July 2005 *MoneyMinute* – Is an Annuity a Good Investment for You?

At ICM, we are all fee-only planners and we're a bit self-righteous about it. But as you read these real-people stories, you'll understand why we couldn't operate our business as anything but fee-only. We have seen some truly horrible cases that involve annuities. Technically these cases are not illegal, but they exhibit ethically challenged advisor behavior. We thought we would share a few of the worst cases as a warning for all and to invite you to share your annuity or bad investment stories with us:

1. Sara, a 40 year old married woman had to roll her 401(k) plan along with her former company pension cash-out to another custodian. Her mother was working with a fellow at AG Edwards, so she went to see him. He recommends that she roll this money into an annuity that would guarantee the principle. Sara is sharp, but not financially savvy. She asks this financial advisor "how do you get paid?" to which he replied, "do you ask your bank how it gets paid?" She figured this advisor knew what he was doing and purchased the annuity. After Sara found her way to me, I looked into the fine print of her annuity. The annual fees are over 3% each and every year. There was also a commission of over $8300 paid to AG Edwards and her advisor. He knew what he was doing! No wonder he dodged Sara's direct question! You may ask, "What's so wrong with this situation?" First, Sara's money was already tax-deferred, it certainly doesn't need a second layer of tax-deferred status within an annuity - - it could just be moved to a Rollover IRA account. Second, if your advisor does not give you a direct answer – run away. You have every right to ask and know how your advisor is compensated. If Sara knew that her advisor would receive an $8000 commission if she put her money where he suggested, I think she might have realized it might not be best for her.
2. This next case involves, Betty, a 60 year old woman who lost her husband in an accident. The gentleman Betty went to see advised her to put the $60,000 payment of life insurance into an annuity. Two or three years later he contacted her to say he had a better investment and moved her money to a different annuity. Well, when he contacted her the third time to say he had an even better investment, Betty came to see me. What's wrong with this situation? This "gentleman" was flipping her annuity in order to generate more commissions for his pocket. With all of these annuities that are sold, there is a withdrawal penalty that usually lasts for three to twelve years. He was asking her pay the penalty and move the annuity to another company just so he could increase his commission. And what were the results of these great "investments"? Betty's original $60,000 was down to $45,000 when I saw her; whereas if it had been invested in a rational, diversified strategy her account would have been worth over $100,000 after all fees.
3. This last situation may be the worst, but thank goodness, Eva's instincts were right on. Eva, 55, lost her husband last year. She went to see her husband's advisor at American Express. She looked over Eva's situation and noticed about $70,000 sitting in a bank account. The advisor

suggested that Eva put that money into an annuity paying 3.5% for life. Eva figured that would barely cover her utility bill, so she said, "no thank you". Well next the advisor suggested that Eva sell her home and move into a mobile home so she could invest the proceeds into the great investment that the advisor has. This great investment turns out to be a limited partnership (very illiquid) that invests in strip malls! Is this an appropriate investment for a recently widowed woman who is looking for a job???!!

We all have stories to share; and we would like to hear yours. If you or a friend happen to be the recipient of one of these unfortunate investments, send us your story or contact us for a second opinion.

Sincerely,

Julie Schatz, Financial Planner

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