W&S Financial Group Distributors

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Avoid Potentially Costly Mistakes and Unintended Distribution Consequences: Proper Annuity Structure Helps Reduce Stress and Support Results

1. **Q: Why is it important to know about annuity ownership, titling and beneficiary designations?**

   A: Annuities are governed by a complex set of rules. It is easy to misunderstand how and when an annuity benefit must be paid out by the issuing insurance company, and who will receive the annuity benefit at the death of an owner or annuitant. This confusion can result in annuities with improper titling or improper beneficiary designations.

2. **Q: What do you mean by "improper?"**

   A: Nonqualified annuities that are either owned or have a beneficiary named, or not named, in a manner that will result in the annuity benefit transferring to an unintended recipient, or passing to a beneficiary at a point in time that was not expected by the owner.

3. **Q: As a financial professional, what can I do about this problem?**

   A: There are several things you can do. Make certain that the annuities you sold in the past and sell in the future are structured so that, at the death of the owner or annuitant, the annuity proceeds will pass to the intended person in the manner intended by the owner.

4. **Q: Do certain life events create important reasons to review annuity structure to make sure the annuity benefit will be paid to the intended beneficiary?**

   A: Yes. A marriage, divorce, birth or death are all important times to review an annuity to make certain it continues to be structured properly, and that the benefit will be paid to the desired person or persons.

5. **Q: Do all annuities work the same way?**

   A: No. All annuities operate based on terms of the contract. Contract terms vary among annuities issued by different companies and even different contracts issued by the same company.

6. **Q: What else affects how an annuity operates?**

   A: Federal tax law, state insurance law and how the issuing company administers the annuity.

7. **Q: Who are the parties to an annuity contract?**

   A: The owner, annuitant and the issuing insurance company are the parties to an annuity contract.

8. **Q: What about the beneficiary?**

   A: An annuity beneficiary is not a true "party" to the contract until the death of the owner (or the annuitant, under an annuitant-driven or trust-owned contract) when the beneficiary has the right to receive the contract proceeds.

9. **Q: What is an "annuitant-driven" annuity contract?**

A: An annuitant-driven contract pays its annuity death benefit to the annuitant's beneficiary at the death of the annuitant.

10. **Q: How is that different than an "owner-driven" annuity contract?**

A: An owner-driven contract pays its death benefit to the beneficiary at the death of the owner.

11. **Q: So, how does this affect my client?**

A: If the owner and annuitant named in an annuitant-driven annuity contract are not the same person, unintended, unexpected and disadvantageous payout results may occur at the death of the owner or annuitant.

12. **Q: I thought an annuitant-driven contract paid out at the death of the annuitant. Why would the death of the owner require a payout to be made?**

A: **All annuity contracts**, including annuitant-driven annuities, **have an owner-driven aspect due** to the provisions of Internal Revenue Code Section 72(s). This code section requires that annuity proceeds be paid at the death of an annuity owner. Many of the annuity contracts issued by Integrity Life and National Integrity Life specify that the contract surrender value be paid to the **owner's beneficiary** at the death of the owner, if different people are named as owner and annuitant, and the annuitant is living at the time of the owner's death.

13. **Q: What is an "owner's beneficiary?" I thought a beneficiary was a beneficiary, and that was that. Are beneficiaries of annuitant-driven contracts different than that of an owner-driven contract?**

A: Yes. An **owner-driven contract has one primary beneficiary position**, and this beneficiary receives the annuity death benefit at the death of the contract owner. The death of the annuitant on an owner-driven contract does not necessarily trigger a payment of the annuity proceeds.

14. **Q: What happens at the death of an owner or annuitant under an annuitant-driven contract?**

A: **Integrity Life and National Integrity Life annuitant-driven contracts have two beneficiary positions:** an owner's beneficiary and an annuitant's beneficiary. If the owner and annuitant are the same person, this person's death causes the death benefit to be paid to the annuitant's beneficiary.

