ANNUITIES

EVERYTHING YOU WANTED TO KNOW AND WERE AFRAID TO ASK

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ANNUITIES IN GENERAL

- DEFINITION: A SERIES OF PAYMENTS OVER A PERIOD OF TIME…
- IMMEDIATE ANNUITIES
- DEFERRED ANNUITIES

IMMEDIATE ANNUITES

- FUNDS PAID TO CARRIER, PAYMENTS TO START ON SPECIFIC DATE – USUALLY WITHIN ONE YEAR OF DATE OF PURCHASE.
- PAYMENTS CAN BE ANNUAL, SEMI-ANNUAL, QUARTERLY, OR MONTHLY.

TYPES OF PAYOUT AND VARIATIONS ON THE THEME

- AN ANNUITY CAN BE PERIOD CERTAIN, LIFE, LIFE AND A PERIOD CERTAIN.
- MAY BE ON MORE THAN ONE LIFE
- NEED NOT BE ON ANY LIFE (PERIOD CERTAIN)
- PAYMENTS CAN BE:
  - LEVEL
  - VARIABLE
  - FIXED WITH COST OF LIVING ADJUSTMENT

CHARITABLE GIFT ANNUITES

- AN ANNUITY THAT CAN ONLY BE PAID OUT
  - BY A CHARITY
  - FOR A LIFE ANNUITY (OR JOINT LIFE)
  - A PORTION OF EACH PAYMENT IS TAX FREE
  - A TAX DEDUCTION IS GENERATED ON PURCHASE

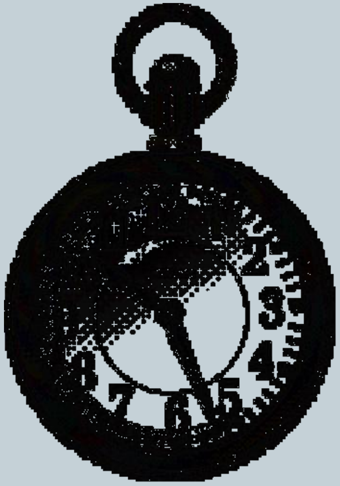
"I'll bet Baptist Hospital Foundation didn't plan on this party when they set up my charitable gift annuity."

DEFERRED ANNUITIES

Types:

- **FIXED GUARENTEED**
- **VARIABLE**
- **INDEXED**

RELATIVE SAFETY OF EACH



INDEXED ANNUITIES

VERY HIGH CARRIER RISK, AS THE ACTUAL ASSETS ARE NOT ALLOCTED OR SEGREGATED, BUT BASED ON A STATED VALUE WEIGHED AGAINST AN INDEX. THE ACTUAL ASSETS ARE IN THE CARRIERS RESTRICTED FUNDS, AND MAY OR MAY NOT ACTUALLY PERFORM TO THE STANDARDS OF THE INDEX. A VERY HIGH COST PRODUCT, AS IT CONTAINS CARRIER GUARENTEES ON MINIMUMS, WITH 'PREMIUMS' LEVIED AGAINST INDEX LEVELS TO PROTECT THE CARRIER. USUALLY HIGHLY RESTRICTIVE ON WITHDRAWALS, AND VERY DATE SPECIFIC ON GUANTEES AND VALUES AT WITHDRAWAL.

VARIABLE ANNUITIES

DEFERRED VARIABLE ANNUITIES ARE THE MOST INTERESTING, AS THEY ALLOW THE PURCHASOR TO DETERMINE WHERE THE MONEY IS INVESTED, AND VALUES ARE CALCULATED ON THE UNDERLYING ASSETS OF THE FUNDS INVESTED. THE RISK IS ALMOST TOTALLY AN INVESTMENT RISK, BASED ON THE FUNDS SELECTED.

COST FACTORS

- SURRENDER CHARGES
- INVESTMENT MANAGEMENT CHARGES
- ANNUITY ‘WRAPPER’ CHARGES
- ENHANCED DEATH BENEFIT CHARGES
- POLICY FEES
- INDEX CAPS

“Obey my commands, protect yourself at all times and think about investing your purse in tax-free annuities. Here’s my card.”

TAXATION OF DEFERRED ANNUITIES DURING DEFERRAL PERIOD

- NO TAX DURING ACCUMULATION
- ON DISTRIBUTION OF FUNDS TO THE ANNUITANT, OTHER THAN AS AN ANNUITY PAYOUT, (LUMP SUM DITHDRAWAL, PERIODIC DISTRIBUTIONS, ETC.) THE CALCULATION IS 'LAST IN FIRST OUT', WHICH MEANS ANY GAIN IS RECEIVED BEFORE INVESTED PRINCIPAL, AND IS SUBJECT OT ORDINARY INCOME TAXES.
- A PENALTY TAX IS LEVIED ON WITHDRAWAL PRIOR TO AGE 59 ½ FOR DISTRIBUTIONS NOT MEETING ANNUITY RULES.
- A TRANSFER OF OWNERSHIP IS CONSIDERED A DISTRIBUTION FOR TAX PURPOSES.
- THE ANNUITY IS TOTALLY INCLUDABLE IN THE ESTATE, BUT THERE IS NO STEP UP FOR THE BENEFICIARY, HENCE THE ORDINARY INCOME TAX ON THE GAIN IS PRESSERVED FOR THE GOVERNMENT!

