

Part IX

Annuities and Retirement Planning

There are many good retirement plans available to the investor, but annuities offer a big advantage—a whole new dimension to retirement assets—that one should consider, no matter how much money he has already put away otherwise for his retirement. Annuities have no annual contribution limits.

While there are tax laws that control how much one can put each year into a 401(k), IRA, and almost every other retirement plan, one can put as much into an annuity as he likes. Money that is put into a 401(k) is salary deferred; so taxes are deferred. IRA contributions, depending on one's eligibility, may also be tax-deductible and all the earnings or gains are tax-deferred.

The money that one puts in an annuity earns interest that accumulates tax-deferred until he begins to make withdrawals or begins to receive his regularly scheduled payments. Annuity payments are composed of two parts: the interest on the money one has invested, plus a return of the money that was invested originally. The return of principal is not taxed.

As in any investment that is tax-deferred, money invested in an annuity grows rapidly for three reasons:

- The original investment earns interest
- That interest earns interest, since it is automatically compounded
- The money one would ordinarily pay out for taxes remains invested—earning interest.

An annuity is an investment one makes through an insurance company. It represents a contractual relationship between an individual and the company. Although annuities are offered only by the insurance industry, they do not have anything to do with life insurance or any other type of insurance coverage. Annuities are marketed and sold through brokerage firms, insurance agencies, banks, savings and loan institutions, financial planners, and investment advisors. When an individual purchases or invests in an annuity, the insurance company gives him certain assurances. The guarantees depend upon the type of annuity.

There are two different types of annuities :

- Fixed Annuities
- Variable Annuities

The fixed annuity has a set rate of return and the variable annuity allows the investor chooses from a series of portfolios that range from conservative to aggressive.

Annuities purchased from an insurance company are called “commercial annuities” while those purchased from a party who is not in the business of selling annuities are called “private annuities.” Technically, the living proceeds received from a life insurance contract are also considered annuities if they consist of payment of both principal and interest. A life annuity promises that as long as the annuitant lives payments will be continued. In other words, the income stream can never be outlived. Life annuities are priced based on the expected mortality experience of a large group of annuitants.

Annuities can be distinguished from life insurance policies by virtue of their different purposes. Life insurance has often been described as protection against dying too soon, while an annuity is considered protection against living too long. Although these descriptions have become a cliché in the insurance business, they are apt. Life insurance protects the insured’s survivors against financial problems that arise when the insured dies before accomplishing financial security goals. An annuity, on the other hand, protects the person receiving annuity funds -- the annuitant -- against financial problems that arise from living beyond the earning years that pay for everyday living expenses.

Types of Annuities

Fixed Annuities

Much like CD's, fixed annuities give one a fixed interest rate for a fixed time period -- usually 1-10 years thus guaranteeing a fixed rate of interest for the life of the contract. If the insurer guarantees the rate for one year, he announces the fixed return for the year ahead at the end of each year. The rate depends on the insurer’s current investment portfolio. The major advantage of a fixed annuity is security. Even if one makes a withdrawal from time to time, the balance remaining in the annuity will continue to earn the fixed rate that was guaranteed.

A fixed annuity guarantees a fixed rate of interest for the life of the contract. The major advantage of a fixed annuity is security. Some fixed annuities offer a fixed rate of interest for a specified period of time. Even if one makes a withdrawal from time to time, the balance remaining in the annuity will continue to earn the fixed rate that was guaranteed.

Fixed-Immediate

The investor puts in a fixed sum of money, and the annuity begins paying him income immediately, or no later than twelve months after the annuity was bought. People who buy immediate annuities are usually trying to supplement their retirement income, and have found the income being paid by the annuity appealing because it can be used primarily as a systematic liquidation of principal and interest over their lifetimes, no matter how long they live.

Variable Annuities

A variable annuity allows one to direct his investment among several types of investment funds while enjoying the tax-deferred benefits of the annuity product. The return fluctuates with the stock, bond, and money markets. Variable annuities, have additional insurance-related expenses, may be subject to surrender charges, and are generally a longer term investment than a mutual fund. With variable annuities, one bears the investment risk.

