# Annuity Owner Mistakes

Tips and Ideas That Could Save You Thousands


PROVIDED TO YOU BY

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INTRODUCTION

# Fixed Annuities — A Great Idea, But...

Annuities can be a great way to make your money work, but many people may not understand the risks, rewards, or the workings of their annuities. This booklet points out common mistakes to avoid, and shows you how to get the most out of your annuity — in plain English. You'll also discover some "hidden" values of annuities that many owners never learn about.

If you have questions after reading, call the representative who provided you this booklet — contact details are on the last page.

| 85% | 54% | $9,277 |
|---|---|---|
| of Social Security can be taxable | of an annuity payment can be tax-free | avg. monthly nursing home cost |

WHAT'S INSIDE

1. The 1035 Annuity Exchange — Does it make sense?
2. How Your Annuity Payments Are Taxed
3. An Annuity That Offers Market Participation
4. Reducing Tax on Your Social Security Benefits
5. Cash Payments for Life — Immediate Annuities
6. Annuities & Long-Term Care Protection

FIVE MISTAKES THIS BOOKLET HELPS YOU AVOID

1. Exchanging annuities without comparing surrender charges and new fees
2. Not knowing how much of each payment is taxable vs. tax-free
3. Missing the cap or participation rate that limits your real return
4. Letting taxable income push more of your Social Security into taxation
5. Having no plan for long-term care costs that exceed $9,000/month

SECTION ONE

# A Closer Look at the 1035 Annuity Exchange

If you own an annuity, you may have been approached about exchanging it for a new model with the latest features. A **1035 exchange** lets you transfer accumulated funds from an existing annuity into another annuity without creating a taxable event — the earnings keep their tax-deferred treatment until you withdraw the money.

The Code allows tax-free exchanges from one life insurance contract to another (or to an annuity), or from one annuity to another annuity — but never from an annuity into a life insurance contract.

## SIX QUESTIONS TO ASK BEFORE YOU EXCHANGE

### 1. Safety

How safe is my annuity? Your money is backed by the claims-paying ability of the issuing company, not a government agency.

### 2. Rate

How does my current renewal rate compare? Introductory rates often expire after 1–2 years.

### 3. Features

Am I missing newer benefits — bonuses, death benefits, LTC riders, guaranteed income?

### 4. Total Cost

Will new fees or charges offset any higher interest or bonus being offered?

### 5. Surrender

Could a new contract reset or extend my surrender charge period?

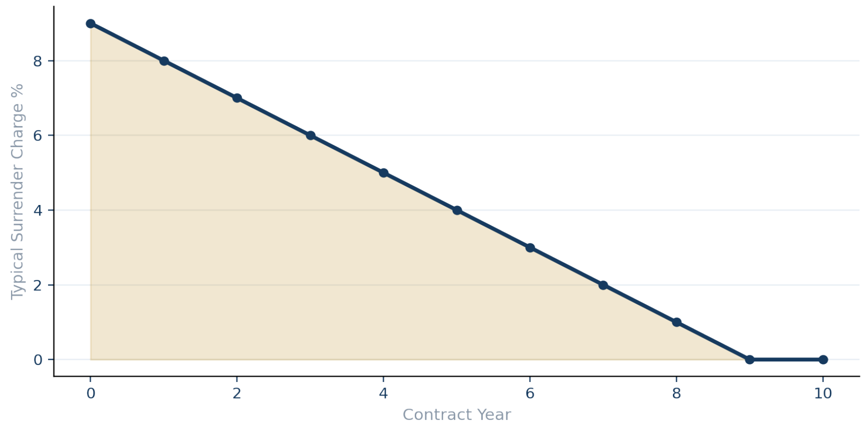
### 6. Necessity

Do I actually need the new features, or do I already have that coverage elsewhere?

**Remember: a 1035 exchange does not eliminate income tax on gains — it only defers it. The cost basis of the old contract simply carries over to the new one.**

## HOW SURRENDER CHARGES TYPICALLY DECLINE

Surrender charges are a key cost to weigh against any exchange — most schedules step down to zero over 5 to 10 years.




*Illustrative surrender charge schedule — actual schedules vary by carrier and product.*

## TYPICAL SURRENDER PERIODS BY ANNUITY TYPE

| Annuity Type | Typical Surrender Period | Typical Starting Charge |
|---|---|---|
| Fixed Deferred Annuity | 5–10 years | 5–9% |
| Equity-Indexed Annuity | 7–15 years | 8–12% |
| Immediate Annuity | None (irrevocable) | N/A |

*Figures are illustrative ranges for comparison purposes; always confirm exact terms in your contract.*

**Tip: Before exchanging an annuity, ask your current carrier exactly how many surrender-charge years remain — you may be closer to a penalty-free withdrawal than you think.**

SECTION TWO

# How Your Annuity Payments Are Taxed


Section 72(b) of the Internal Revenue Code lets you recover your own contributions to a non-qualified annuity — your **cost basis** — free of tax, gradually, over the time you receive payments. The portion of each payment above your basis is taxed at ordinary income rates, ranging from 10% to 37% depending on your bracket.

