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ROBERT POWELL

## Insuring for a long life

**Longevity insurance solves problem of outliving assets, but there are downsides**

By [Robert Powell](#), MarketWatch

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**BOSTON (MarketWatch) -- The good news is that Americans are living longer than ever before, with Americans' life expectancy hitting a record high of 78.1 years in 2006.**

The bad news?

Those 50% of Americans who will live beyond life expectancy (it's 80.7 years for women, 75.4 years for men, and varies further based on ethnicity) need to make sure they have enough assets to support their lifestyle should they live a long life.



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more asset classes."

And few individuals seem inclined to buy such insurance at the moment, but in the coming years, it's likely that longevity insurance will play a role in some retirement-income portfolios.

But when is the use of longevity insurance indicated? And what are the advantages and disadvantages of the product?

### What is it?

At its core, longevity insurance is a fixed payout annuity with a long deferral period, said Chad Runchey, a manager with Ernst & Young's Insurance and Actuarial Advisory Services. "It's insurance against the risk of living too long," he said.

According to NAVA, an industry trade group, "the defining characteristic of these products is that they provide ... guaranteed future income, generally starting at an advanced age such as 85, to those who are still living. The idea is that longevity is a risk that can be pooled and diversified much like life insurance.

"Those who die prior to age 85 'subsidize' the income stream paid to those who reach 85. With these products, a relatively small portion, for example 10%, of the retiree's nest egg is invested in annuities. The remaining 90% can be used to fund retirement prior to age 85 as the longevity insurance will provide an income stream to cover the years after age 85," according to NAVA.

In the case of the Hartford Income Security product, the minimum issue age is 40; the premium payment options are either a single premium (\$10,000 minimum) or level premium payments (\$10,000 minimum over a maximum 10-year period); and the income payment options are single lifetime, joint lifetime, single life with cash refund, and joint life with cash refund (the maximum income start age is 85).

According to The Hartford's Web site, a 60-year old male who wants to receive \$1,000 a month beginning at age 85 would have to pay \$16,000 for a single life/cash refund policy.

"Longevity insurance is basically an income annuity with a long deferral period (typically 20 to 30 years) before payments begin," according to Joseph Tomlinson of Tomlinson Financial Planning, LLC, author of "Products for Managing Retirement Risk -- Looking to the Future."

Tomlinson says that a "key advantage of longevity insurance over a standard income annuity is the product price.

For example, if a 65-year-old wanted to purchase a lifetime annuity that paid \$40,000 in the first year, increasing at 2.5% per year thereafter, the cost would be about \$625,000. If the same person wanted to purchase longevity insurance based on the same payment stream, with payments of \$65,500 beginning at age 85 (\$40,000 increased at 2.5% annually for 20 years), the cost would be only \$95,000."

#### Who needs it?

For his part, Runchey said Americans for whom outliving their assets is a big concern are ideal candidates for longevity insurance, as are Americans who have a history of family members living past 85.

Ideally, he said longevity insurance would be used in combination with other products and investments. For instance, the typical buyer might invest 10% of their assets in longevity insurance now, knowing that 90% of their assets will cover their living expenses until age 85. Then the longevity insurance would kick in to cover living expenses after age 85.

Another advantage, according to Runchey, is that buyers of longevity insurance might be able to invest more aggressively knowing that their income needs are covered after they turn 85. "These products allow you to take on additional risk," he said.

#### Consider the downsides

Longevity insurance is not without disadvantages. Typically, longevity insurance doesn't come with an inflation or cost-of-living rider. That means the buyer may have to buy longevity insurance in combination with investments or other products that mitigate the risk of inflation, such as TIPs or stocks, and/or they might consider purchasing longevity insurance that pays out in excess of one's estimated income need at age 85.

Another disadvantage: If the buyer dies before age 85, the money belongs to the insurance company. Runchey said a buyer can purchase a rider that guarantees return of premium should the owner die before age 85. But those policies might either cost more or pay out less than policies without that rider.

Longevity insurance poses other problems as well. One has to do with investor behavior. Americans aren't so fond of delayed gratification. In other words, Americans may not be eager to shell out money now in hopes of getting something in return 20 years hence.

In addition, longevity insurance is subject to anti-selection risk. That's the risk that only people who are likely to live beyond age 85 will purchase such insurance. And those two issues could mean that longevity insurance will forever remain a niche product. "While the approach is conceptually interesting, anti-selection risk and delayed gratification may impede widespread availability and adoption," said NAVA.

Runchey, for his part, said that longevity insurance should be given a fair and complete evaluation. "It's a complicated product for people to understand if they are in the accumulation mindset," he said. "But it's the only product that is set up to take the risk of outliving assets out of the picture. And it does that efficiently."

Tomlinson wrote in his report that "perhaps the biggest problem faced today in making this product a success, is that it is so different from the types of products that planners and financial sales people have been offering to their clients," he wrote.

"Retirement planning, including the use of annuity products, has always focused on savings. This is the first attempt to focus on more of an insurance product to deal with longevity risk." ■

*Robert Powell has been a journalist covering personal finance issues for more than 20 years, writing and editing for publications such as The Wall Street Journal, the Financial Times, and Mutual Fund Market News.*



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