Variable annuities appeal to the investor who wants the opportunity for the higher returns that may come from assuming higher risks. The insurance company offers as investment options a diversified portfolio of securities—for example, stocks, bonds, or other securities.

Deferred Annuities

They accumulate their earnings tax-deferred. Most deferred annuities allows the investor to withdraw once a year free of a company charge—up to 10% of the total value of his annuity. For amounts over 10% withdrawn in a single year, the insurance company may impose a charge. When the money is taken out, the tax laws require that the earnings, which are taxable, be withdrawn first. The excess in the withdrawal would be a return of one's investments, and so would not be taxed. Deferred annuities come in three flavors: fixed, variable, and modified guarantee.

A Modified Guarantee Annuity

This annuity is similar to a fixed annuity with one major difference. Usually, if funds are left to the end of each guarantee period one chooses, the principal and interest are guaranteed. However, if funds are withdrawn prior to the end of the guarantee period, a market value adjustment may happen. If prevailing interest rates have increased since the commencement of the guarantee period, the adjustment will be negative. Conversely, if the rates have gone down, the adjustment will be positive. This kind of annuity generally offers more guarantee period interest rate choices (one to ten years) and thus a set of varying interest rates, both short and long term. Because of this “market value adjustment” feature, interest rates will generally be somewhat higher than in a conventional fixed annuity.

Single Premium Fixed Annuity

The Single Premium Fixed Annuity offers a tax-deferred growth where the money accumulates without taxation and may grow faster than in a comparable, currently taxed investment.

- It offers competitive, banded interest rates - one can earn a base interest rate that historically has been higher than average one-year CD rates.
- It gives 1% first-year additional interest rate and generous access to money.
- Withdrawals prior to age 59 ½ may be subject to a 10% IRS penalty.
- The owner has control over finances because he decides when to receive the money and pay taxes on the earnings.
- It offers a guaranteed death benefit without the costs and delays of probate, if payable to the beneficiary.

The SPFA gives the opportunity to generate a guaranteed lifetime income. The initial interest rate will be determined by the amount of premium payment and when the insurer receives it.

Interest Rates

During the first year one will receive an extra 1% over the current base interest rate. (This 1% first-year additional interest rate only applies to policies with a one-year initial interest rate guarantee period issued to individuals prior to age 86.) One can choose either a one-year or three-year initial interest rate guarantee period. After the initial interest rate guarantee period, the policy will receive a new interest rate on each subsequent policy anniversary, and that rate is guaranteed for one year. Money will earn the rate according to amount that the insurer is crediting for premium payments on the date we receive payment.

Principal Guarantee

The principal is guaranteed because upon full surrender of the policy within the first three years, the insurer guarantees that the contract owner will receive an amount equal to at least the premium paid. However, the principal guarantee does not apply if one makes any partial withdrawals. Withdrawals give the contract owner immediate access to the money. There is no limit to the number of withdrawals made each year. Withdrawals may generate a tax liability on amounts not previously taxed and that withdrawals prior to age 59½ may be subject to a 10% IRS penalty.) All withdrawal requests must be for at least \$100. The cash value may not fall below \$2,000 due to a partial withdrawal.

Periodic Partial Withdrawals (PPW)

An individual may decide that he or she wants to receive payments from a policy on a regular basis (monthly, quarterly, semi-annually, or annually). With a Single Premium Fixed Annuity, the contract owner can choose to receive scheduled payments of the interest earned according to the 10% Window, or any other specified amount, but each payment must be at least \$100. The 10% Window allows the individual to make withdrawals from the policy during the surrender charge period and avoid surrender charges.

During the first six years of the policy, up to 10% of the policy's cash value on the preceding anniversary may be withdrawn each year without incurring any surrender charges. At any time during the policy year, the 10% Window equals 10% of the policy's cash value on the preceding policy anniversary less any prior surrender charge-free withdrawals taken during that policy year. After six years, the full cash value is available at any time without any surrender charges. If the payment is \$100,000 or more, the contract owner may withdraw (without incurring surrender charges) the greater of the gain in the policy, known as the Gain Window, or the 10% Window. The Gain Window is the portion of the accumulation value, as of the previous anniversary, that exceeds the payment made to the policy.

