

Using An Annuity To Fund Life Insurance

Scenario

Seventy-year-old Mrs. Smith, a healthy non-tobacco user, has a \$50,000 tax-deferred annuity with a cost basis of \$35,000. She has no intention of using this annuity for retirement income purposes. Instead, this asset is earmarked for her daughter, the beneficiary. Mrs. Smith and her daughter are both in a 27% income tax bracket.

Objective

To maximize the amount of wealth that Mrs. Smith leaves to her daughter, while minimizing the income tax impact to Mrs. Smith.



Solution

- 1 Obtain an annuity quote for a five-year payout on the existing deferred annuity to determine the amount available to fund a life insurance policy. In this example, the annual annuity income before taxes would be \$10,599.74, based upon a rate of 3%. The after-tax annuity amount would be \$9,627.81 (based upon exclusion ratio).
- 2 Use that after-tax amount to fund an Aviva Keepsake 201 universal life insurance policy structured as a five-pay plan with a minimum guaranteed death benefit.

Benefits

- 1 Mrs. Smith has peace of mind knowing her daughter will likely receive a larger legacy upon her death.
- 2 Mrs. Smith mitigates her own income tax liability on her annuity by spreading the taxes over a five-year period.

Annuity Only**

END OF YEAR	ANNUITY VALUE	AFTER-TAX VALUE TO BENEFICIARY
1	51,500.00	47,045.00
2	53,045.00	48,172.85
3	54,636.35	49,334.54
4	56,275.44	50,531.07
5	57,963.70	51,763.50

Taxation

Life insurance death benefits are income tax-free to the beneficiary. Any gain in an annuity received by a beneficiary upon death of the owner/annuitant is taxable as ordinary income to the beneficiary. Each annuity payment received is comprised of taxable (earnings) and non-taxable (return of basis) dollars. Mrs. Smith pays income taxes on a portion of the annuity income received that represents earnings. Since the value of Mrs. Smith's estate is less than the unified credit exemption, there are no estate tax implications to this case design.

Combination

YEAR	Annuitization			Life Insurance			Total TOTAL NET BENEFIT
	ANNUITY PAYMENT	OWNER INCOME TAX	PREMIUM	MIN. GUAR. DEATH BENEFIT ***	PRESENT VALUE OF REMAINING ANNUITY (BEFORE TAX)	REMAINING ANNUITY (AFTER TAX)	
1	10,599.74	971.93	9,627.81	16,059.00	40,582.27	36,861.13	52,920.13
2	10,599.74	971.93	9,627.81	31,722.00	30,882.01	28,050.33	59,772.33
3	10,599.74	971.93	9,627.81	47,013.00	20,890.74	18,975.19	65,988.19
4	10,599.74	971.93	9,627.81	61,951.00	10,599.74	9,627.81	71,578.81
5	10,599.74	971.93	9,627.81	76,553.00	0.00	0.00	76,553.00

* This example is for illustrative purposes only. Actual results will vary.

** Assumes earning 3%.

*** Provided there are no loans or unfunded increases to the face amount. Withdrawals will reduce the death benefit proportionally.

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Form # LP34770 / LC34772 (A different form may be offered in certain states.)

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Results

The combination of annuity and life insurance provides a greater benefit to the insured's beneficiaries. The annuity alone would have resulted in a lesser amount to the beneficiary in any given year assuming equivalent rates.



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