuitization choices under two treatments in Survey 2: i) the All or Nothing treatment, in which the only options were 0% Annuitization and 100% annuitization, and ii) the Minimal Framing baseline which contained five annuitization options (from 0% to 100% in increments of 25%).

Figure 7 shows the distribution of annuitization percentages chosen under each condition prior to seeing the mortality chart. We find that a majority of individuals (59%) choose partial annuitization when given the opportunity to do so. These partial annuitants represent shifts from both the full annuitization and full lump-sum outcomes under the All or Nothing treatment. The fraction of individuals who fully annuitize falls from 50% to 21%, and the fraction of individuals who choose a full lump sum similarly falls from 50% to 20%. Correspondingly, allowing for partial annuitization increases the fraction of people choosing a positive amount of annuitization from 50% to 80%. Finally, allowing partial annuitization raises the average percent of pension

wealth annuitized from 50% to 57%. These last two differences are significant at the 1% level and do not qualitatively change if we additionally control for age, gender, having a college degree, marital status, retirement status, number of children, and home ownership (regression results in Online Appendix Table A2). Our findings suggest that expanding the use of partial annuitization in DB settings where total cash-outs are already allowed might lead to higher annuitization rates.¹⁷

D. Slopes of annuity payments and COLAs

Our surveys measured subjects' preferences with respect to the slope of the annuity payout stream. Recall that Survey 1 respondents made binary choices between payments of identical present value that decline 2% per year, stay flat, or increase 2% per year in real terms. Figure 8 shows that among respondents with single-peaked preferences over payout streams,¹⁸ 19% preferred the declining real annuity (-2% per year), 32% preferred the flat real annuity, and 50% preferred the rising real annuity (+2% per year).¹⁹ In other words, our respondents overwhelmingly preferred flat or rising real retirement payment paths rather than falling real paths, holding the present value of the payments fixed.²⁰

By comparison, Hurd and Rohwedder (2011) find that, holding household composition fixed, real consumption *declines* by about 2% per year during retirement. How can we reconcile our survey respondents' reported preference for rising payments with the declining actual consumption streams of retired households? Several complementary explanations are plausible.

¹⁷ Using data on annuitization choices in Swiss defined-benefit plans, Büttler and Teppa (2007) find that most people choose 0% or 100% annuitization even when partial annuitization is an option. This could be due to workers being unaware of the partial annuitization option and/or communications materials focusing on all or nothing (rather than partial) annuitization options.

¹⁸ By this, we mean excluding the 11% who both chose real payments that decline 2% per year over flat real payments and real payments that increase 2% per year over flat real payments.

¹⁹ When we regress a dummy for choosing a declining real annuity on Survey 1 participants' ratings of the importance of various factors in their lump sum versus annuitization choice, we find that a one standard deviation increase in worry about the company not being able to pay in the future is associated with a 3.4% higher likelihood of choosing the declining annuity, a one standard deviation increase in worry about inflation is associated with a 5.6% lower likelihood of choosing the declining annuity, and a one standard deviation increase in concern that the lifetime payments would not provide for one's spouse is associated with a 3.1% lower likelihood of choosing the declining annuity. The other measured motives have no significant correlation with choosing the declining annuity.

²⁰ However, the percent of balances annuitized rather than cashed out is not very responsive to the annuity's payout slope, averaging 61.4%, 60.4%, and 62.5% for the decreasing, flat, and increasing annuities, respectively. Only the difference between the flat and increasing annuities is significant at the 5% level.

First, annuities enable agents to shift resources from death states to survival states. This has the effect of lowering the implied rate of return in death states (when the value of the annuity is lost) and raising the implied rate of return in survival states (since the annuitant receives the normal market rate of return plus an implicit survivorship bonus, a transfer from the decedents in the annuity pool). Because of this state-dependent rate of return, an agent with access to an annuity should choose a higher rate of consumption growth relative to an agent without access to an annuity. The Appendix contains a formal (Euler equation) derivation of this familiar result. If individuals in the real world do not have access to fairly priced annuities while those in the survey do, this could potentially reconcile the different patterns.

Second, households may have biased expectations. For example, households may underestimate the frequency of transitory spending needs, such as home repairs, out-of-pocket healthcare expenses, etc. This will cause them to spend more than the annuity value of their wealth, resulting in a realized consumption path that declines over time due to the budget constraint despite their preference for a rising path. Households may be overly optimistic about their asset returns, which would also cause their realized consumption path to decline faster than they expected. Households may not anticipate the extent to which consumption and health status are complements (Finkelstein, Luttmer, and Notowidigdo, 2012), causing them to believe they will want to spend more in advanced old age than they actually do.

Third, Survey 1 respondents may believe their life expectancy to be longer than the life expectancy that equates the present value of the various payment streams. Such a belief would lead them to expect to collect a greater present value of payments from the rising annuity than from the other two annuities. The greater perceived present value of the rising annuity could then cause respondents to choose it despite otherwise preferring a downward-sloping consumption path.

Fourth, households may have money illusion and set their early retirement spending at a level that allows them to sustain a flat nominal spending trajectory, not fully appreciating that a flat nominal path is a real path that falls at the rate of inflation. We leave a fuller discussion of money illusion in the annuity market to future work.

In practice, annuity and pension payouts change over time through cost of living adjustments (COLAs). Note that a typical COLA has two features: it changes the expected slope of payouts, and it provides a hedge against surprise inflation. While in principle these two

features could be separated, they are in fact almost always bundled together. The prevalence of inflation-adjusted payouts differs dramatically across institutions. Contractual COLAs of some sort are almost universal in state and local government DB pension plans (Novy-Marx and Rauh, 2011). In private DB plans, contractual COLAs are relatively rare; these plans tend to instead have either ad-hoc adjustments (occasional and less than the inflation rate) or no adjustments (Allen, Clark, and Sumner, 1984, 1986a, 1986b). The vast majority of single-premium immediate annuities (SPIAs) purchased are not indexed to inflation.

In Survey 2, we asked respondents whether they wanted to add a COLA to their annuity. Doing so led to an initial monthly payment that was 32% lower than the no-COLA monthly payment. When this question was asked in the Minimal Inflation Information condition, 44% of participants chose the COLA. Adding a short description of inflation and explaining how much 2% annual inflation erodes purchasing power over two decades in the Inflation Compounding treatment raised the demand for a COLA from 44% to 67% (see Figure 9), a 23 percentage point increase that is significant at the 1% level.²¹ This result suggests that an insufficient awareness of inflation's effects might depress the demand for COLAs in pension and annuity settings, and that enhancing the information about inflation's impact that is provided to retirees could substantially raise COLA take-up rates.

E. Framing

How do alternative frames influence annuitization choices? Figure 10 shows the distribution of annuitization choices made by respondents in the main framing treatments of Survey 2. We examine the impact of these framing treatments on two outcomes: whether respondents chose to annuitize any balances before seeing the mortality graph, and the fraction of balances annuitized. The key explanatory variables in the regressions are six framing

²¹ We also administered the Inflation Compounding With Graph treatment, which included a graph showing nominal annuity payments by age. We find that 62% of participants chose the COLA, a fraction that is significantly higher (at the 1% level) than the COLA take-up rate in the Minimal Inflation Information condition but significantly lower (at the 1% level) than the COLA take-up rate in the Inflation Compounding treatment (without a graph). It is possible that the nominal payments graph was a visual distraction that made participants less attentive to the text explaining inflation, but there are several alternative potential interpretations.

treatment dummies (the Minimal Framing treatment is the excluded category); the regressions also include a set of demographic controls.²²

The first column of Table 5 reports the results from a linear probability regression where the dependent variable is a dummy for the respondent annuitizing a positive amount. The only framing treatment effect that is significant at conventional levels is that of the Flexibility and Control treatment, which told participants, “Choosing a bigger lump sum gives you more control over your investments and more flexibility over the timing of your spending.” This treatment decreased the probability of annuitizing any balances by 7.8 percentage points relative to the Minimal Framing baseline (significant at the 1% level). The Investment Framing treatment—which told participants that the annuity’s return would be high if they died old and low if they died young, whereas the lump sum would give them the same return regardless of longevity—reduced the probability of any annuitization by 4.8 percentage points, an effect that is marginally significant at the 10% level.

The second column of Table 5 reports results from a regression whose dependent variable is the fraction of balances annuitized. Both the Flexibility and Control and Investment Framing treatments decreased the level of annuitization relative to the Minimal Framing baseline at the 1% significance level; those in the Flexibility and Control treatment have an 8.7 percentage point lower level of annuitization, while those in the Investment Framing treatment have a 6.0 percentage point lower level of annuitization.

Brown et al. (2008) find that an investment frame discourages annuitization relative to a consumption frame, but Brown, Kapteyn, and Mitchell (2012) do not find an investment framing effect in the context of Social Security claiming age. Our results fall in the middle, finding a negative effect of investment framing that is significant but smaller in magnitude than the results of Brown et al. (2008).

The remaining four framing treatments shown in Table 5 have coefficients that are generally of the anticipated positive sign (all of them in the first regression and all but one in the second regression), but these coefficients are closer to zero and not statistically significant. These null effects cast some doubt on the hypotheses that motivated these treatments: that annuity demand is suppressed by the fear of foregoing a better deal elsewhere, by the large contrast

²² The All or Nothing treatment recipients are excluded from the regression sample.

between the magnitude of the lump sum and the magnitude of the monthly annuity payment, by the failure to recognize the longevity insurance embedded in an annuity, or by the failure to recognize the attractive state-contingent payment properties of an annuity.

As a final framing experiment, we asked Survey 2 participants to make their annuitization choice again after seeing a graph of the probabilities of surviving to different ages, conditional on living to age 65. Figure 11 shows the average annuitization rates for participants before and after seeing this mortality chart. The average annuitization rate in every experimental condition is lower after seeing the mortality graph; the percent of balances annuitized across all conditions drops from 55.4% to 52.2%, a difference that is significant at the 1% level. The systematic drop could indicate that our respondents were on average over-optimistic about their expected relative longevity, and the mortality chart mitigated some of this bias, reducing annuity demand.²³

F. Annuities with “bonuses”

Survey participants cited the desire for “flexibility in the timing of my spending” as one of the most important factors in their annuitization decision. Our ex ante expectation that this consideration would be important motivated exploring the demand for an annuity that offered a higher “bonus” payment in one month of each year, funded by lower payments in the remaining months. We find that 60% of Survey 1 respondents preferred a Match-Inflation Income with Bonuses annuity over a Match-Inflation Income annuity without a bonus. Among those choosing the bonus, 58% wanted the bonus to be paid during the winter holiday season—November, December, and January (see Figure 12). However, our explanation of the bonus used “the December holiday season” as an example of when a bonus might be received, so some of the concentration in these months could be due to the explanation itself. Another caveat to keep in mind is that we did not measure the willingness to pay for this bonus feature, so we do not know the strength of the preference for bonuses.