Single Premium Immediate Annuity (SPIA)

People are living longer and longer these days, but they haven't always made sure that they have the financial resources for an extended lifetime. SPIA is a product that can take away these worries. SPIA gives more security than a typical savings account, which one can continuously draw upon, hoping it will last a entire lifetime. SPIA does not have an account value one can access, but the income received from the insurance company is guaranteed never to run out. That's something a savings account cannot offer. And SPIA also offers alternatives that can provide a lifetime income for both the contract owner and his or her spouse or provide income to loved one's if the contract owner dies prematurely. The SPIA income is a fixed amount of money based on the age, the gender, the amount of premium payment, and the frequency with which one receives income payments: monthly, quarterly, semi-annually, or annually.

If one dies prematurely, the total accumulation value of the policy is paid directly to the named beneficiary(ies), avoiding the costs and delays of probate. These funds could provide much-needed comfort to beneficiaries during a stressful time, when other monies may be unavailable to them. If a spouse is the primary beneficiary, he or she even has the option of becoming the new owner of the annuity, and continuing to build money, tax-deferred.

In addition to providing a guaranteed lifetime income, SPIA can also take away some of the worry about managing money. Unlike income from stocks and bonds, the SPIA payments will not be affected by market swings.

Tax-Qualified Money

If one has money tucked away in tax-qualified plans, such as an IRA or 401(k) plan, that money will become taxable once it is received. Not only could that extra money throw an individual into a higher tax bracket, it could even be subjected to 85% of Social Security benefits for taxation. Furthermore, if one places tax-qualified money in SPIA, he or she might not have to worry about how to satisfy the Internal Revenue Services' Required Minimum Distribution (RMD) requirements - because the SPIA could automatically satisfy them. This is important, because the IRS imposes severe penalties if these requirements are not met. An individual can receive the highest income for premium amount, gender, and age if he or she selects "life only" SPIA. It guarantees that the insurer will pay the policy owner regularly for the rest of his or her life. Upon death, payments will cease. Sometimes, income for one life is not enough. Many couples want to make sure that they have enough income to last for both of their lifetimes. If one selects a Joint & Survivor SPIA, he or she will receive payments for as long as either one is alive. This way, both policy owner and his or her spouse will be protected against outliving the savings amassed together. None of us like to think that if we were to die shortly after giving a lot of money to an insurance company, that money would be completely lost. An insurance company will generally offer alternatives to prevent this.

Guaranteed Period Certain SPIA

With this SPIA, can choose a minimum period of time during which he or she will receive payments: either 5, 10, 15, or 20 years from the date that an individual purchased his or her SPIA policy. If he or she dies before this guaranteed number of years has passed, the insured will continue sending payments to a chosen beneficiary(ies) for the duration of the guarantee period.

Guaranteed Total Amount SPIA

If the policy owner dies before the total money received equals the amount of the original premium payment, the insurer will continue to pay the chosen beneficiary(ies) until the total amount paid to an individual and his or her beneficiaries matches the initial premium. So everyone gets what they have paid in. These alternative SPIAs can also help ease the burden on beneficiaries if the policy owner dies before all of the guaranteed payments have been made. Payments go directly to the beneficiaries, unlike many other assets that may get tied up in probate. The SPIA payments could be helpful to beneficiaries at a very difficult time.

Single Premium Retirement Annuity (SPRA2)

This annuity helps save for retirement on a tax-deferred basis. If one is worried about saving enough for retirement, this product may help to realize retirement goals. Single Premium Retirement Annuity is a competitive deferred annuity designed to satisfy retirement needs. Even if an individual has not reached retirement, the time to begin shaping a financial future

is now. A deferred annuity could provide the money needed, down the road. A deferred annuity could provide a very good solution to many situations in an individual's life such as a savings alternative that can take care of financial needs and perhaps even provide a legacy for children or grandchildren.

