



Annuity Maximization

Annuity Max is an estate planning technique for transferring the value in a deferred annuity into a more transfer tax efficient arrangement using an ILIT and life insurance policy.

The appropriate Annuity Max prospect is a client with a large deferred annuity that will not be needed to support his/her/their retirement.

Taxation:

- Annuities owned at death are subject to estate inclusion thus increasing any estate taxes owed.
- Annuities do not receive a “stepped up basis” at death
- Amounts received by the decedent’s beneficiary are taxable as ordinary income (income in respect of a decedent) - the same as if the decedent had received the distribution

The Process

1. Client establishes an irrevocable life insurance trust (ILIT) that is owner and beneficiary of a life insurance policy insuring client(s)
2. Client takes distributions from annuity.
3. Distributions may be subject to surrender charges and may be subject to a 10% penalty unless an exception exists
Exceptions include (IRC § 72(q):
 - a. Client is age 59 ½ or older
 - b. Client is disabled
 - c. Distribution is part of a series of substantially equal periodic payments
4. Client pays income tax on annuity distribution received
5. Client gifts remaining distribution to ILIT
6. ILIT Trustee sends out Crummey notices to make the gifts a “present interest”, allowing client to use annual exclusions
7. Trustee pays premiums on life insurance policy (Consider using a “No-Lapse Guarantee” product or rider to guarantee Death Benefit)
8. At client’s/insured’s death, Trustee collects life insurance policy proceeds that are free from income and estate taxes

Advantages

- Unneeded annuity’s value is more transfer-tax efficiently transferred to the next generation (or subsequent generations)
- Reduces (or eliminates if a life only annuity) estate and income taxes associated with owning an annuity at death and subsequent distributions from that annuity
- Can provide for an orderly distribution or retention of ILIT assets

Bottom line

Annuity Max can be an effective way for your client to minimize estate and income taxes associated with owning an unneeded annuity, and maximize the amount of wealth transferred to subsequent generations.

The preceding summary is intended to be a general discussion of the topic presented, and is based on our current understanding of applicable tax laws, regulations and rulings. In actual practice, the transaction discussed may be more complex and will require the attention and expertise of professional advisors. In no way should this summary be construed to constitute tax or legal advice. **For agent use only.**