The Match-Inflation Income with Travel Bonuses annuity proved to be less popular, although it still appealed to a significant fraction of the population. Forty-five percent of

²³ There is a vast empirical literature on how subjective survival expectations relate to objective survival expectations. See, for example, Hamermesh (1985), Hurd and McGarry (1995), Hurd, McFadden, and Merrill (2001), Smith, Taylor, and Sloan (2001), Smith et al. (2001), Hurd and McGarry (2002), Gan, Hurd, and McFadden (2005), and Ludwig and Zimper (2012).

respondents preferred the Match-Inflation Income with Travel Bonuses annuity over the Match-Inflation annuity without bonuses. The lesser appeal of the travel bonuses may be due to the fact that they are paid in June; the fact that their size declines with each decade of life, creating an overall declining real path for yearly annuity payments; and/or the fact that they make salient respondents' physical decline in old age. Our previously discussed results showed that people usually prefer their bonuses to be paid in November, December, or January and that people dislike downward-sloping real payment paths.

V. Conclusion

In this paper, we analyzed two large surveys of hypothetical annuitization choices to learn what motives are important in annuitization choices and whether annuity product design and framing of the annuity choice can significantly affect annuity demand. Although hypothetical choices must be interpreted with caution, since they may not closely correspond to the choices people would actually make, they allow us to measure preferences for products not currently available in the market and examine choices in economic environments that differ from the current one. Surveys like ours provide a starting point for designing field experiments that involve actual consequential choices.

Our results have several implications for annuity product design and choice architecture. To increase annuity demand, annuity providers could design products that give beneficiaries more flexibility and control. Our bonus annuity is an example of personalization that increases flexibility and control without compromising longevity insurance. Another example is an annuity with multiple annual bonuses. Such bonuses could either be pre-selected at the time the annuity was purchased or selected at the beginning of each calendar year. In fact, the payout stream for a given year could be made completely flexible without creating a substantial adverse selection problem. Problematic adverse selection would only arise if inter-year reallocations were allowed, so that a beneficiary could drain his entire annuity following a significant adverse health event.

Other forms of personalization and flexibility could also be adopted, such as limited penalty-free early withdrawals and even asset allocation flexibility (adopting some features of the variable annuity market). Of course, there is a tradeoff between greater flexibility/control and greater complexity. Too much flexibility may drive some consumers away from annuities (cf.

Iyengar and Kamenica, 2010). Finding the optimal mix of flexibility and simplification is a significant challenge.

We also find that most consumers prefer partial annuitization of their retirement nest egg over either 0% or 100% annuitization. We find that the availability of partial annuitization raises the average fraction of wealth that ends up annuitized.

Framing changes may also increase the appeal of annuities, especially frames that make the option of partial annuitization salient. In addition, frames that downplay investment attributes of annuities may increase annuitization rates. Regarding choices about COLAs, discussing the implications of inflation for purchasing power over long horizons increases demand for rising nominal payment paths.

Finally, participants report that fears of counterparty risk play a large role in their annuitization choices. By adopting regulations that reduce this fear, policy makers may create moral hazard problems from consumers disregarding the financial stability of annuity providers, but they may also increase overall demand for annuities.

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Appendix 1: Optimal Consumption Path With and Without Annuitization Contracts

In this appendix, we study the rise in the slope of the optimal consumption path when an actuarially fair annuity is introduced.

We consider a two period problem of an agent with constant relative risk aversion $\gamma \in (0, \infty)$, pure (conditional on survival) discount factor $\delta = \exp(-\rho)$, and survival rate $s = \exp(-\mu)$. Thus, the discount rate is ρ and the mortality rate is μ . For simplicity, we assume that all variables are real. The objective of the agent is given by

$$u(c_1) + s\delta u(c_2) + (1-s) \times 0 = u(c_1) + s\delta u(c_2).$$

Note that there are two sources of discounting in this model: pure time discounting and mortality discounting.

If the gross interest rate is $R = \exp(r)$ and the agent does *not* have access to an annuity contract, then the first order condition (Euler equation) is

$$\begin{aligned} u'(c_1) &= s\delta R u'(c_2) \\ c_1^{-\gamma} &= s\delta R c_2^{-\gamma} \end{aligned}$$

Taking logs yields,

$$\ln(c_2) - \ln(c_1) = \frac{1}{\gamma}(r - \rho - \mu).$$

In other words, the growth rate of the optimal consumption path is $\frac{1}{\gamma}(r - \rho - \mu)$.

Now assume that the agent *does* have access to a fair annuity contract. To buy R dollars of consumption in the survival state costs s dollars in period 1. In other words, the price of the annuity is s . The Euler equation is now

$$\begin{aligned} su'(c_1) &= s\delta R u'(c_2) \\ c_1^{-\gamma} &= \delta R c_2^{-\gamma}. \end{aligned}$$

Now, the growth rate of the optimal consumption path is $\frac{1}{\gamma}(r - \rho)$.

Hence, the introduction of the annuity *raises* the growth rate of the optimal consumption path by μ / γ . Intuitively, this effect arises because the annuity raises the effective rate of return for claims on consumption in the survival state from R to R/s (a substitution effect).

Appendix 2: A model of annuity demand.

Consider an annuity that is defined by a set of attributes, indexed by $k = 1, \dots, K$. Assume that annuity demand by consumer i depends on (i) the price of the annuity, P , (ii) the marginal value of each attribute to consumer i , α_i^k , and (iii) the intensity of that attribute in the annuity product, A^k .²⁴

$$Q_i = \sum_k \alpha_i^k A^k - \gamma P \quad (1)$$

The price of the annuity, P , and the vector of attributes, $\{A^k\}_{k=1, \dots, K}$, are the choice variables of the firm. Suppose the cost to the firm of including attribute k with intensity A^k is a quadratic function:

$$C^k = \frac{1}{2} \theta^k (A^k)^2. \quad (1)$$

Now consider a monopolist firm that is designing a wide range of products that appeal to each type of consumer. The firm chooses P and $\{A^k\}_{k=1, \dots, K}$ to maximize:

$$Q_i \left(P - \sum_k C^k \right) = \left(\sum_k \alpha_i^k A^k - \gamma P \right) \cdot \left(P - \sum_k \frac{1}{2} \theta^k (A^k)^2 \right) \quad (2)$$

Differentiating (3) with respect to P and $\{A^k\}_{k=1, \dots, K}$ yields a set of first order conditions. Combining and simplifying these yields a set of optimal intensities,

$$A^{k*} = \frac{\alpha_i^k}{\gamma \theta^k}. \quad (3)$$

Equation (4) tells us that the firm should choose a higher value of A^k for attributes that have high marginal value to consumers—i.e., attributes that have a high α_i^k —and lower values of A^k for attributes that are more expensive to create—i.e., those with high θ^k .

Finally, we need to map this analysis back to our survey. There are two polar cases that we study for illustrative purposes: (i) respondents have little cross-sectional variation in the perceived magnitudes of A^k , substantial cross-sectional variation in the taste parameter α_i^k , and their survey responses are proxies for α_i^k , and (ii) respondents have substantial cross-sectional variation in the perceived magnitudes of A^k , little cross-sectional variation in the taste parameter α_i^k , and their survey responses are proxies for their perceived value of A^k . Under case (i), product design should focus on the attributes with the highest average values reported in Figure 6. Under case (ii), product design should focus on the attributes with the highest regression coefficients reported in Table 4.

²⁴ There could be variation across people in the *perceived* intensity of the attribute, in which case we would need to index A^k by i . This case is considered at the end of the appendix.

Table 1. Survey clarity assessment by survey participants

Assessment of clarity	Survey 1	Survey 2
Clear	53.0%	64.3%
Mostly clear	33.8%	28.2%
Sometimes clear	4.7%	3.2%
Sometimes confusing	7.8%	3.2%
Mostly confusing	0.1%	0.4%
Completely confusing	0.3%	0.2%
Decline to answer	0.3%	0.4%
Total	100%	100%

Source: Authors' calculations

Table 2. Participant characteristics

	Survey 1	Survey 2
Age (mean)	59.5	59.6
Male	50.2%	49.6%
Married	55.4%	54.5%
Number of children (mean)	2.1	2.0
Retired	35.6%	40.3%
Have a DB pension	39.3%	37.6%
Own home	71.3%	69.5%
Net worth (among respondents)		
Median	\$162,500	\$150,000
Mean	\$298,217	\$286,594
Highest education attained		
No high school diploma	1.9%	1.7%
High school diploma	22.9%	23.8%
Some college	35.0%	35.8%
College degree	27.1%	26.6%
Graduate degree	12.8%	11.8%
Decline to answer	0.3%	0.3%
Life expectancy		
Longer than the average person my age	36.4%	33.9%
About the same as the average person my age	54.1%	54.3%
Shorter than the average person my age	9.5%	11.8%

Source: Authors' calculations

Table 3. Demographic correlates of percent of balances annuitized

	Survey 1			Survey 2	
	Steady Income	Match-Inflation	High-Growth	Before mortality chart	After mortality chart
Age (years)	0.001 (0.002)	0.001 (0.002)	0.002 (0.002)	0.000 (0.001)	0.001 (0.001)
Male	-0.031 (0.024)	-0.018 (0.025)	-0.045 (0.025)	-0.020 (0.012)	-0.007 (0.012)
College Degree	0.003 (0.025)	0.033 (0.026)	0.009 (0.026)	0.007 (0.012)	0.012 (0.012)
Married	0.027 (0.027)	0.011 (0.027)	0.039 (0.027)	0.039** (0.013)	0.023 (0.013)
Retired	0.039 (0.030)	0.043 (0.030)	0.020 (0.031)	0.023 (0.014)	0.030* (0.014)
# children	0.005 (0.007)	0.005 (0.008)	-0.004 (0.008)	-0.005 (0.003)	-0.007* (0.003)
Homeowner	-0.058* (0.029)	-0.042 (0.030)	-0.038 (0.030)	0.009 (0.014)	0.017 (0.014)
Constant	0.580** (0.127)	0.509** (0.130)	0.511** (0.131)	0.524** (0.061)	0.443** (0.060)
N	974	974	974	4,052	4,052
R ²	0.009	0.008	0.008	0.005	0.005

Source: Authors' calculations. Each column reports the coefficient estimates from a regression of the percent of balances annuitized on the demographic variables listed in the rows. The dependent variable takes values between 0 and 1. Standard errors are in parentheses. * Significant at the 5% level. ** Significant at the 1% level.