- SPRA-2 allows money to grow tax-deferred at competitive interest rates.
- SPRA-2's liberal withdrawal provisions offers the flexibility to control financial situations.
- SPRA-2's allow an individual to use the money that has accumulated to generate a retirement income that he or she cannot outlive.

The Single Premium Retirement Annuity helps ensure that an individual will not outlive a retirement savings. With SPRA-2, one can get more mileage out of money that's currently sitting in a CD or other currently taxable investment. Or it can be used to consolidate several smaller IRAs. However, emergencies do arise, so SPRA-2 has a 10% "window" that allows someone to take up to 10% of money, each year, without any surrender charges. And after eight years, one can take out as much money as is needed, at any time, without any surrender charges.

Parties to the Annuity

The Insurer

The insurer is the one who is licensed to sell annuities and is the agreement between an individual and an insurance company. This person may be

- in a local bank
- a financial planner
- a brokerage firm

but it will always be an individual who is licensed to sell annuities. There are over 2,000 insurance companies in the United States; several hundred of these insurers deal in annuities. The insurance company that an individual chooses is also know as the insurer, and he or she will be the person investing the money. In addition to investing an individual's money, the company makes certain promises. These assurances and the Term of the agreement are contained in the annuity contract. The contract spells out what can and cannot be done. Items such as additional investing, withdrawals, cancellations, penalties, and guarantees are all defined in the contract.

The Contract Owner

Whether or not the annuity is purchased directly through the insurance company or through any of its authorized agents, the investment contract is always written between the investor and the insurance company. The **contract owner** is the person or the couple who invests in the annuity. A minor child can be the contract owner only if a guardian or custodian is prominently listed. Because the investor is the owner of the investment, he can gift the annuity contract to anyone or any entity at any time. It is their money, they decide among the different options offered. A contract owner has the right to add more money, make investment decisions and changes, withdraw all or a part of the investment, change the parties to the investment, and to terminate the agreement. The contract owner is similar to the purchaser of a mutual fund or bank CD. When an individual buys a mutual fund, he or she is the owner. This individual has the right to invest more money, liquidate the entire account, take some or all of the money out, and change the title of the account or its ownership. Since the contract owner controls the investment, he or she can gift or will part or all of the contract to anyone or any entity at any time.

The Annuitant

The **annuitant** is similar to the insured in an life insurance policy. The annuitant is the individual or entity that is named on the annuity contract and the annuity will remain in force until the contract owner makes any changes or the annuitant dies. The annuitant, unless it is the contract owner, has no say in or control of the annuity contract. The annuitant does not have the power to make withdrawals, deposits, change the names of the parties to the agreement, or terminate the contract. Just as when an individual purchases life insurance on someone else, the annuitant must also sign the annuity contract. The person that this individual names as the annuitant can be anyone: the annuitant, his or her spouse, parent, child, relative, friend, or neighbor. The only qualification is that the named annuitant is a person currently living who is under a certain age.

The maximum age of the proposed annuitant depends on the insurance company. Most companies require that the annuitant be under the age of 75 when the contract is initially signed. Other companies set a maximum age of 70 or 80. It is important to note that the contract may still stay in force after the annuitant reaches the maximum age. Most annuities allow the contract owner to change the annuitant at any time. The only stipulation is that the new annuitant must have been alive when the contract was originally set up.

The Beneficiary

The **beneficiary** is like a vice president of a country because he or she is of little value until the death of a certain individual. In the case of an annuity, the beneficiary is waiting for the death of the annuitant. And, like the beneficiary of a life insurance policy, the beneficiary of

an annuity has no voice in the control or management of the policy. The only way in which the beneficiary can prosper from an annuity is upon the death of the annuitant. The named beneficiary(s) can be

- children
- friends
- relatives
- spouses
- neighbors
- trusts
- corporations
- partnerships

There may be four parties involved in an annuity investment but there may not be four individuals. The same person can hold multiple titles. So one individual could be the contract owner and beneficiary or one individual could be the owner, annuitant, and beneficiary. In fact, any combination is acceptable. However, if the contract owner chooses an entity, the entity can only be the contract owner and or beneficiary, a living individual under a certain age but not a couple must be named as the annuitant. The insurer is always an insurance company and in order to change the insurers he or she must change insurance companies.

