Difference Between Annuity and Life Insurance

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Key Difference - Annuity vs Life Insurance

Both annuities and life insurance should be considered as a part of a long-term financial plan. The key difference between annuity and life insurance is that **annuity is a means of retirement plan where an individual keeps aside a lump sum of money to be used in retirement** whereas **life insurance is taken out to provide economic protection for dependents at the death of the individual**. In certain types of annuity and life insurance, a beneficiary who takes either policy to gain the legal right to claim the funds is specified by the individual.

What is Annuity?

Annuity is an investment from which periodic withdrawals are made. To invest in an annuity, an investor should have a large sum of money to be invested at once and withdrawals will be made over a period of time. Annuities are tax-deferred financial products, meaning tax savings are allowed on withdrawals made. Annuities are mainly taken out as retirement plans to receive a guaranteed income on retirement. Below mentioned are some main types of annuity.

Fixed Annuity

A guaranteed income is earned on these type of annuities where the income is not affected by changes in interest rates and market fluctuations; thus these are the safest type of annuities. The following are different types of fixed annuities.

Immediate Annuity

The investor receives payments soon after making the initial investment.

Deferred Annuity

This accumulates money for a pre-determined time period before starting to make payments.

Multi Year Guarantee Annuities (MYGAS)

This pays a fixed interest rate each year for a certain period of time.

Variable Annuity

The amount of income varies in this type of annuities since they give the opportunity for investors to generate higher rates of return by investing in equity or bond subaccounts. Income will vary based on the performance of the subaccount values. This is ideal for investors who wish to benefit from higher returns, but at the same time, they should be prepared to endure the probable risks. Variable annuities have higher fees due to the associated risk.

Since the terms of various annuities are different from one another, the payments for some annuities end at the death of the annuitant while others continue to make payments to a designated beneficiary.

What is Life Insurance?

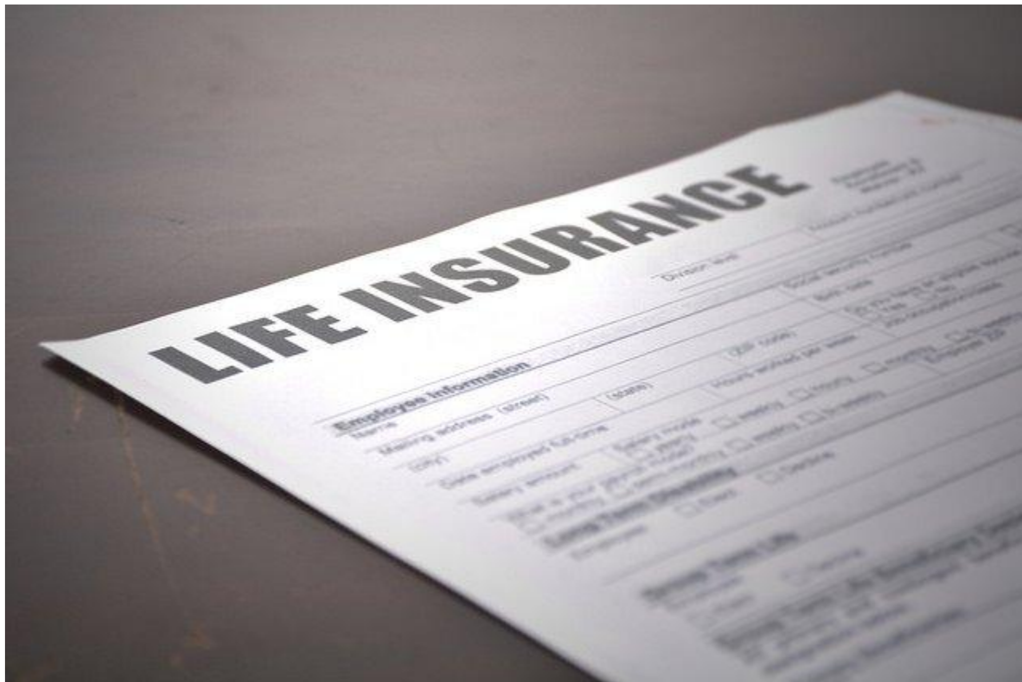
Life insurance, also referred to as **life assurance**, is a contract between an insurer (party that sells the insurance) and the insured (person covered by the insurance) where the insured is obliged to pay insurance premium in return for compensation by the insurer for a specific loss, illness (terminal or critical) or death of the insured. The contract terms will require the insured to pay the premium in periodic installments or as a lump sum.

In an insurance contract, the insurer is often the policy owner i.e. the person who is responsible for making insurance premium; however, these can be two individuals as well. One person can take out an insurance policy on behalf of another. At the event of the death of the policy owner, the designated beneficiary will receive the funds of the policy. The designated beneficiary is specified by the policy owner at the time of taking out the insurance.

E.g. Ian and Jessica are husband and wife. If Ian applies for an insurance policy and makes the insurance payments, then he is both the policy owner and the insured. If he takes an insurance policy on Jessica's life, she is the insured and Ian is the policy owner. The policy owner is the guarantor and he or she will be the person to pay the insurance premium.

The insurance premiums are calculated by the insurance company considering the adequate level of funds to cover claims, cover administrative costs, and make a profit. The cost of insurance is calculated by actuaries (experts in risk estimation and assessment employed in the insurance business). Actuaries consider the below factors in calculating the cost of the insurance.

- Personal and family medical history
- Driving record
- Height and weight matrix, known as BMI



What is the difference between Annuity and Life Insurance?

Annuity vs Life Insurance	
Annuity is a means of retirement plan where an individual keeps aside a lump sum of money to be used in retirement.	Life insurance is a contract between an insurer and the insured where the insured is obliged to pay an insurance premium in return for compensation for specific loss, illness or death of the insured.
Purpose	
The purpose of an annuity is to accumulate money in a tax-deferred product to use in retirement.	The purpose of life insurance is to provide income for dependents.
Initial Investment	
An individual requires a significant initial investment to invest in an annuity.	Since insurance premiums can be made on a periodic basis, a significant initial investment is not required for life insurance.

Summary - Annuity vs Life Insurance

The difference between annuity and life insurance primarily depends on the objective of the individual taking either policy. Investing in an annuity is usually done by a person closer to retirement in order to receive a guaranteed income during retirement. Taking out a life insurance policy mainly relates to being prepared for unforeseen and unfortunate circumstances such as critical illness and death where the policy owner wishes to provide financial protection for loved ones.

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