Table 4. Association between annuitization percentage before seeing mortality graph and factor importance ratings in Survey 2

Income later in life	0.05 ^{**} (0.01)
Flexibility in spending timing	-0.04 ^{**} (0.01)
Company might not pay me	-0.06 ^{**} (0.01)
Spending need sometime during retirement	-0.00 (0.01)
Worried about inflation	0.01 [*] (0.01)
Want to invest money on my own	-0.11 ^{**} (0.01)
Prevent overspending	0.06 ^{**} (0.01)
Give money to children or others	-0.01 [*] (0.01)
Worried about dying early	-0.04 ^{**} (0.01)
Keep money from children or others	0.00 (0.01)
Constant	0.55 ^{**} (0.01)
N	4,130
R ²	0.262

Source: Authors' calculations. This table reports the coefficient estimates from a regression of the percent of balances annuitized on respondents' factor importance ratings for their lump sum versus annuity choices. The dependent variable takes values between 0 and 1. Each factor importance rating is standardized to have mean zero and variance one. Standard errors are in parentheses. * Significant at the 5% level. ** Significant at the 1% level.

**Table 5. Effect of framing on annuity choices
before seeing mortality graph in Survey 2**

	Annuity outcome	
	Any balances annuitized (0/1)	Percent of balances annuitized
Framing treatments		
Minimal framing treatment (omitted)	--	--
Good Deal treatment dummy	0.020 (0.025)	-0.002 (0.022)
Total Payments treatment dummy	0.017 (0.025)	0.019 (0.022)
Investment Framing treatment dummy	-0.048 (0.026)	-0.060** (0.022)
Flexibility and Control treatment dummy	-0.078** (0.026)	-0.087** (0.022)
Longevity Insurance treatment dummy	0.004 (0.025)	0.017 (0.022)
Mortality Credits treatment dummy	0.010 (0.026)	0.014 (0.022)
Other controls		
Age	-0.002 (0.001)	0.000 (0.001)
Male dummy	-0.023 (0.014)	-0.019 (0.012)
Has college degree dummy	-0.000 (0.014)	0.003 (0.012)
Married dummy	0.002 (0.015)	0.041** (0.013)
Retired dummy	0.013 (0.017)	0.025 (0.014)
Number of children	-0.001 (0.004)	-0.003 (0.003)
Homeowner dummy	0.010 (0.016)	0.010 (0.014)
Constant	0.899** (0.072)	0.546** (0.062)
N	3,547	3,547
R ²	0.009	0.017

Source: Authors' calculations. This table reports the coefficient estimates from regressions of annuitization outcomes on a set of framing treatment indicator variables and a set of demographic variables. The dependent variable in first column is an indicator variable (0/1) for whether any balances were annuitized. The dependent variable in the second column, the percent of balances annuitized, takes values of 0, 0.25, 0.50, 0.75, or 1.0. The sample excludes participants in the "All or Nothing" treatment. Standard errors are in parentheses. * Significant at the 5% level. ** Significant at the 1% level.

Figure 1. Mortality graph in Survey 1

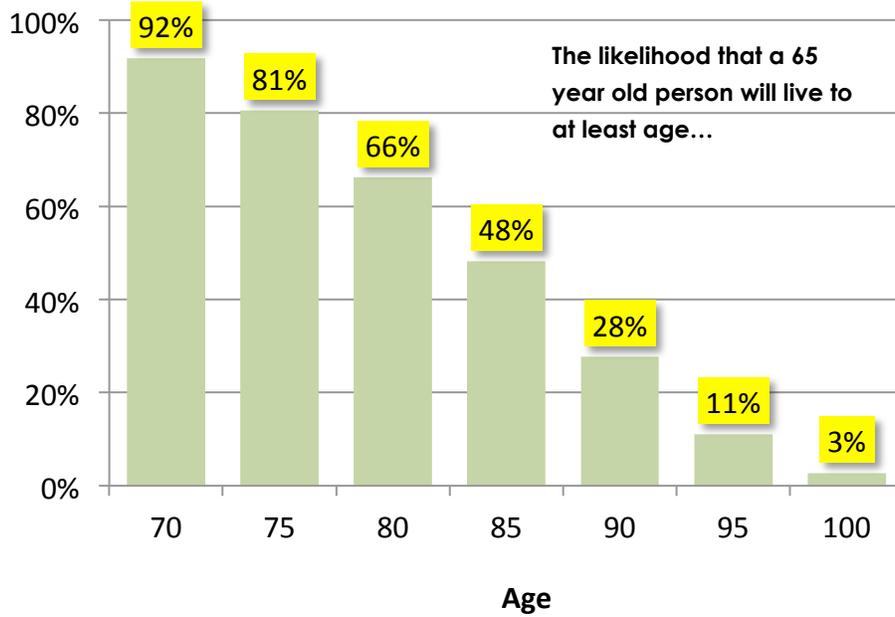


Figure 2. Inflation graph in Survey 1

Here is a graph that shows how much things that cost \$1 today will cost you in the future.

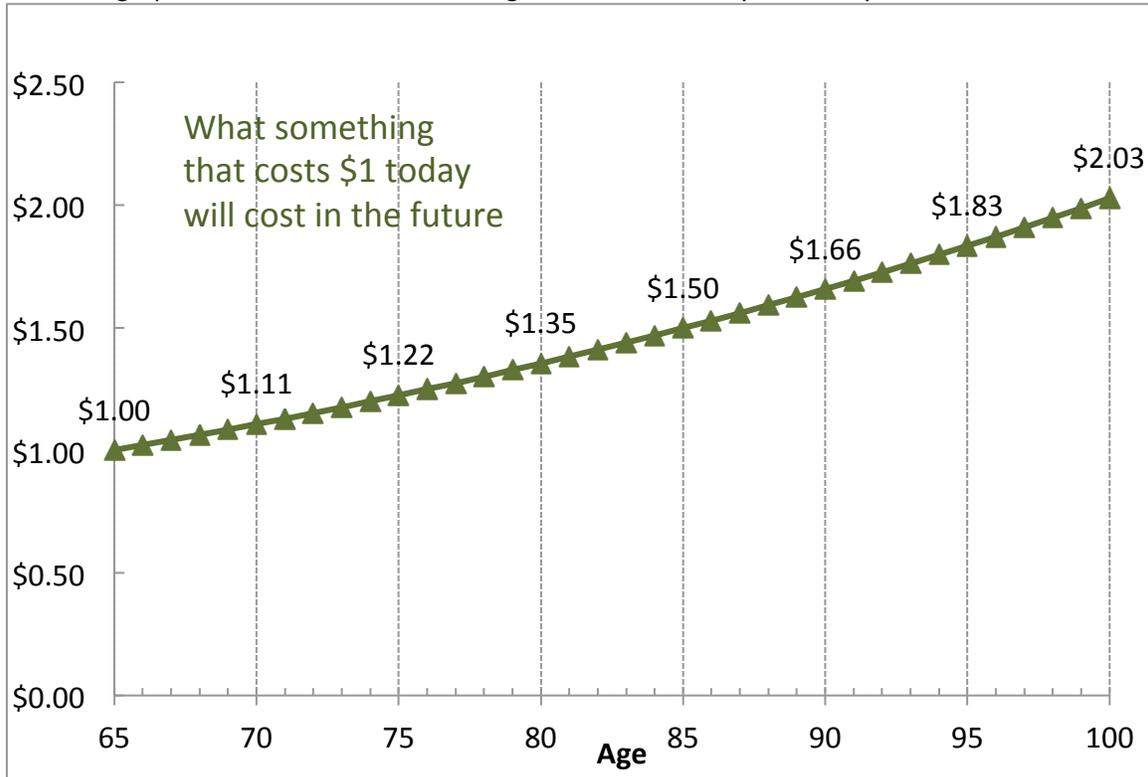


Figure 3. Match Inflation vs. Steady Income nominal payment graph in Survey 1

The graph below shows how much you will receive under each plan at each age if you are still alive.

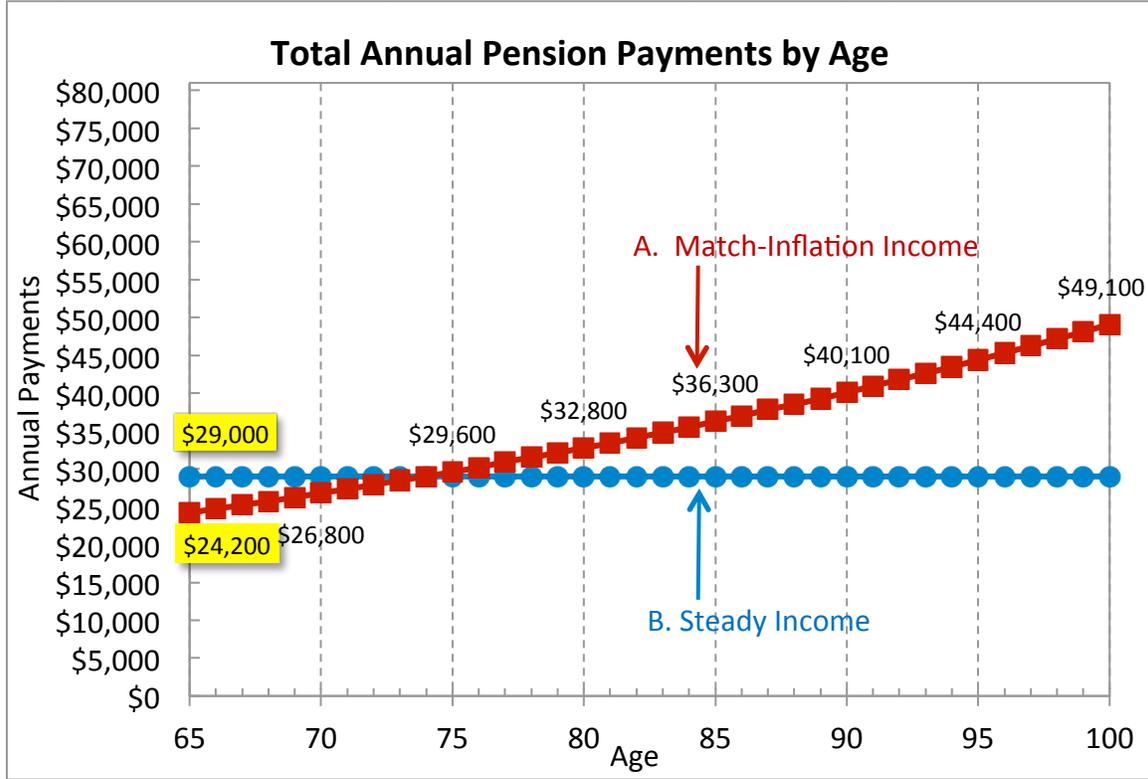


Figure 4. Graph of nominal payments for Match-Inflation cash-out question in Survey 1