Mechanics of Annuities

Pay-Out Options

Immediate – Pay

Under this purchase method, the investor gives the insurance company one single lump sum payment. And usually, in about 30 days the insurance company will begin monthly payments. A person who is still working and not near retirement (10 - 40 years away) would ordinarily not choose this method. This would be an alternative for someone who has a large lump sum of money and is at or near retirement and wishes to begin payout immediately.

Single Payment Deferred

This method of purchasing an annuity is 'Single Payment Deferred'. With this type of payment option the investor puts a lump sum into an annuity. The payment begins years later when the annuitant begins his payout. For example, a 30 year old decides to put \$20,000 into an annuity. He wants the payout to begin when he is 65 years old. For the next 35 years the \$20,000 he put into the annuity builds up earnings. With this payment option, the payout is deferred. And the money that is put into it originally accumulates earnings for

the deferral period. This is a good way to begin retirement planning if an individual has a fair amount of money that he or she does not need for immediate use.

Periodic Payment Deferred

The third payment option is the 'Periodic Payment Deferred Annuity'. With this type of payment option, the investor puts a specified amount money into his annuity account periodically over a period of years. However, it is possible to vary the periodic payment amount. Each time the investor puts money into the account the insurance company keeps track of the principal and interest. This method is also a good way to defer paying taxes on earnings. As with all annuities, the tax is deferred on earnings until the payout begins. And what makes this even better is that if one can choose a form of monthly payout, by only paying taxes on the annual payout. At retirement, most people are in a lower tax bracket.

Accumulation Units

The insurance company uses an accounting method called Accumulation Units. A mutual fund, uses Net Asset Value per share to account for its investments. A variable annuity also uses Net Asset Value. Each evening at 4 p.m. eastern time when the New York Stock Exchange closes, the separate account portfolio is valued and divided by the total number of accumulation units. This works very similar to a mutual fund valuation. Annuity purchases placed prior to 4 p.m. eastern time are credited to the individual as of that day. And annuity purchases placed after 4 p.m. eastern time are credited to the individual as of 4 p.m. eastern time the following day.

When the contract owner retires and begins monthly payouts, the insurance company is going to go through a process called annuitizing. On that day, the insurance company will convert the account into a fixed number of annuity units. Regardless of what happens in the future, the amount of annuity units will remain the same for the rest of the annuitant's life. With a variable annuity, what will change is the value of each annuity unit. So what is important at this point is not the amount of annuity units, but rather the value of each annuity unit. The value of each annuity unit will fluctuate. And it is the value of each annuity unit which determines how much will be received each month in the monthly payout. To figure out exactly how much is in an annuity after payout begins, the contract owner can multiply the annuity units by the net asset value. Also, some annuity contracts call for the annuity payout to be changed monthly, some call for quarterly changes, some call for semi-annual changes, some call for annual changes. Payout will come in the form of annuity units.

Surrender Charges

The actual length of the surrender charges are vital in planning out the time frame in which one may desire to start receiving his benefits without penalties. An individual whose age is presently 55, and who would like to retire and start collecting the annuity benefits at 62, would maximize earnings and at the same time avoid any penalties by selecting a 7 year annuity. However, if this same individual purchased an annuity that had a 12 year surrender period, he would incur a significant surrender charge.

Variable Annuities

All variable annuities have certain predetermined investment objectives, as well as various restrictions set by the portfolio managers. As an investor, one has the choice of which annuity portfolio, out of over 1,500 available annuities, to invest in, and based on the requirements, how much money to invest. Investors are always looking for the optimum results for their investments as the future of their families' financial well being is at stake. In order to choose the proper investment vehicle and annuity to invest in, the individual investor must analyze the marketplace based on, but not limited to the following:

- Existing portfolio
- Investment time line
- Family and individual goals
- Tax bracket
- Level of acceptable risk

A variable annuity is an investment company, or other official entity, that analyzes and makes investments on behalf of individuals and organizations who have selected specific areas and goals to invest in. The annuity will pool together money received by all the investors to invest in a particular portfolio or subaccount. Investments can be as little as \$10 or as high as \$10,000, all depending on the specific requirements of each portfolio subaccount. The portfolio managers selected to oversee the funds use the money that has been pooled from the investors to purchase various investments such as stocks, bonds, and commodities that, in their opinion, will help the investors meet their individual and collective financial objectives. No matter what the level of investment held by an investor in an annuity, all investors will receive the same percentage yield or return from the subaccount.

