

Instructions for entering data and viewing results in annuity spreadsheet:

You may only enter data in the yellow fields. Results will be instantly displayed in the blue fields after entry.

- Beginning value – the initial investment amount. Enter dollar amount with no dollar sign, commas or periods.
- Gross return – the average rate of return before expenses and taxes. To make a fair comparison, they should be the same. There is no possible reason to expect a higher gross return in a variable annuity account than a fund would generate. Enter percent as whole numbers with decimal places (i.e. 11.2% should be entered as 11.2).
- Expense ratio – The expenses at the mutual fund level for management fees, etc. Very often variable annuities have higher expenses than a clone mutual fund, but in this case we will give them the benefit of the doubt. Expense ratios can vary from 0.2% to over 2.0%. Industry average is about 1.3%. Enter expense less than 1% with a zero point preceding it (i.e. 0.2% should be entered as .2%, typing in the % sign).
- Mortality and Expense Ratio – The additional charge to cover the mortality guarantees of the variable annuity contract. Mutual funds do not impose these charges. While a few “no-load” variable annuities may have M&E charges as low as 0.4%, most charge about 1.4%. M&E fees are almost pure profit to the insurance company, and the value of any guarantee is questionable.
- Net Return – The difference between the gross return and the expenses. Because of the M&E fees, annuities are at a severe disadvantage.
- Separate account fees – A fee imposed by most Variable Annuity contracts for each separate account. A typical fee might be \$20 per year per fund. So an investor using five funds inside one contract might be charged a flat \$100 extra each year. Separate account fees impose a very heavy burden on small accounts. Few mutual funds impose them.
- % of Annual Return Capital Gains – Mutual fund investors pay taxes on capital gains distributions each year. Enter the average percent of the distribution that is subject to capital gains tax. Variable annuities pay no tax during the holding period.
- % of Annual Return Ordinary Income – Mutual fund investors pay taxes on short term capital gains, dividends, and interest distributions each year. Enter the average percent of the distribution that is subject to ordinary income tax. Variable annuities pay no tax during the holding period.
- The total of the two tax percentages may not exceed 100%. You will notice that taxes are a significant burden on mutual fund returns. These taxes are almost exclusively due to turnover inside the mutual fund, so low turnover is a must in taxable accounts.
- Accumulation Tax Rate Ordinary – The average marginal income tax of the investor during the holding period. The individual’s rate may vary from 0% to

- 39.6%. The appropriate tax amount is withdrawn from the account each year in our mutual fund calculation. Variable annuities pay no tax during the holding period.
- Accumulation Tax Rate Capital Gains – The investor's capital gains rate, either 10 or 20 percent. The appropriate tax amount is withdrawn from the account each year in our mutual fund calculation. Variable annuities pay no tax during the holding period.
 - Distribution Tax Rate – The ordinary income tax rate at which the distribution from the Variable Annuity will be taxed. This rate may be higher or lower than during the accumulation phase. All funds withdrawn in excess of the basis in the annuity are taxed at ordinary tax rates. The loss of capital gains treatment for annuity distributions is a tremendous disadvantage.
 - Distribution Capital Gains Rate – The investor's capital gains rate upon liquidation of the account. This rate may be higher or lower than during the accumulation phase. Previous taxable distributions increase the basis in the account, lowering the amount of capital gains tax upon liquidation.

Tab down to see the results below the inputs. How much you have to tab will depend on your screen resolution. We illustrate results after all taxes for 10, 15, 20 and 50 years. The difference is what a Variable Annuity costs the investor.

We have compared an average mutual fund against the average variable annuity. If we had chosen to compare a no-load index fund against a variable annuity, the results would be even more lop sided against the annuity. And, of course, I would strongly suggest that that's the approach investors should take.

Conclusion: Just say no to variable annuities! The loss of capital gains treatment and additional annuity expenses eat up more than the benefit of deferral in almost any reasonable case you can make up.