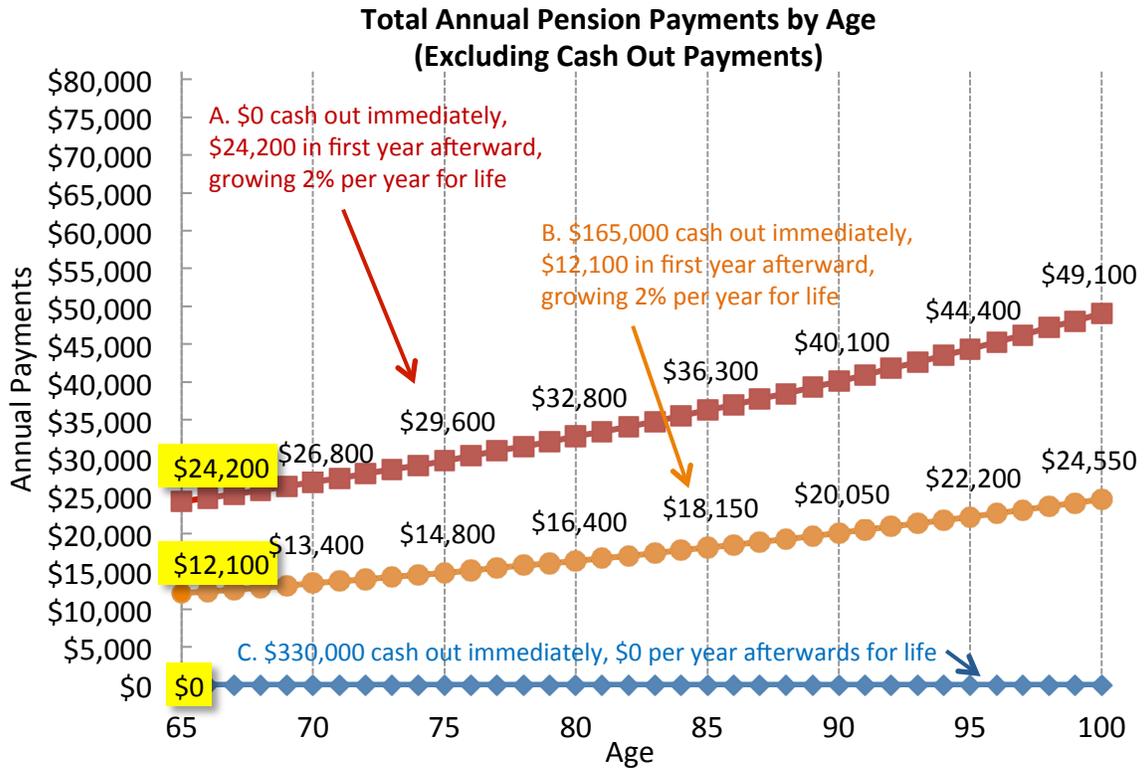


Figure 5. Minimal Framing initial choice screen for unmarried subjects in Survey 2

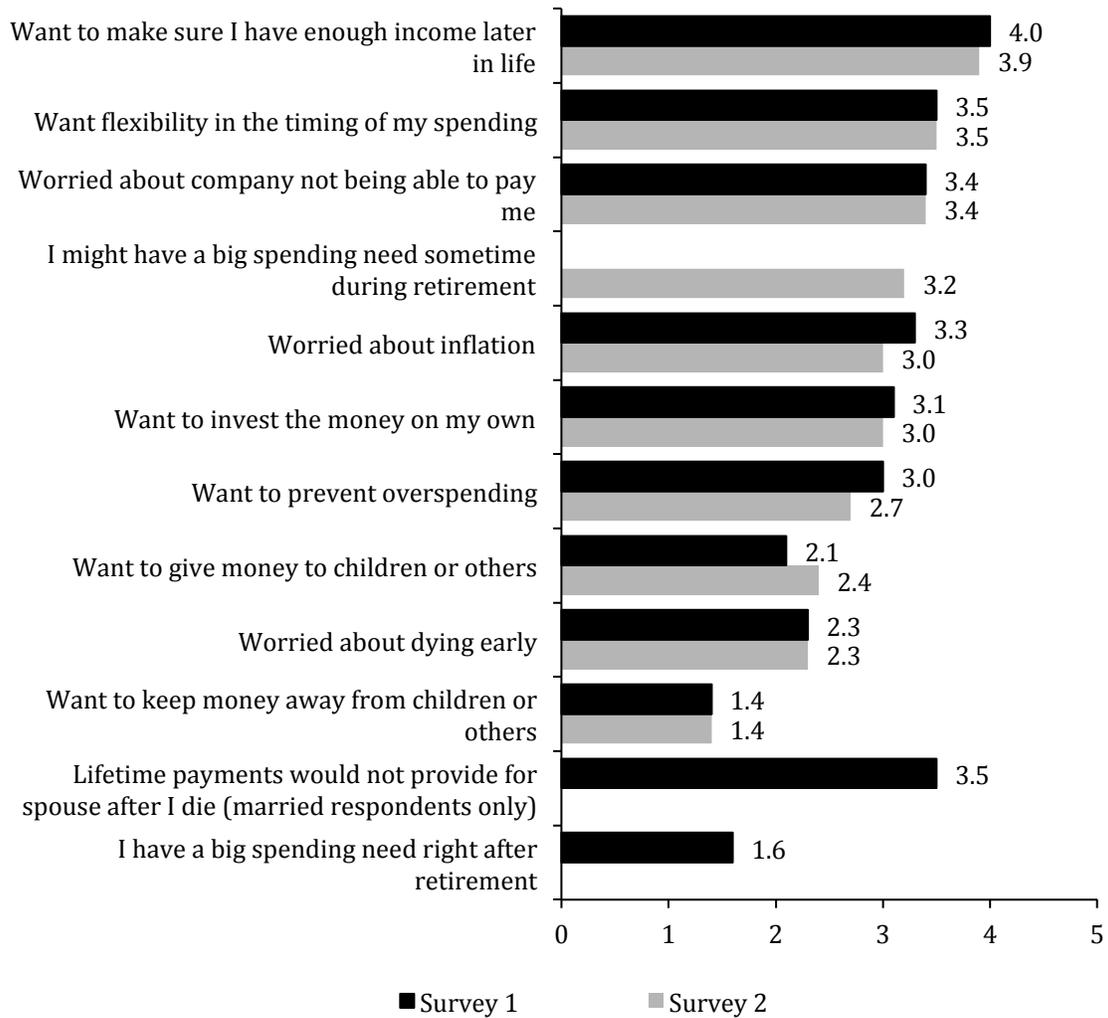
How would you choose to receive your pension payments?

Lower lump sum/
More guaranteed
income

Higher lump sum/
Less guaranteed
income

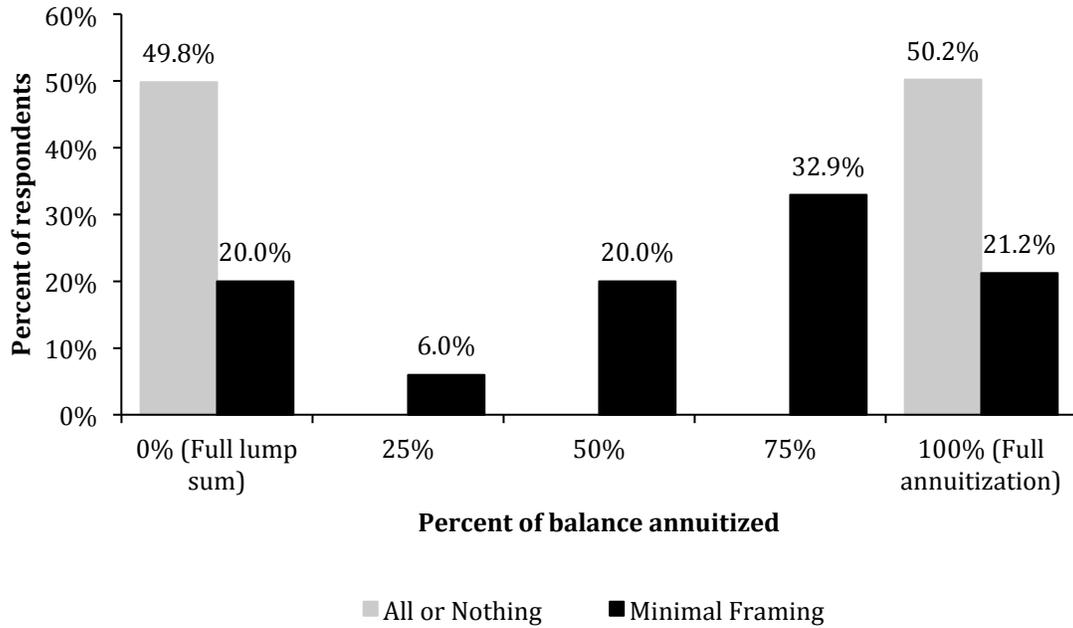
0% lump sum, 100% guaranteed income (\$0 up front, \$2,981 monthly payment)	25% lump sum, 75% guaranteed income (\$125,000 up front, \$2,235.75 monthly payment)	50% lump sum, 50% guaranteed income (\$250,000 up front, \$1,490.50 monthly payment)	75% lump sum, 25% guaranteed income (\$375,000 up front, \$745.25 monthly payment)	100% lump sum, 0% guaranteed income (\$500,000 up front, \$0 monthly payment)
--	--	--	--	--

Figure 6. Average reported importance of motives for lump sum vs. annuity choices