TAXATION OF IMMEDIATE ANNUITES

- EACH PAYMENT TO THE ANNUITANT REPRESENTS 'RETURN OF PRINCIPAL' AND 'INTEREST' EARNINGS.
- RETURN OF PRINCIPAL IS TAX FREE (OTHER THAN PRINCIPAL FROM IRA OR QUALIFIED PLAN)
- INTEREST IS TAXABLE AS ORDINARY INCOME, NOT CAPITAL GAIN
- IF THE ANNUITANT LIVES LONG ENOUGH, THE PAYMENTS CAN BECOME FULLY TAXABLE, AS IT IS ASSUMED THE INTIAL PRICIPAL HAS BEEN PAID OUT.
- IF THE PAYMENTS CONTINUE AFTER THE DEATH OF THE ANNUITANT (PERIOD CERTAIN ANNUITES), THE PRESENT VALUE OF THE FUTURE PAYMENTS IS IRD, AND SUBJECT TO ALL THE ESTATE AND INCOME TAX RAMIFICATIONS OF IRD.

WHAT MAKES ANNUITES GOOD?

- CREDITOR PROTECTED IN STATE OF FLORIDA
- TAX DEFERRAL ON GROWTH, THEREFORE GROSS AND NET COMPOUNDING RATES EQUAL.
- A VARIABLE ANNUITY ALLOWS ACCESS TO MUTIPLE INVESTMENT OPTIONS AT A RESONABLE COST.
- NO WAY TO OUTLIVE 'LIFETIME INCOME'!
- THE ULTIMATE IN INCOME SECURITY.
- MOST HAVE MINIMUM DEATH BENEFIT GUARENTEES, SO IF THE ANNUITANT HAS THE BAD LUCK OF DYING IN A DOWN MARKET, THE INVESTED PRICIPAL IS PAID TO THE BENEFIARY, AS A MINIMUM.

WHAT MAKES ANNUITIES BAD?

- RELATIVELY HIGH COST INVESTMENTS – GENERALLY 1.3% TO 2.9% TOTAL ANNUAL COST OF OWNING. (OTHER THAN FIXED ANNUITIES.)
- FIXED ANNUITY RATES MAY NOT OUTPERFORM INFLATION!
- SURRENDER CHARGES CAN BE HIGH
- EARLY WITHDRAWALS MAY BE SUBECT TO IRS PENALTY AS WELL AS SURRENDER CHARES!
- ORDINARY INCOME INSTEAD OF CAPITAL GAIN TREATMENT.
- ESTATE INCLUSION, YET TRANSFER AT BASIS.

ANNUITIES IN QUALIFIED PLANS AND IRA'S

- THERE ARE NO 'ALWAYS' OR 'NEVERS'.
- A SHELTER WITHIN A SHELTER.
- REDUNDANT CREDITOR PROTECTION.
- AN EASY WAY TO ACCESS MANY INVESTMENT COMPANIES WITH SMALL AMOUNTS OF MONEY.
- NO NEED TO SELL AND BUY FOR INCOME AT RETIREMENT.

WHAT ABOUT PAYOUT?

- SELECTING A VARIABLE PAYOUT, ACADEMICALLY, IS THE BEST BET. THE PAYMENTS INCREASE WITH MARKET INCREASES – BUT THEY CAN GO DOWN!
- JOINT AND SURVIVOR GUARENTEES THAT NEITHER THE JOINT ANNUITANTS CAN OUTLIVE INCOME!
- FIXED INCOME WITH COST OF LIVING INCREASE IS THE COMPROMISE – SOME COSTS INVOLVED, BUT A GUARENTEE OF INCREASED INCOME, TO SOME EXTENT, IN TIMES OF INFLATION.
- IF ITS LIFE ONLY, OR JOINT AND SURVIVOR, AND THE SURVIVOR IS A SPOUSE, YOU ARE PRETTY MUCH GUARENTEED OF NO ESTATE TAXES – EVER, ON THE FUNDS!

ANNUITY ESTATE PLANNING

- ANNUITIZING GUARANTEES THE HIGHT LEVELS OF INCOME.
- THE INCREASED INCOME CAN BE USED:
  - TO LIVE ON
  - TO GIFT TO AN IRREVOCABLE TRUST.

THE TRUST CAN PURCHASE LIFE INSURANCE TO REPLACE THE ASSETS USED TO PURCHASE THE ANNUITY, AND TRANSFER THOSE ASSETS TAX FREE.

Trivia and other details

- FIFO for annuities issued before Aug 1982
- No tax on gain for transfers of annuities issued before April 1987.
- 1035 exchanges are possible – for annuities.
- Gifts of annuities – gain is taxable (if issued after 1987.
- Non natural person owned annuities lose tax deferral advantage.
- Annuities gifted to charity: The full value is a gift, income tax must be paid by the donor on the 'gain' – if the gift is a 'qualified' annuity, first the tax, then the gift. (Exception, over 70 ½, direct from IRA, up to $100,000.00 – and possibly expiring!)

After tax income comparison

- Assumptions: $250,000 of ‘CD’s’
- 28% tax bracket.
- Age 65 – life and ten year certain – ‘no named’ carrier, but competitive and in the business.
- CD paying 4% (we won’t talk about renewal..)
- Net income from CD = $7,200 per year
- Net income from annuity = $16,156.23, for first 20 years, then $12,808.11.
- Burning, searing question: Can you replace the asset with the difference in income? Do you want to?

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