## WORKED EXAMPLE

A healthy 60-year-old male invests $250,000 into a fixed deferred annuity that begins lifetime income at age 65, paying $1,916/month. At a 22% marginal tax rate, here's how each payment breaks down:


| | |
|---|---|
| **Investment in contract** | $250,000 |
| Monthly annuity payment | $1,916 |
| Expected payments over life (20 yrs) | $459,840 |
| **Tax-free excluded amount** | **$1,035 (54%)** |
| Taxable portion of each payment | $881 |
| **Federal tax per payment (22%)** | **$194** |

*Figure: Breakdown of a single $1,916 monthly annuity payment.*

If the owner passes away before reaching life expectancy, the remaining unused cost basis can be deducted on the final tax return. In our example, a death in year five would allow a **$186,300 deduction**. Conversely, payments received after life expectancy are fully taxable.

Like all annuity guarantees, payments are subject to the claims-paying ability of the issuing company. Results vary by age, income, tax status, and health. Always consult your tax advisor.

## KEY TAX RULES TO REMEMBER

### Section 72(b)

Lets you recover your own non-qualified cost basis tax-free over time.

### Exclusion Ratio

Determines what % of each payment is tax-free vs. taxable.

### Final Return

Unused basis at death becomes a deduction on the decedent's last return.

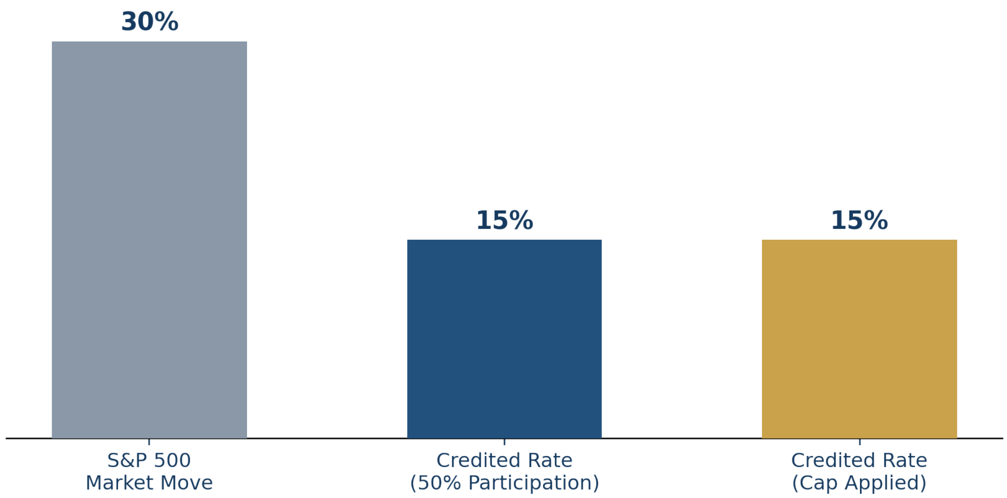
SECTION THREE

# An Annuity That Offers Market Participation

Choosing a retirement vehicle isn't easy. Some want the guarantee of principal and past earnings; others prefer the higher-return potential of equity markets. An **equity-indexed annuity** aims to offer both — tracking a market index like the S&P 500 while helping protect principal when the market declines.

## HOW A PARTICIPATION RATE WORKS

Say the S&P 500 rises 30% in a year and your contract has a 50% participation rate — and a 15% cap. Here's how that hypothetical translates into your credited interest:




*Hypothetical illustration only — not based on any actual product or index performance.*

## SIX THINGS TO CONSIDER BEFORE YOU BUY

- **Surrender fees** — typically apply for 5–15 years and decline over time.
- **Features vary widely** — minimum guaranteed rates can range from 0% to 3% across carriers.
- **Loans & withdrawals** — early withdrawals can reduce downside protection under the contract.
- **Tax consequences** — withdrawals before 59½ may trigger a 10% IRS penalty plus income tax.
- **Fees and expenses** — asset management, maintenance, and contract charges can reduce returns.
- **Company stability** — all guarantees rely on the claims-paying ability of the issuer.