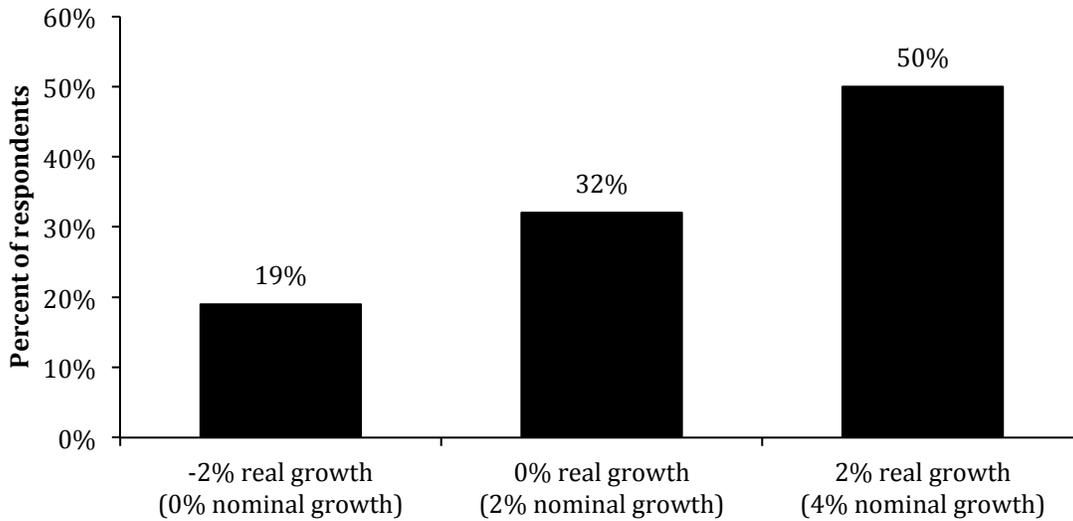
Source: Authors' calculations

Figure 7. Distribution of percent of balance annuitized in Survey 2 before seeing mortality chart under the All or Nothing treatment and Minimal Framing baseline



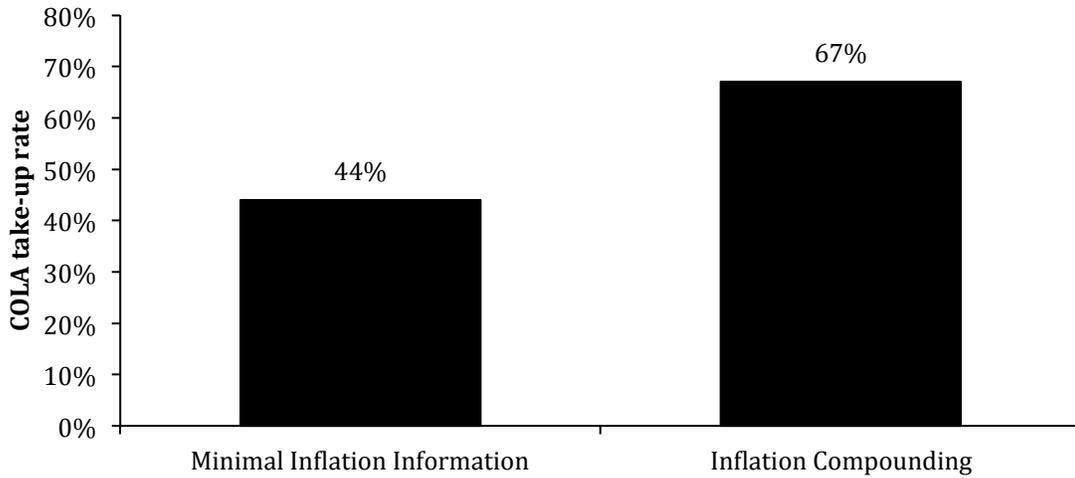
Source: Authors' calculations

Figure 8. What slopes do people prefer for their annuity payouts in Survey 1?



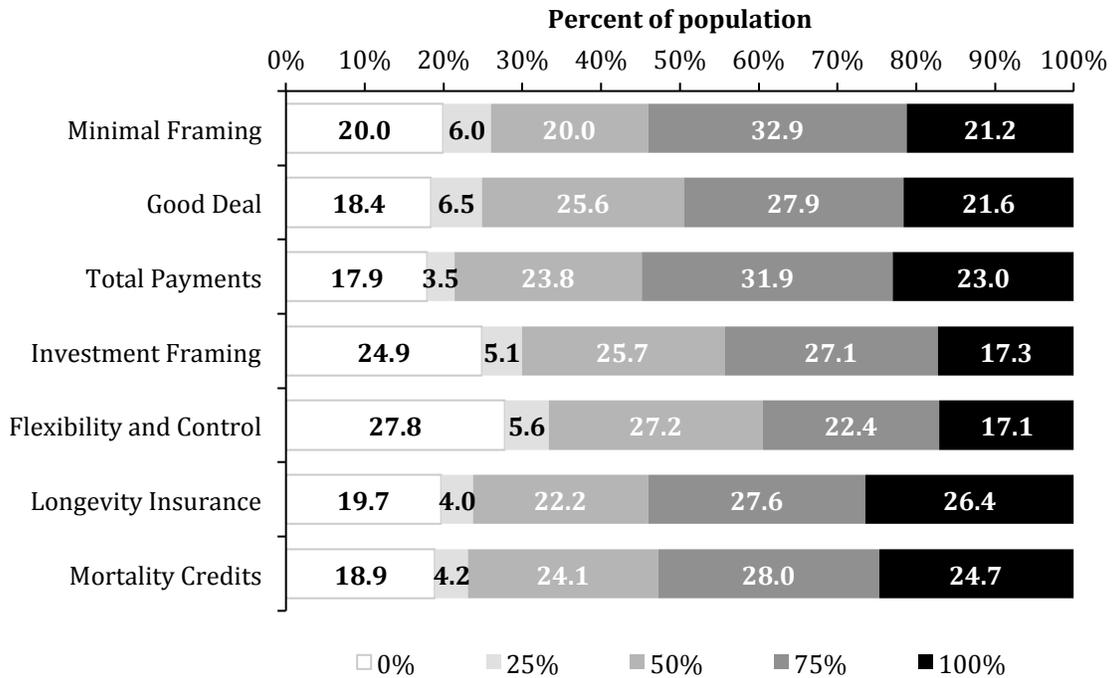
Source: Authors' calculations. This figure reports the percent of respondents in Survey 1 who most prefer the indicated intertemporal slope of annuity payouts. The sample is restricted to respondents with single-peaked preferences over payout slopes.

Figure 9. COLA take-up rates in the Minimal Inflation Information baseline and the Inflation Compounding treatment, Survey 2



Source: Authors' calculations. This figure reports the percent of respondents who chose to add a COLA to their annuity in the Minimal Inflation Information baseline and the Inflation Compounding treatment.

Figure 10. Distribution of percent of balance annuitized before seeing mortality chart in Survey 2 across frames



Source: Authors' calculations

the

SOCIAL SECURITY CLAIMING GUIDE

*A guide
to the MOST
IMPORTANT
financial decision
you'll likely make*





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How old you are when you claim Social Security has a dramatic effect on the monthly benefits you and, if married, your spouse will get for the *rest of your lives*.

Your most important financial decision

The later you claim Social Security, the higher your monthly benefit.

As you approach retirement, how long you work and when you claim will usually have a far greater impact on how much income you'll have in retirement than how much you save or how you invest.



DO YOU NEED A HIGHER RETIREMENT INCOME?

Working longer and retiring later could be the best way to get it.

The power of patience



You can start collecting at any age between 62 and 70.

** If you'd get \$1,000 a month at 62, you'd get at least \$1,333 at 66 and \$1,760 at 70.*

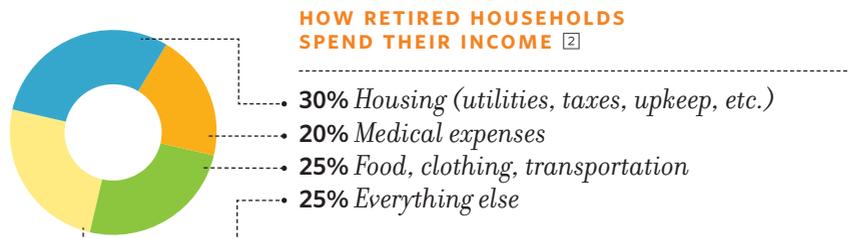
If you start to collect at:	62	66	70
Your monthly benefit is:	your minimum	at least 1/3 more	at least 3/4 more

How much income will you need in retirement?

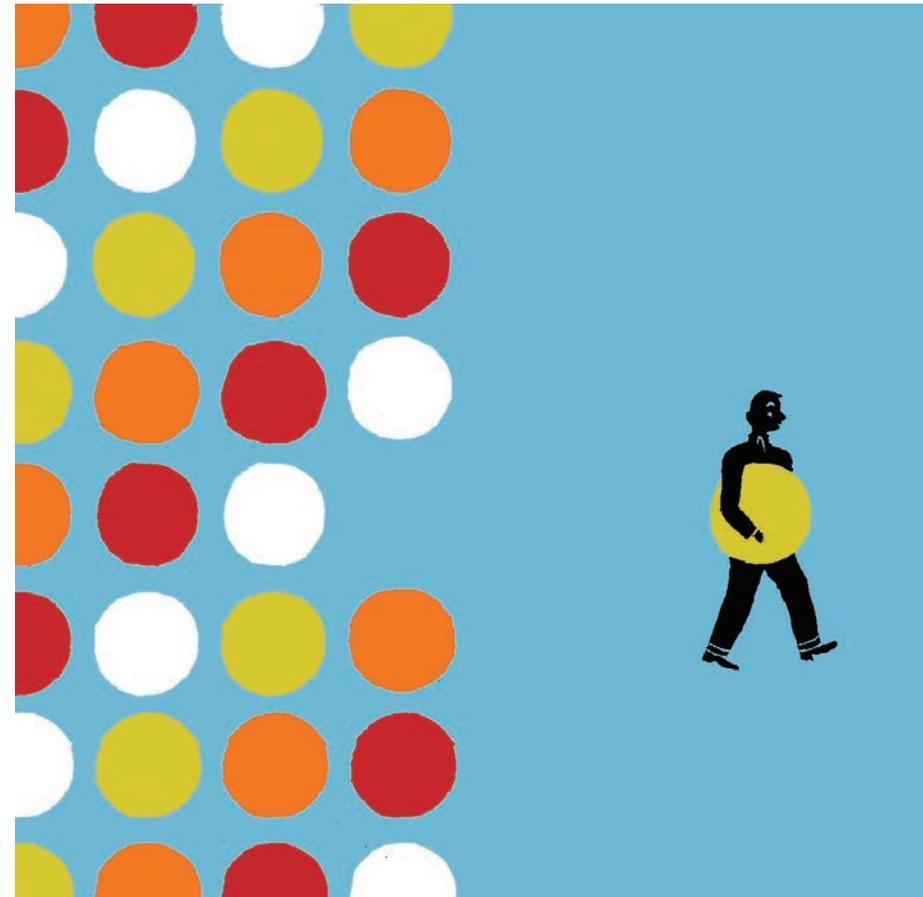
There's no simple answer. But to maintain your standard of living, you won't need as much as you currently earn.

- YOU WILL PAY LESS TAX.
 - You won't pay payroll tax on income from Social Security, savings, or employer pensions.
 - You won't pay income tax on all your Social Security benefits.^[1]
- YOU WON'T NEED TO SAVE FOR RETIREMENT.
- THE MORTGAGE WILL PROBABLY BE PAID OFF (OR WILL BE SOON).
- THE KIDS WILL PROBABLY BE OUT ON THEIR OWN (OR WILL BE SOON).

