

Is Your Insurance Company Safe?



The recent financial difficulties of some of the largest and oldest insurance companies may have you wondering about the financial strength of your insurer. Here are some sources of information that you can use to help you determine whether your insurance policy is safe.

It's in the ratings

There are several rating services that review, evaluate, and rank insurance companies based on their financial strength and claims-paying ability. The primary players in the ratings game are A.M. Best (www.ambest.com), Standard & Poor's (www.standardandpoors.com), Fitch (www.fitchratings.com), Moody's (www.moody.com), and The Street.Com (formerly Weiss, www.thestreet.com).

The standards used by each ratings service differ, and the ratings ultimately reflect the service's opinion of the financial strength and claims-paying ability of the insurer--it is not a guarantee of future performance. So you should consider your insurer's ratings from at least two or more services to determine its financial strength.

State regulation

Insurance companies are heavily regulated by the states in which they are headquartered. Generally, each state requires that an insurer has sufficient reserves to pay all of its claims. In addition, states require that companies file updated financial reports that often are available to the public through the state's insurance department. Check with your state's department of insurance for information about the company maintaining your policy.

Important financial information

While financial ratings are important, there are other sources that provide financial information about your insurer. For instance, the National Association of Insurance Commissioners (NAIC) is an organization representing the insurance departments of all 50 states. You can access their information by going to www.naic.org. An important statistic contained in the NAIC's financial report of each company is the assets to liabilities ratio.

This statistic compares the insurer's total assets to its total liabilities. For example, a favorable assets to liabilities ratio may be \$108 of assets for each \$100 of liabilities.

Comparing companies

Many insurers subscribe to the Standard Analytical Service, Inc., an independent organization that compares insurance companies based on financial statements filed with state departments of insurance. Many insurers publish the Standard's reports on their websites.

The reports compare insurers based on a few important statistics. One such statistic compares the ratio of an insurer's bonds, stocks, cash, and short-term investments to liabilities. A higher ratio of liquid assets to liabilities may indicate the company's ability to cover unforeseen emergency cash requirements if they arise.

Another statistic compares an insurer's surplus assets to life insurance in force. A high ratio of surplus to life insurance in force provides evidence of a company's ability to meet its claims obligations.

If you claim benefits from your policy during a period of extraordinary claims activity, will your insurer be able to satisfy your claim? The chances are better if the insurer has a high ratio of assets, including capital, to policy reserve liabilities. A high surplus ratio may indicate a company's ability to meet its claims obligations even during a period of high volume.

If the worst happens ...

If your company experiences severe financial difficulties, it might be taken over by the state's insurance department. Generally, claims continue to be honored as long as premiums are current. If the company lacks sufficient assets and reserves to pay all claims, the state's guaranty association will either pay claims directly or transfer the policies to a financially stable insurance company that will honor the claims. The National Organization of Life and Health Insurance Guaranty Association (NOLHGA) provides information on state guaranty associations and insurance companies that have failed or are in danger of failing (www.nolhga.com).

Income Annuities Can Help Fill the Retirement Income Gap

If you're like many retirees, you may find that your sources of fixed retirement income, such as employer or military pensions and Social Security, aren't enough to meet all of your retirement income needs. To make up the difference, you can draw from your savings and investments, but how much can you safely withdraw without running out of money? One option is to create a stream of income for the rest of your life by investing some of your savings in an income annuity.

Income annuities (also known as immediate annuities) are purchased from insurance companies. In exchange for a lump sum of money, the issuer promises to make payments to you for a fixed period of time or for the rest of your life, or for the rest of your life and that of your spouse.

You can use almost any type of savings or investments to create a stream of income that can last for your lifetime. For example, you can purchase an income annuity with money from your personal savings accounts, matured CDs, or investments such as stocks, bonds, and mutual funds. You can even convert a portion of your retirement plan, such as an IRA or 401(k), to a lifetime stream of income by purchasing an income annuity within the retirement plan. However, some of these transactions may have income tax implications, so consult your tax advisor before you proceed.

You have options

You generally can choose how long your income annuity payments will last. For example, you can choose to receive payments for the rest of your life. This option allows you to supplement lifetime income from other sources, such as Social Security. However, payments end at your death, providing no benefits to your surviving spouse or heirs.

To ensure that your spouse continues to receive income after your death, you can select a joint and survivor payment option. The annuity will make payments to you, then at your death, to your surviving spouse until his or her death. Payments end at the death of the surviving spouse, with no benefits payable to your heirs.

You also can choose to receive income payments for a fixed period of time, such as 5 or 10 years, by setting up an income annuity. If you die during the payment period, your beneficiary will receive the remainder of the payments, either systematically or in a lump sum.

Another choice combines lifetime payments with the fixed period option. Payments are made for life or for a fixed period of time, whichever is longer. This alternative makes certain that payments will last for a minimum number of years.

