Life

Using life insurance for annuity maximization

Help your clients make the most of their annuity

Marketing guide

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Maximize your client's annuity funds by using life insurance

Even the best financial plans can run into unforeseen problems with taxation that could leave your client's heirs with less than planned. By using life insurance to maximize annuity funds, you can help provide your clients with the most value for them, without the limitations of income or estate taxes.[1]

Who Can Benefit?

Many of your clients have used annuities as a savings vehicle. Some of your clients may no longer need the money in the annuity for themselves. Instead, they plan to pass the money on to their heirs.

But did you know that the gains on your client's annuity (the portion that exceeds the original investment)[2] could be taxable income to heirs? In addition, the full value of the annuity is includible in your client's taxable estate, which could result in a diminished inheritance. This results in your client's heirs receiving a portion of the intended amount.

To maximize your client's annuity dollars, one strategy is to purchase a life insurance policy with the annuity funds. The beneficiaries of the policy would receive a generally tax-free death benefit.

Why Life Insurance?

Life insurance provides a generally income tax-free death benefit and can be structured to be excluded from the owner's taxable estate. Using annuity funds to buy a life insurance policy can maximize the value for your client's heirs.

How Does It Work?

There are two common ways to use the annuity maximization strategy.

1. Single premium

- Surrender the annuity and use the lump sum to purchase a paid up, guaranteed universal life insurance policy on your client's life.[3]
- Leverage lump sum dollars into the largest guaranteed death benefit for beneficiaries.[4]

2. Spread out premium payments

- Annuitize or 1035 exchange the annuity into a Single Premium Immediate Annuity (SPIA).[5]
- Use the income stream to fund a life insurance policy.
- Your client retains access to potential cash value accumulation, if needed.
- Beneficiaries receive the life insurance death benefit proceeds, generally tax-free.

Both options present different advantages and disadvantages—depending on your client's goals. The risks, benefits, and cost of surrender from an annuity and the need for life insurance must be considered prior to making a decision. Talk to your client today about this strategy to maximize annuity funds for heirs.

Life insurance considerations

There are also some important considerations that should be covered with your clients to determine if life insurance fits their needs. These considerations include:

- **Cost of insurance charges (COIs) or other charges:** Life insurance comes with charges that your clients need to be aware of for planning purposes.
- **Maintaining the death benefit:** Additional premiums may be necessary to continue the desired death benefit, depending on funding.
- **Modified Endowment Contracts (MECs):** MECs may have tax implications that your clients need to know about when considering their options.[6]
- **Loss of premium.** Depending on funding, life insurance may not guarantee avoiding loss of premium.
- **Surrender charges:** Withdrawals may be subject to surrender charges and the amount available for policy loans.[7]

Be sure to conduct a thorough needs-based analysis and determine the need for death benefit coverage in order to help your clients make an appropriate decision. Review illustrations thoroughly for guaranteed and non-guaranteed death benefit values and the amount available for policy loans.

Offer your clients financial protection and help to grow their legacy for future generations.

Talk to your MGA for more details!

1. This material does not constitute tax, legal or accounting advice, and neither North American nor any of its agents or employees give such advice. It is not intended and cannot be used for the purpose of avoiding any tax laws or IRS penalties. Any of your clients interested in these transactions or topics should seek advice from his or her own attorney, tax advisor and/or accountant based on his or her own particular circumstances.
2. If the original investment was pre-tax, then the full value of the annuity will be taxable income to heirs.
3. Removing funds from an annuity may result in surrender charges and/or income taxes.
4. Guaranteed death benefits are subject to premium payment requirements.
5. Using a SPIA to fund the life insurance policy is not the only option and may not be the best option for the client. Please make sure to review and consider the current payout factors before making any decisions.
6. For most policies, withdrawals are free from federal income tax to the extent of the investment in the contract, and policy loans are also tax-free so long as the policy does not terminate before the death of the insured. However, if the policy is a Modified Endowment Contract (MEC), a withdrawal or policy loan may be taxable upon receipt. Further, unpaid loan interest on a MEC may be taxable. A MEC is a contract received in exchange for a MEC or for which premiums paid during a seven-year testing period exceed prescribed premium limits (7-pay premiums).
7. In some situations, loans and withdrawals may be subject to federal taxes. North American Company for Life and Health Insurance does not give tax or legal advice. Clients should be instructed to consult with and rely on their own tax advisor or attorney for advice on their specific situation. Income and growth on accumulated cash values is generally taxable only upon withdrawal. Adverse tax consequences may result if withdrawals exceed premiums paid into the policy. Withdrawals or surrenders made during a Surrender Charge period will be subject to surrender charges and may reduce the ultimate death benefit and cash value. Surrender charges vary by product, issue age, sex, underwriting class, and policy year.

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