The investment strategies and objectives of each individual portfolio and as illustrated and explained in each individual prospectus creates the philosophy in which investments are made. The fund manager uses it to steer his investments in the right direction, and the

investor utilizes it to choose the right vehicle for his investments and personal financial goals. The prospectus will also give detailed information on the specific funds restrictions as well as all costs and expenses connected to the investment.

When a fund earns money, the dividends are reinvested in the fund for the account of the investor unless otherwise requested, and is reflected as an increased value per unit. Variable annuities have become a very popular investment vehicle as they give any individual the opportunity to access a diverse element of investment opportunities. Annuity investments also allow an individual to invest in foreign-based stock and bond markets as the ease of investing in international annuities allows easy entry into the varied international markets.

A variable annuity fund is owned by all of the investors who purchased units in the fund. The annuity's day to day operation is overseen by a management company, who is often an outside mutual fund group and who may offer other financial products and services as well as insurance. The manager of the fund is paid an average of 0.75% for their services and decides where to invest the funds assets. The fund managers make all of their investment decisions based on comprehensive and continual research into the operational and financial performance of select companies within their sphere of interest. On the basis of the information gathered, the fund managers decide what companies to buy, when to buy them, when to sell, and which investments to hold for long term equity. The variable annuity company may also employ an outside underwriter who will package and offer units of a particular fund to the general public.

Investing In A Variable Annuity

The investment in a variable annuity is defined by the purchase of units or shares in one or more subaccounts of a particular investment annuity. By virtue of the size of the investment, a contract owner will become the owner of a set number of units in the annuity chosen. The actual price of the units in any given subaccount is directly related to the value of the securities held by that specific investment account.

Because of the higher costs associated with annuities, one should first invest as much as he can in regular retirement plans, such as the 401(k), IRA, and Keogh. If he still has money to put away on a tax-sheltered basis, he can start thinking about a variable annuity. Obviously, he wouldn't want to hold a variable annuity in an IRA account, just as he wouldn't want a tax-exempt bond fund put into an IRA. This would be placing one tax shelter into another which would be a major mistake.

The outstanding advantage is higher long term return on average. Since the end of World War II, equity based investments have outperformed debt based investments (bonds) for

long term investors. Assuming this historical data holds true into the future, a variable annuity held for a number of years can outperform a conventional deferred annuity, on average. The negative rates of return are the greatest disadvantage. Unlike fixed annuities which guarantee a minimum rate of return, variable annuity returns can be negative in any given year.

A tax favored annuity is a long-term retirement plan that provides a systematic, tax-sheltered way to accumulate funds for retirement. If one works for a school or other qualifying tax-exempt organization covered under IRC Section 501(c)(3) he or she can accumulate money for retirement in a special tax-sheltered plan - a 403(b) Tax Favored Annuity. A tax favored annuity reduces current taxable income. Tax favored annuity contributions are excluded from current taxable income and are tax deferred until the contract owner begins to receive distributions from the annuity. Interest earned on the annuity contribution is tax-deferred until one begins to receive distributions. A tax favored annuity offers a high degree of financial security. Tax favored annuities are commonly offered in the form of fixed annuities. These are guaranteed to earn no less than a guaranteed minimum interest rate stated in the annuity contract. The fixed annuities are backed by the general account of the insurance company. A tax favored annuity does not reduce other retirement benefits.

