Annuities are more popular than ever: Last year, buyers put a record $310.6 billion into the hybrid insurance and investment products, and sales are still going strong. Fixed-rate annuities, which guarantee a rate of return over a set time period, did particularly well, more than doubling their sales from the previous year.

Why are annuity sales surging? One reason is that stocks and bonds both had terrible years in 2022, and they haven't been stellar this year either. Meanwhile, the Federal Reserve has raised interest rates aggressively, fueling recession fears. Both factors have made annuities, with their promise of predictable income streams, look like a safe haven. In addition, those rising interest rates have also translated into higher annuity payouts.

Early in my career I really liked annuities. They provide that reliable stream of income over a specific period or for life. They can help provide financial stability during retirement, and help mitigate the risk of outliving your savings.

But I quit selling them 15 years ago. One of my big concerns with annuities is that there's a huge incentive for financial advisors to push them on clients. The sales commissions are typically 5% or 6%. So if an advisor sells a $1 million annuity, he or she pockets a quick $50,000 or $60,000. It's easy for advisors to overlook the question of whether an annuity is right for their client when they know recommending one could put a new Tesla in their driveway.

By the way, I never receive sales commissions for selling any financial product. As a fee-only, fiduciary advisor, I'm paid strictly for giving objective advice about investing and financial planning.

Annuities also lock up your money, typically for five to 10 years. During this "surrender period," if you withdraw more than a certain percentage of your annuity's value, you may be subject to steep surrender charges. Surrender charges typically start at 7% in the first year and decrease by 1% each subsequent year until they reach 0%.

Tying up your money for several years also carries an opportunity cost. In other words, you may miss a change to earn higher returns elsewhere. If, for example, we get another bull market

where you have a chance to earn 10%, 15% or 20% returns, you'll have to settle for single-digit returns from a fixed-rate annuity.

It's true that you can earn more using an index-linked annuity. But annuities in general tend to have higher overall costs and fees than, say, mutual funds due to their insurance features, guarantees and administrative expenses. And the returns of index annuities are typically capped so that the insurance companies that issue them can ensure that they make a profit. In other words, you can leave money on the table with an index annuity.

Finally, annuities can create bad tax situations for both their owner and any heirs. Annuities aren't tax-free, they're tax deferred. And they're taxed as ordinary income, which is a higher rate than the capital-gains rate that applies to stocks and bonds. And it's impossible to say what your income-tax rate will be during the course of your retirement. If you're in a high tax bracket, you could really get walloped.

Furthermore, if you pass away while holding an annuity, your beneficiaries may not receive a step-up in tax basis as they would with stocks and other kinds of investments. This means that any gains that have accrued within the annuity would be subject to income tax when the beneficiaries receive distributions.

There are probably cases where annuities make sense for certain people, but I'm hard-pressed to name one. With the benefit of 24 years' experience as an investment advisor, I've come to believe there's pretty much always a better alternative. Don't hesitate to reach out to me if you'd like to learn more.