UNITED METHODIST FOUNDATION OF MICHIGAN

Understanding Annuities: Important Considerations for Church Leaders

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As stewards of their congregations' financial health, church leaders often navigate complex decisions regarding value-aligned investments and financial planning. One such decision involves the misguided consideration of index or variable annuities for churches. Insurance annuities are sometimes misrepresented as a viable option for securing future church income. However, it's crucial to understand why annuities do not align with the financial principles of a church.

What is an Annuity?

An annuity is an insurance product typically sold by insurance companies. It functions as a contract where an individual or organization pays a lump sum or periodic payments to an insurer. In turn, the insurance company then promises to pay back the principal amount plus earnings in the form of periodic payments or a lump sum at a later date. Annuities are often marketed as a way to provide a steady income stream for individuals in retirement. This article does not address the individual benefits of an income annuity as part of an individual's retirement portfolio. However, these personal benefits are not comparable to an indexed or variable annuity that is marketed to a nonprofit organization.

Why Should a Church Avoid Purchasing Annuities?

1. **Nature of Annuities as Insurance Products:** Annuities are fundamentally insurance products with high surrender fees or commissions. They are designed to mitigate personal risks such as longevity risk (outliving one's savings) and market volatility. While these reasons may seem appealing to a broader market than individuals, nonprofit organizations, like churches, operate under extremely different financial goals and stewardship principles than individual investors.
2. **Investment vs. Stewardship:** Churches typically manage funds with a focus on socially responsible stewardship and long-term sustainability. Annuities, however, involve complex fee structures and terms that do not align with the transparent and prudent financial management expected of church leaders. They limit liquidity and lock-in investors for a defined time period.
3. **Limited Growth Potential:** Unlike investments in diversified portfolios, like the Balanced Fund, annuities often offer limited growth potential. Returns may not keep pace with inflation or match the potential returns from other diversified investment strategies.

4. **Long-Term Financial Planning:** Churches are encouraged to adopt long-term financial planning strategies that balance growth, liquidity, and risk management. Annuities, with their fixed terms, lack of transparency, and limitations on access to funds, restrict flexibility in adapting to future financial needs or opportunities.

What Are a Few Best Practice Approaches for Churches?

1. **Value-Aligned, Diversified Investment Strategies:** Consider diversifying investments across various asset classes to balance risk and return objectives while maintaining liquidity. The Balanced Fund is an excellent example of this type of diversification.
2. **Financial Education and Guidance:** Equip church leaders with financial education and seek guidance from Foundation staff who understand the unique financial considerations and requirements of United Methodist churches.
3. **Stewardship Principles:** Uphold stewardship principles by ensuring transparency, accountability, and ethical management of financial resources entrusted to the church.

Conclusion:

In conclusion, while annuities may serve as a viable option for some individuals seeking guaranteed income, index or variable annuities do not align with the financial objectives and stewardship principles of churches. Annuities customarily are among a class of imprudent products for endowment funds. Understanding the distinction between insurance products, like annuities, and traditional investment choices, like stocks, bonds, and money markets, is crucial for making informed financial decisions that uphold the integrity and long-term sustainability of church finances.

By prioritizing transparency, prudent financial management, and strategic planning, church leaders can navigate value-aligned financial decisions with confidence and ensure that resources are used effectively to support the mission of the church. In essence, while the decision to purchase an index or variable annuity may initially seem attractive for leaders of a declining church, understanding the fundamental difference between an insurance product and an open market of investment opportunities is imperative to ensuring responsible stewardship of resources for generations to come. Church leaders would be well advised to revisit their core purpose, long-term vision, and organizational life cycle to determine their best approach to financial solvency and sustainability. The Foundation provides a variety of staff and services to help address all of these unique challenges.