Immediate Annuities

With an immediate annuity, the annuitant pays an insurance company a certain amount of money as a premium. In return for this premium, the insurance company promises to pay a specified amount to the annuitant (or his or her beneficiary) for a specified period. With an immediate annuity, a 60 year old annuitant may pay a \$100,000 premium to an insurance company. After considering the annuitant's age and gender the company will then guarantee to pay the purchaser some fixed fee per year for as long as he or she lives (or a certain period of time). A portion of this payment is considered a return of premium and therefore not taxable to the annuitant. The remainder is considered interest and will be taxable as such. One of the advantages of an immediate annuity is that an annuitant cannot outlive his or her guaranteed payments. While deferred annuities are designed to help maximize savings, immediate annuities are there to make sure savings provide an income for as long as is needed. Immediate annuities, as the name implies, begin paying an immediate income and last for a specific time period that the contract owner selects. They are often designed to pay as long as one lives. These annuities are commonly used to provide pension benefits to retired employees.

Qualified

The term qualified when applied to immediate annuities refers to the tax status of the source of funds used for purchasing the annuity. These are premium dollars which until now have "qualified" for IRS exemption from income taxes. The whole payment received each month from a qualified annuity is taxable as income since income taxes have not yet been paid on these funds. Qualified annuities may either come from corporate-sponsored retirement plans (such as Defined Benefit or Defined Contribution Plans), Lump Sum distributions from such retirement plans, or from such individual retirement arrangements as IRAs, SEPs, and Section 403(b) tax-sheltered annuities, or Section 1035 annuity or life insurance exchanges. Generally speaking, insurance companies use male/female (sex-distinct) rates to price qualified annuities in situations where the purchaser and/or owner is a corporation. When the annuity is being purchased by an individual, annuity rates are generally unisex. Some states, however, require that unisex rates be used for all qualified annuities.

Non-qualified immediate annuities are purchased with monies which have not enjoyed any tax-sheltered status and for which taxes have already been paid. A part of each monthly payment is considered a return of previously taxed principal and therefore excluded from taxation. The amount excluded from taxes is calculated by an Exclusion Ratio, which appears on most annuity quotation sheets. Non-qualified annuities may be purchased by employers for situations such as deferred compensation or supplemental income programs, or by individuals investing their after-tax savings accounts or money market accounts, CD's, proceeds from the sale of a house, business, mutual funds, other investments, or from an inheritance or proceeds from a life insurance settlement. While most insurance companies apply their male/female (sex-distinct) tables to non-qualified annuities, some states require the use of unisex rates for both males and females.

Required Minimum Distribution (RMD) Option

For tax-qualified annuity policies, the IRS generally requires that all policy owners begin receiving payments from their policies the year in which they reach age 70 1/2, or, if later, the year in which they retire. These payments are called Required Minimum Distributions (RMDs). Contract owners who fail to withdraw their RMD amounts may be subject to IRS penalties. With the single premium fixed annuity, the insurer will automatically calculate the amount of the RMD payments. If an individual selects this option, he or she will not incur surrender charges for withdrawing the RMD amount, even if it is greater than the 10% Window. RMDs can be received on a monthly, quarterly, semi-annual or annual basis. RMD withdrawals will count toward the 10% window for any previous or future withdrawals. Periodic partial withdrawals and automated RMD cannot be used concurrently.

**Part Nine --
Annuities and Retirement Planning**

The interest or growth on annuity investment is taxable in the year in which it was withdrawn and only on the amount actually received. One of the reasons that it is tax-deferred is that IRS never taxes a return of principal. In fact, participants in annuities purchased before 1981 can opt to withdraw principal first and growth or interest later. By utilizing such a strategy, no taxes would be paid on any of the redemptions until such cumulative withdrawals equaled the contract owner's contributions or the principal.

The avoidance of income taxes can continue indefinitely. The death of the annuitant would normally mean that the contract is terminated. However, if one spouse is named as the contract owner and the annuitant and the other spouse is named as the beneficiary, the contract can continue. The surviving spouse has the option of liquidating part or all of the investment without cost, fee, or penalty by either the IRS or the issuer. Withdrawals or complete liquidations trigger an income tax event to the extent that any monies the survivor receives are considered growth or interest.