To maintain your standard of living, experts say you'll need roughly **75%** of your current income.



Some are willing to live on less



If work is difficult, you might want to retire early even if it means having a lower standard of living.

But be careful: You're talking about a lower standard of living for the rest of your life.

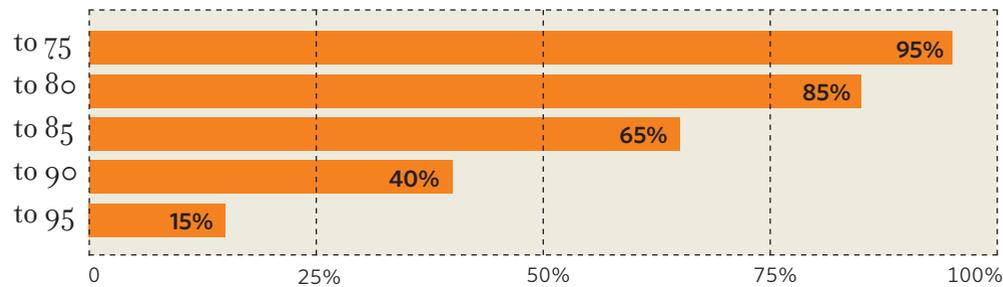
* You also need money in reserve for medical emergencies, unexpected home repairs, and other "rainy day" expenses.

How much really secure income will you need?

Social Security is especially good for providing a basic retirement income that you and your spouse can rely on. The income it provides is inflation-proof and keeps coming as long as you or your spouse is alive.

YOUR CHANCES FOR A VERY LONG LIFE ARE EXCELLENT

Chances that one person in a married couple, both age 62, will live...



INFLATION-PROOF!

You get more dollars from Social Security if prices rise, so what you can buy stays the same.

Income from other sources is less secure



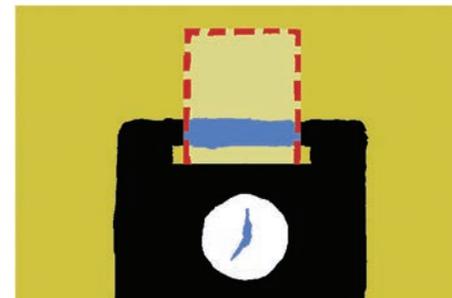
Employer pensions and private annuities provide a guaranteed income for the rest of your life.

But they are rarely inflation-proof. If prices rise 3% a year, in 20 years they'll buy barely half what they do today.



401(k)s, Individual Retirement Accounts (IRAs), and other savings can be invested in stocks that could produce high returns, saved for rainy days, or passed on to your children.

But high returns bring increased risk, and financial shocks are likely over the course of your retirement. On the other hand, cash in the bank is not inflation-proof.



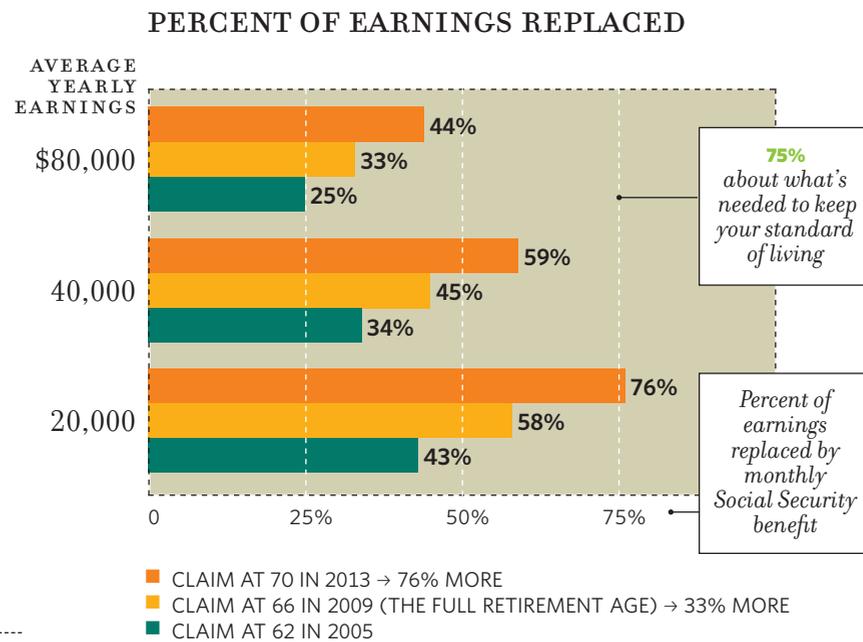
Work is an important source of income for some retirees.

But very few people work past 70. So relying too much on earnings could be a big mistake.

** Social Security will likely be much more important as you age, as other sources of income often dry up.*

The later you claim, the more you get

The monthly benefit you earn as a worker is generally based on when you start to collect and the average of the highest 35 years of earnings on which you've paid Social Security payroll tax.³



LET'S IGNORE INFLATION

Because Social Security benefits rise in line with prices, all examples in this Guide ignore inflation.

As the Full Retirement Age rises to 67, benefits claimed at any age will replace a smaller share of earnings.

You get even more ...

... if working longer raises the average of the highest 35 years of earnings on which you've paid Social Security payroll tax.

For example, say you were 62 in 2005 and had 31 years of employment, at \$40,000 a year.

If you retire and start to collect benefits at 62:

The average of your highest 35 years of earnings is:

\$35,400



Your monthly benefit, based on your average earnings and claiming age =

\$1,030

If you work four more years, at \$40,000 a year, and retire at 66:

The average of your highest 35 years of earnings is:

\$40,000



Your monthly benefit, based on your average earnings and claiming age =

\$1,500

33% for claiming later
+12% more for more earnings
= 45% more overall

More options if you're married

Special rules that raise the benefits of the lower-earning spouse—most often the wife—generally make claiming later an attractive option for married men.

The spousal benefit

If both husband and wife have claimed benefits, each is guaranteed half what the other would get at the Full Retirement Age (which used to be 65, is now 66, and will be 67).^[4]

- Spousal benefits are reduced up to 35% if claimed before the recipient's Full Retirement Age.

The survivor benefit

Widow(er)s can keep their own benefit or, if they chose, instead claim a survivor benefit equal to their spouse's monthly benefit.

- Survivor benefits are available as early as age 60, or age 50 if disabled, but are reduced up to 28.5% if claimed before the recipient's Full Retirement Age.^[5]
- Survivor benefits almost always go to widows, as most survivors are women (wives are generally younger than their husbands and live longer) and most wives have lower monthly benefits (they generally earn less and start to collect at younger ages).

Ex-spouses are entitled to these benefits if the marriage lasted 10 years.^[6]

WIDOWS' BENEFITS ARE CRITICAL

One in four widows over 65 is poor or near-poor.^[7]



Husbands can get more for their wives



Most wives will outlive their husband, by about 7 years on average, and most widows get their husband's higher monthly benefit in place of their own.

A husband can increase the monthly benefit his wife gets as his survivor more than 20% if he claims Social Security at 66, not 62, and 60% if he claims at 70.

Claiming later could be the most effective way a husband can improve his wife's long-term financial security.

You can continue to work after you claim

However, Social Security is designed to replace your earnings when you no longer work. So if you start to collect benefits and continue to work before you reach your Full Retirement Age, some of your benefits might be withheld.

Before the Full Retirement Age, Social Security withholds ...

\$1 for every	you earn above (in 2009) [Ⓜ]	
\$2	\$14,160/yr.	In calendar years <i>before</i> you reach the Full Retirement Age
\$3	\$3,140/mo.	In the calendar year <i>in which</i> you reach the Full Retirement Age

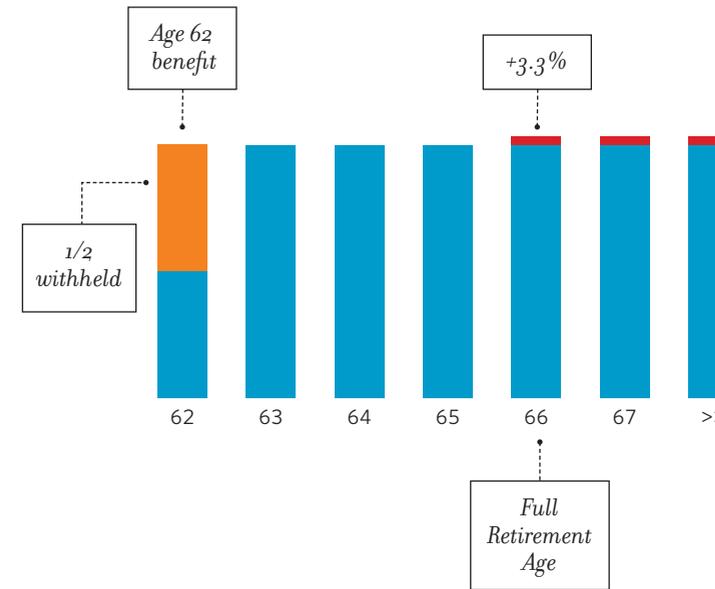


NO BENEFITS ARE WITHHELD

after the Full Retirement Age no matter how much you earn.

Benefits withheld aren't lost

They're rolled forward to increase your Social Security monthly benefits *after* you reach the Full Retirement Age.



For example, say you start to collect benefits at 62, continue to work, and only retire for good at 63. If you earn so much that half your monthly benefits are withheld, at the Full Retirement Age your monthly benefit is raised to what it would be had you started to collect at 62 and a half.

***** Benefits are withheld to increase your monthly benefits down the road.

You don't have to claim when you retire

Retiring and claiming are two different things. So if you have enough savings when you retire, you have two options.

OPTION 1

- *Start collecting right away. That's what most people do.*

OPTION 2

- *Delay and, while you wait, use a portion of your savings to live on. This option will draw down your savings more quickly, but increase the inflation-proof Social Security benefit you'll get each month for the rest of your life.*



YOUR CHOICE

Do you want a higher monthly benefit OR a bigger pile of retirement assets?

Should you delay or claim right away?



No one wants to draw down all their savings.

Savings are valuable as a reserve, can be invested in high-yielding assets, or left as an inheritance. But drawing an income out of your savings, over an extended period of time in retirement, can be tricky.

So it could make sense to use some of your assets to live on and delay claiming Social Security:

- ✓ If you need to assure you and your spouse a higher basic income for the rest of your lives.
- ✓ If you will still have enough savings for “rainy day” emergencies.

The choice is whether to use your savings to buy stocks, bonds, CDs, real estate, some other investment, or, in effect, a higher monthly Social Security benefit.