15. **Q: What if the owner and annuitant named in an annuitant-driven annuity contract are different?**

A: The death of the owner of an annuitant-driven contract structured this way causes the **surrender value** of the annuity to be paid to the **owner's beneficiary**. The death of the annuitant of an annuitant-driven contract causes the **death benefit** of the annuity to be paid to the **annuitant's beneficiary**.

16. **Q: Is there a preferred way to structure an annuitant-driven contract?**

A: Yes. Naming the same person as owner and annuitant of an annuitant-driven annuity contract is the structure that is least likely to cause unintended payout results at the death of the owner/annuitant.

17. **Q: What if naming the same person as owner and annuitant of an annuitant-driven contract is not possible?**

A: If different people are named as owner and annuitant of an annuitant-driven contract, it is very important to make certain that you and the owner understand that the death of the annuitant will cause the death benefit of the annuity to be paid to the annuitant's beneficiary, and the death of the owner will cause the surrender value of the annuity to be paid to the owner's beneficiary.

18. **Q: Is it a good idea to establish an annuity with joint owners?**

A: No. As a general rule, joint ownership of an annuity is not a good idea. A provision in the Internal Revenue Code treats the death of one joint owner as the death of both owners, requiring a payout of the annuity to its beneficiary. This can cause an unintended payout to a beneficiary when one spouse (the surviving joint owner) is still living. The death of either a joint owner husband or wife will require payout of the annuity proceeds, unless the annuity contract language specifically states that the surviving joint owner will be the primary beneficiary in this situation.

19. **Q: What is "spousal continuation?"**

A: The Internal Revenue Code allows a spouse named as the sole owner's beneficiary to move into the position held by the deceased spouse without requiring payout of the annuity death benefit. This is commonly referred to as spousal continuation. It is important for an annuity purchased for use by both spouses or by either spouse, during their lifetime, to be properly structured to assure that spousal continuation will be possible if desired by the surviving spouse. Check with the issuing insurance company to make certain proper annuity ownership and beneficiary designation are established to allow spousal continuation of the contract according to the contract terms.

20. **Q: What is a 1035 exchange?**

A: Internal Revenue Code Section 1035 allows the tax-free exchange of the following:

- An annuity for an annuity contract
- An annuity for a qualified long-term care insurance contract
- A life insurance policy for an annuity contract
- A life insurance policy for a life insurance policy
- A life insurance policy for a qualified long-term care insurance policy

21. **Q: Do any special rules need to be followed to make sure that an exchange of this type is tax free, meaning the exchange will not cause the annuity or life insurance contract owner to be required to pay income tax on any tax-deferred gain inside the contract at the time of transfer?**

A: Yes. The rules of Internal Revenue Code Section 1035 discussed in question 20 must be followed. Also, the owner and annuitant of an annuity contract, or the owner and insured of a life insurance policy, must be the same before and after the exchange. This requirement is sometimes referred to as the "like-for-like" rule.

22. **Q: Can a trust own or be the beneficiary of an annuity?**

A: A trust can be the owner of a nonqualified annuity. Generally, annuities owned by non-natural persons do not receive tax deferral of gain treatment. However, Internal Revenue Code Section 72 (u)(1)(B) provides an exception for a trust that holds an annuity as agent for a natural person and meets other legal requirements of a trust. If a trust is the owner of a nonqualified annuity issued by Integrity or National Integrity, the trust must be named as the annuity beneficiary.

23. **Q: Are there any special rules that need to be followed when a trust is the owner and beneficiary of a nonqualified annuity?**

A: Yes. The beneficiary of a trust-owned nonqualified annuity issued by Integrity Life or National Integrity Life must be the trust that owns the annuity contract. Because a trust is a non-natural person beneficiary, the longest period of time that the annuity death benefit payout can be deferred is five (5) years from the date of death of the annuitant.

For more information, contact your W&S Financial Group Distributors representative.