Annuities essay

Business

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An annuity consists of a series of equal payments over a specified period of time (Smith, Skousen, Stice, & Stice, 1998). An annuity is a sequence of equal periodic payments made at equal time intervals for purposes of paying a loan or creating a fund. Interest payments on bonds, premiums on insurance, payments on installment purchases, and payments of rent are examples of annuity. The payment intervals for the payment of annuity may be of any length, but the most commonly used are the annual, semi-annual, quarterly, and monthly payment intervals.

Simple annuity is an annuity whose payment interval is the same as the interest period. There are annuities that are fixed, meaning that the term starts and ends on definite dates. Monthly payment on installment purchases are called annuity certain since the payment starts on a definite date and continue regularly until the last payment. There are three types of simple annuity namely: ordinary annuity, annuity due, and deferred annuity.

Ordinary annuity is one whose periodic payments are paid at the end of each payment interval. The first payment in ordinary annuity is made at the end of the first period. Annuity due, on the other hand is an annuity whose payments are due at the beginning of each payment period. The first payment is due immediately at the beginning of the first period. Lastly, deferred annuity’s first payment is deferred or postponed, and is to start at some future date.

Contingent annuity is one whose term depends on some uncertain events. Many life insurance policies are examples of contingent annuity. The earnings of life insurance policies frequently fund annuities. Policy holders of insurance or social security may be paid from the funds that were

established for their benefit on the deaths or other claims of other policy owners.

Reference

Smith, J., Skousen, K. F., Stice, E., & Stice, J. (1998). Annuity. Intermediate accounting (p 248). South Western