Yes, you might get less over your lifetime if you claim later

Monthly benefits are set so that lifetime benefits are much the same no matter when the average person starts to collect.

- *If you're in poor health and unlikely to live as long as the average person, you'll probably get less, over your lifetime, the later you claim.*
(That's because you probably won't get the higher monthly benefit long enough to make up for starting later.)
- **BUT NOTE:** *many whose health is poor still outlive the "average person."*

**ONLY 1 IN 7
COUPLES LOSE 15%**

*of lifetime benefits if the high earner starts at 66, not 62.*⁹

Should you bet that your life will be short?

No one really knows how long they will live.

But if your health is OK, you'll probably outlive the average person.

If you're married and both in good health, the odds are even greater that you or your spouse outlives the average person.

The cost could be quite high if you lose the bet and live "too long."

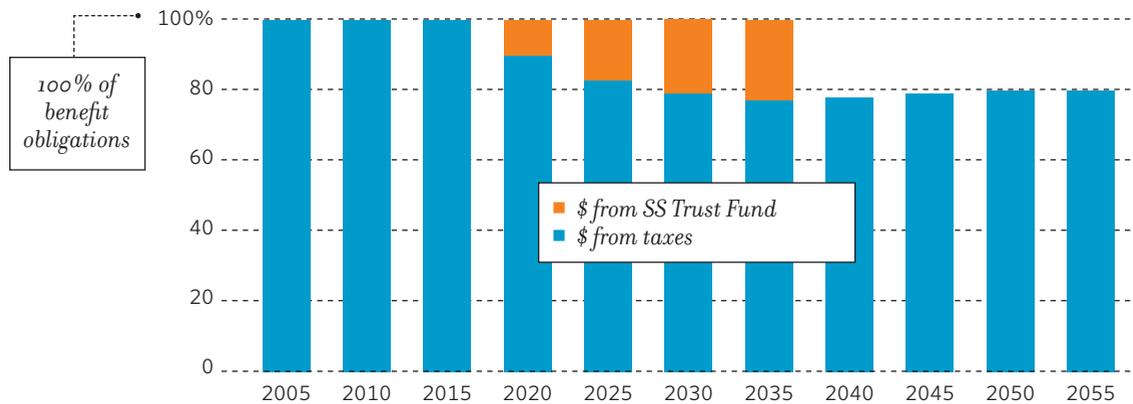
If blessed with long life, you might barely scrape by in your 80s.

***** *If you claim early, the odds of "losing big" could be much greater than the odds of "winning big."*



Don't start early because Social Security has money problems

Yes, Social Security has money problems. After benefit payments deplete the program's Trust Fund, in about 2037, Social Security will only be able to pay about 78¢ on the dollar.

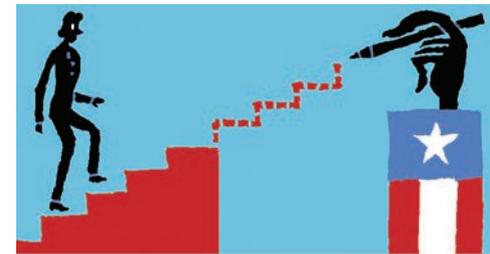


SOMETHING WILL BE DONE ¹⁰

Benefits will be cut and/or revenues will be raised.

You won't get more if you do

The most prominent proposals to cut benefits:



Raise the Full Retirement Age. (So those affected would need to claim later, and collect for a shorter period of time, to get the same monthly benefit.)



Freeze the purchasing power of monthly benefits at current levels. (So if wages continue to rise, Social Security would replace a smaller share of the earnings of those affected.)



Cut the benefits of high earners, but protect the benefits of low earners.

NONE OF THESE PROPOSALS give you more if you claim early. If you are affected, you'll get less no matter when you claim.

Nearly all proposals to fix Social Security would also protect those age 55 and older.

Special rules for some government workers

Social Security is designed to provide a basic retirement income to workers and their dependents. To achieve this objective and treat all workers fairly, Social Security:

- *Replaces a greater share of the earnings of low-wage workers, as they spend a greater share of their income on necessities and have less opportunity to save.*
- *Provides spousal and survivor benefits to dependent spouses who earn little or no pension on their own.*
- *Uses special rules to calculate benefits for workers with a pension from a job where they did not pay Social Security payroll tax.*

THE SPECIAL RULES MAINLY AFFECT:

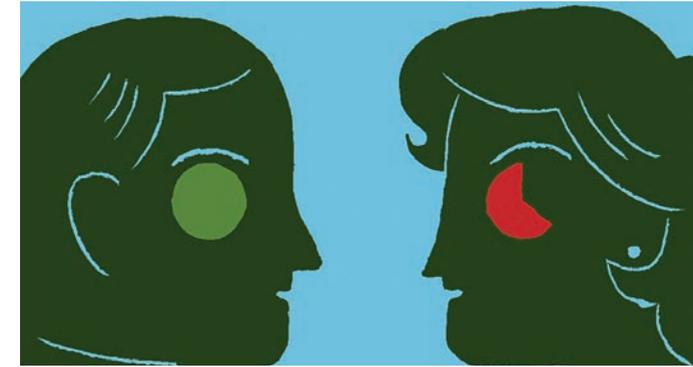
Government workers not covered by Social Security.

The standard rules don't work ...

... if you have a pension from a job where you did not pay Social Security payroll tax.

The standard rules determine if you are a **low-wage worker** based on the average of your highest 35 years of earnings on which you've paid Social Security payroll tax. But if you had a job where you did not pay payroll tax, that average is not a good indicator that you need a greater share of your earnings replaced.

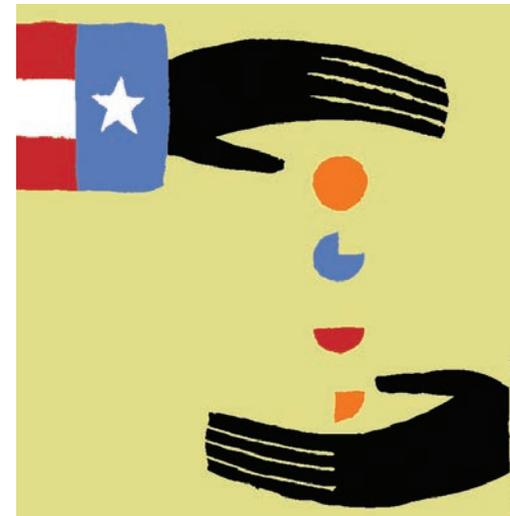
So if you have a pension from that job, special rules (which are complicated!) *more or less* base your benefits on how many years you paid payroll tax and your earnings during those years. [□]



The standard rules determine if you are a **dependent spouse** based on the Social Security benefits you've earned. But if you have a pension from a job where you did not pay payroll tax, your Social Security benefits alone clearly can't show that you earned little or no pension on your own.

So the special rules deduct from your spousal and survivor benefits $\frac{2}{3}$ of any pension income you've earned from a government job where you did not pay payroll tax. [□]

 To see how these rules affect you, go to the [Social Security benefit estimator](http://www.socialsecurity.gov/estimator) at www.socialsecurity.gov/estimator.



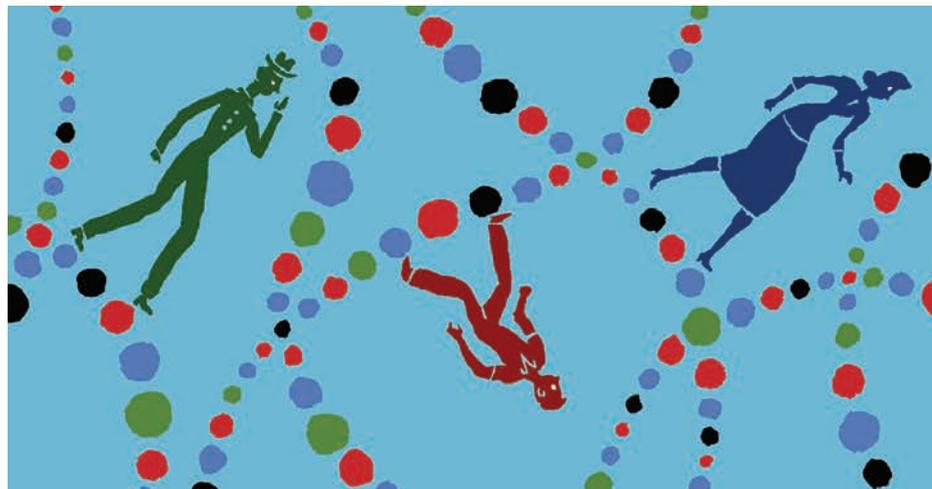
Next steps

You can claim Social Security at any age between 62 and 70.

- *Social Security is your safety net if at 62 you're in poor health or can't find a job.*
- *But if you can work, you have critically important options. You might want to quit and relax. But it's important to think long term. What's at stake is nothing less than the financial well-being of you and your spouse for the rest of your lives.*

SOCIAL SECURITY IS YOUR SECURITY

You can draw it down or save it up. The choice is yours.



What you can do now

Estimate how much retirement income you and your spouse will need and how much of that income needs to be secure.

Target when you would like to retire, considering the effect on your retirement income and how difficult (or easy) it would be to work longer. Social Security's estimator should be a big help: www.socialsecurity.gov/estimator.

Now make a plan that allows you to work to that age. It could mean learning new skills, taking on a new role at work, and seeing that your employer, or perhaps a new employer, has plans that allow you to stay on that long.



The key to any retirement plan is setting a target retirement age, and having a plan that allows you to work to that age.

Explanations

For publications cited below and information on topics not covered in the Guide, go to http://crr.bc.edu/special_projects/claiming.html

¹ Your Social Security benefits are not subject to federal income tax if your “combined income” (adjusted gross income + non-taxable interest + ½ your annual benefits) is less than \$25,000 (\$32,000 if married and filing jointly); 85% is taxed if your “combined income” is at least \$34,000 (\$44,000 if married and filing jointly); and 50% is taxed if your “combined income” is between these two amounts.

² Barbara A. Butrica, Joshua H. Goldwyn, Richard W. Johnson, “Understanding Expenditure Patterns in Retirement.” Center for Retirement Research at Boston College, 2005.

³ When calculating average Social Security earnings, earnings prior to age 60 are updated to account for national average wage growth. For further details, see Social Security Administration, *Your Retirement Benefits*, SSA Publication No. 05-10070.