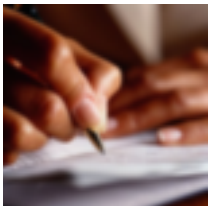
Other factors to consider

- Payments from income annuities funded with pretax dollars, such as 401(k)s and IRAs, may be subject to income tax. Income annuities purchased with after-tax funds are taxed only on the earnings part of each payment. The remaining portion is considered a return of your investment and is not subject to taxation.
- Usually, once you select a payment option, you can't change it. This means you may not have access to any of the funds you used to purchase the income annuity aside from the income payments you receive.
- Since some payment choices, such as the life or the joint and survivor life options, end at death, it's possible you won't live long enough to receive at least the return of your investment in the income annuity.
- Fixed income annuity payments don't change, even if your income requirements do. You may find that the income from the annuity isn't enough to meet increased income needs.
- Choose a financially strong company. Annuity guarantees are entirely dependent on the insurance company's financial ability to meet its obligations. Check the financial ratings of the company offering the income annuity before making your purchase.

Is an income annuity right for you?

Consider an income annuity if you want a guaranteed income to fill the gap between your retirement income needs and your fixed retirement income. Also be sure you can buy the income annuity and still have enough savings for other expenses.

Ask the Experts



How much of your company's stock should you hold?

No matter how good a company you work for, you should think carefully about how much you should have invested in it. Yes, there are companies

whose employees have become wealthy from company stock that was part of their compensation. But there also are stories about employees of companies such as Enron, Bear Stearns, and Lehman Bros.--people who believed in their employers but learned the hard way that allowing one company--especially a current employer--to dominate their investment or retirement portfolio can have devastating consequences.

According to the most recent Employee Benefit Research Institute statistics (Issue Brief No. 308, August 2007), company stock represents an average of 11% of 401(k) plan participants' assets (though that percentage is less than in previous years). However, few mutual fund managers would allow a single stock--any stock--to represent that much of a fund's portfolio. And a corporate pension plan is actually prohibited from investing more than 10% of its holdings in the company's own stock.

What issues might company stock options raise at tax time?

If stock options are part of your compensation package, a significant market downturn can mean special financial pain.

In many cases, people who receive options to buy their company's stock find that during a downturn, the stock's market price is lower than the option's exercise price. Since few would choose to exercise an option that requires paying more than the market price, the option is said to be "underwater"--a situation that was widespread last year. If your options are underwater, it's worth checking to see if your company has considered asking its shareholders to approve repricing the options, or exchanging them for a smaller number of options with a lower exercise price. Some companies are taking such steps to try to retain valued employees.

If you exercised options to purchase your company's stock in 2008, you may face a more complex problem. The type of option and when you exercised it can raise a number of issues at tax time. If you own nonqualified stock options, you'll generally owe ordinary income tax on the difference between the exercise price and the stock's market value as of the date you exercised it. That amount is considered

Ironically, the better your company's stock has performed, the greater the chance that it may have grown to dominate your portfolio. However, even if your company is a good one, working at a company means you've invested your "human capital"--your earning ability--in that firm. If you also have a large portion of your investment capital there, your financial well-being is even more dependent on a single company. If a company's stock is suffering, it might react by cutting jobs companywide. If yours were one of them, both your human and investment capital would be hit.

And don't forget to consider whether an equity mutual fund you hold also may have invested in your company's stock. You can find out a fund's holdings by checking its annual and semiannual reports. You can use the information to estimate your total exposure to your employer's stock.

compensation and, if you're an employee, should be listed on your W-2 form.

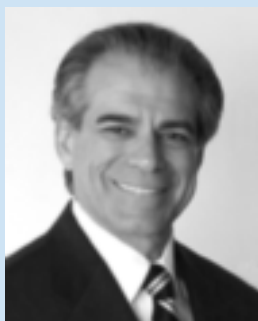
If you exercised incentive stock options (ISOs), tax is ordinarily deferred until you sell the stock that you acquired. However, unless you sold the stock in the same year that you acquired it, you have to factor in the alternative minimum tax (AMT). For AMT purposes, when you exercise an ISO, income is generally recognized to the extent that the fair market value of the shares when acquired exceeds the option's exercise price. This means that a significant ISO exercise in one year can trigger AMT liability, even though no income is actually received. This application of AMT could be a real problem if you exercised the options in early 2008 and later saw the value of the stock you received dramatically decline in value. If you are subject to AMT as the result of an ISO exercise, you'll be entitled to a resulting AMT credit that can be used in future years. The Emergency Economic Stabilization Act of 2008 included some relief for taxpayers who exercised ISOs prior to 2008, and makes it easier to claim unused AMT credit. However, it will be of little help if you exercised ISOs in 2008.

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**Hillard Rest
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Hillard Rest is a well-known expert in those matters concerning "Retirement Income Planning" and "Wealth Preservation strategies." He strives to educate his clients on how to invest profitably and avoid loss by providing conservative options. Hillard earned the coveted recognition of Certified Financial Planner professional in 1987.

You are invited to listen to my radio show "Focus on Finance." Tune in on Sundays at 10 am on KLAA AM830. I have archived the shows on the Focus on the Finance website at www.FocusOnFinanceRadio.com so that you can hear them at your convenience.

I want to help you make smart and prudent financial decisions as you plan your life in pre-retirement and retirement. Call me anytime to talk about your finances or for answers to any particular questions you may have at 800-786-4098

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