⁴ The Social Security Full Retirement Age depends on when you were born:

Birth Year	1943-54	1955	1956	1957	1958	1959	1960 & later
Full Retirement Age	66	66 + 2 mos.	66 + 4 mos.	66 + 6 mos.	66 + 8 mos.	66 + 10 mos.	67

The spousal benefit top-up (the difference between your own earned benefit at your Full Retirement Age and half your spouse’s benefit at his or her Full Retirement Age) is reduced 30% if you claim at 62 and your Full Retirement Age is 66, and 35% if your Full Retirement Age is 67. For more on the spousal benefit, see Social Security Administration, *Retirement Benefits*, SSA Publication No. 05-10035.

⁵ Widow(er)s are guaranteed at least 71.5% of their deceased spouse’s Full Retirement Age benefit if they claim the survivor benefit before their Full Retirement Age, and at least 82.5% if they claim the survivor benefit after their Full Retirement Age. For more on survivor benefits, including survivor benefits for dependent children, see Social Security Administration, *Survivors Benefits*, SSA Publication No. 05-10084.

⁶ Benefits paid to an ex-spouse do not reduce your benefits, nor the benefits of a subsequent spouse.

⁷ Authors’ calculation from the U.S. 2007 Current Population Survey.

⁸ The amounts you can earn before Social Security benefits are withheld are updated each year to account for national average wage growth. Also see Social Security Administration, *How Work Affects Your Benefits*, SSA Publication No. 05-10069.

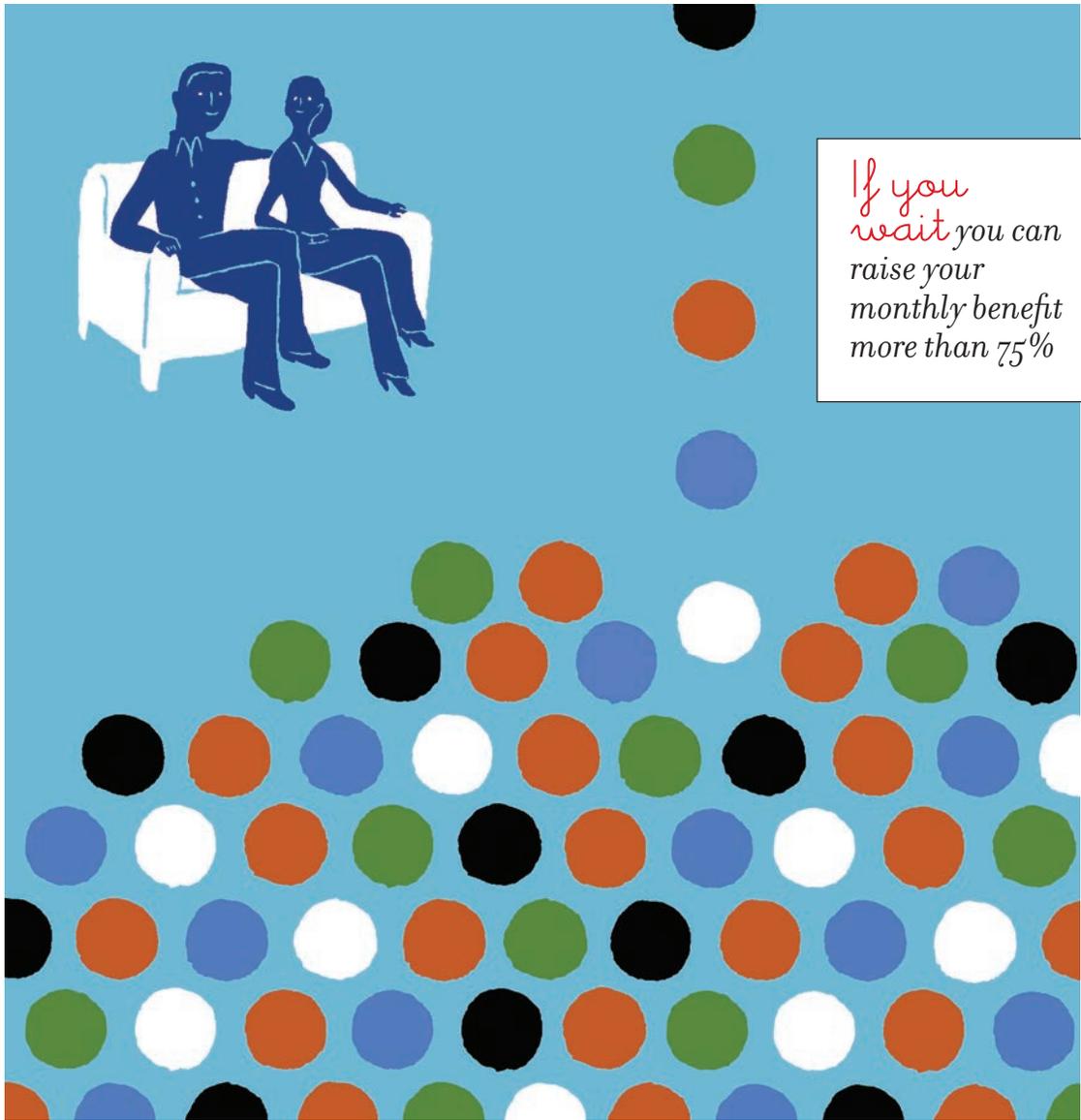
⁹ One-earner households with average mortality patterns.

¹⁰ For a guide to the most prominent proposals for fixing Social Security’s long-term financing problem, see *The Social Security Fix-It Book*, Center for Retirement Research at Boston College, revised 2009 edition.

¹¹ Social Security Administration, *Windfall Elimination Provision*, SSA Publication No. 05-10045.

¹² Social Security Administration, *Government Pension Offset*, SSA Publication No. 05-10007.





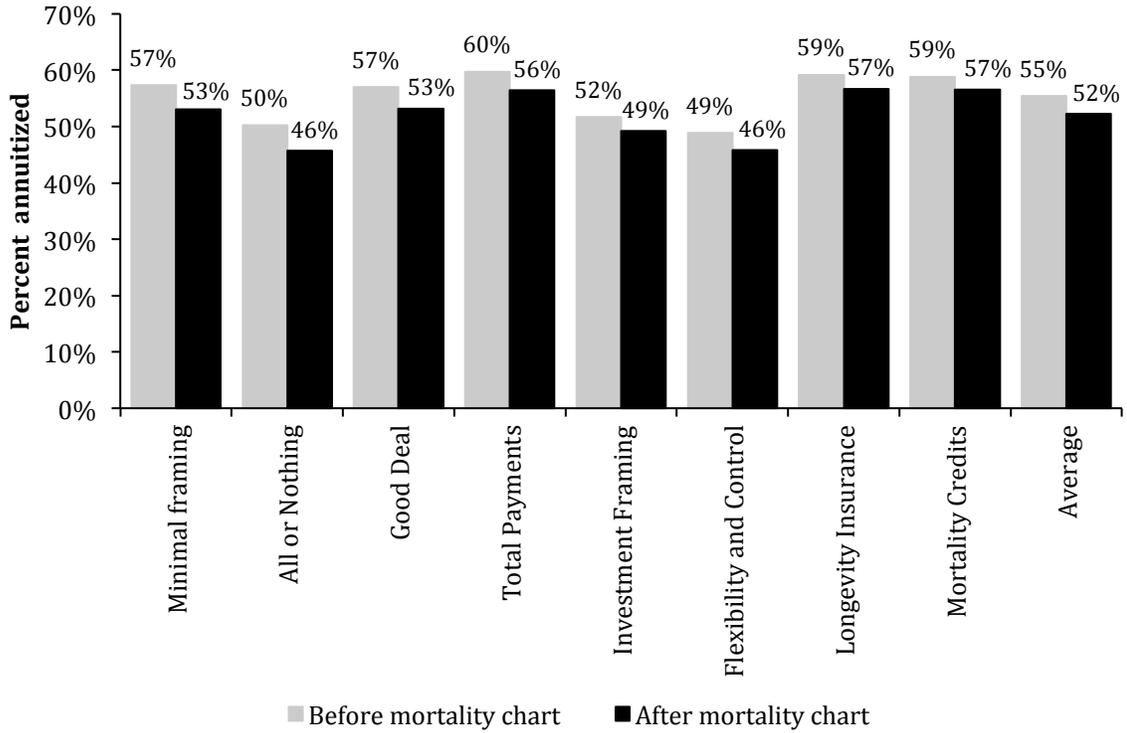
*If you
wait you can
raise your
monthly benefit
more than 75%*

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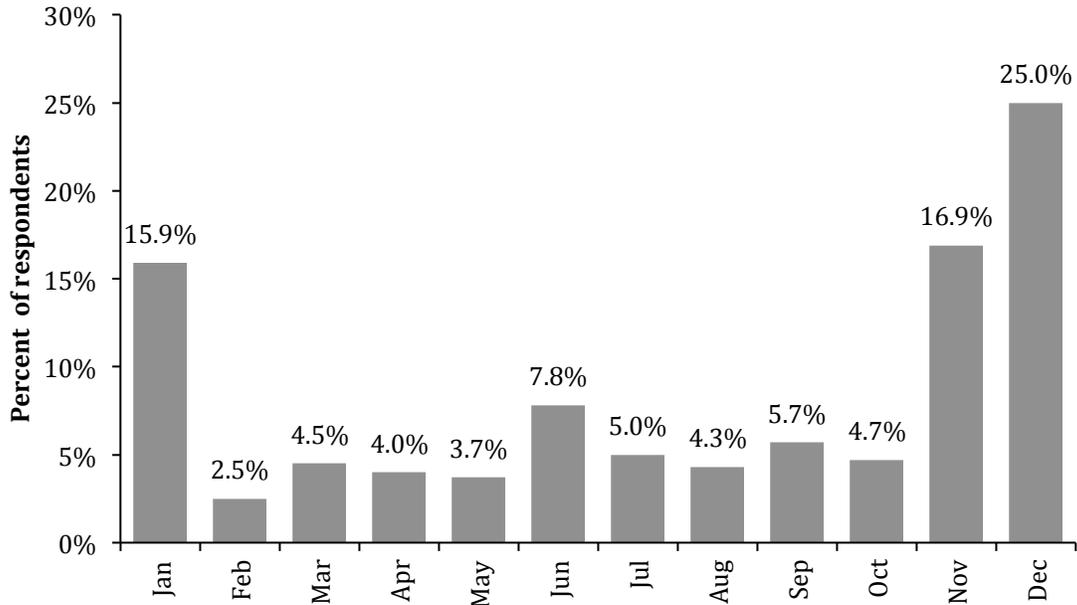
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Figure 11. Average percent of balances annuitized in Survey 2 before and after seeing mortality chart



Source: Authors' calculations

Figure 12. Month chosen for bonus payment in Survey 1



Source: Authors' calculations

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My opinion or numerous sources compiled by me

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