SECTION FOUR

# Reduce or Eliminate Tax on Your Social Security Benefits


Before 1984, Social Security income was entirely tax-free. Today, taxpayers can pay federal income tax on up to **85%** of their Social Security benefits. The good news: annuities can help reduce — and sometimes eliminate — that tax.

The IRS calculates tax on Social Security based on your *total* income from all sources. Income that accumulates inside an annuity does not appear on your current tax return — so sheltering income in an annuity can lower the total income used in the Social Security tax calculation.

## INCOME THRESHOLDS TO WATCH

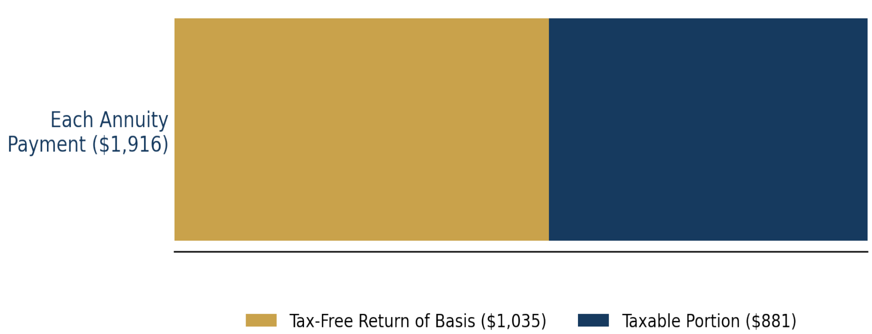
| Filing Status | AGI Threshold | Up to 85% Taxable Above |
|---|---|---|
| Single | $25,000 | $34,000 |
| Married Filing Jointly | $32,000 | $44,000 |

*Source: IRS Publication 17 — modified adjusted gross income thresholds.*

Want to see if this works in your favor? Bring a copy of your tax return (including Schedule B) to the representative who provided this booklet — they can estimate how much you could save.

**Shelter enough income in annuities to bring AGI below the threshold, and you may pay zero tax on your Social Security income.**

## WHY THIS WORKS



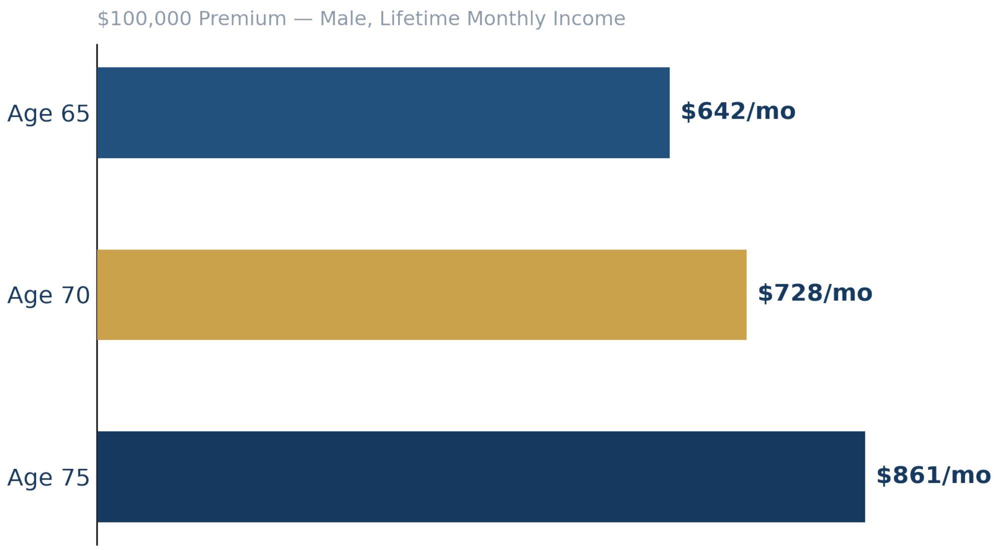

Just as only a portion of each annuity payment counts as taxable income (see page 4), deferred growth inside an annuity stays off your tax return entirely until withdrawn — keeping today's reportable income, and the tax on your Social Security, lower.

SECTION FIVE

# Cash Payments for Life — Immediate Annuities

A fixed immediate annuity converts a lump-sum premium into a guaranteed stream of monthly payments — for a set term, or for life. Part of each payment is income; part is a return of your own principal.

Your monthly payout depends on your life expectancy, the amount invested, and the interest rate locked in at purchase. Payouts are generally higher the older you are at the time of purchase.




*Comparative Annuity Reports, August 2025 — $100,000 premium, male, highest life annuity payments.*

## WHO IS A FIXED IMMEDIATE ANNUITY SUITABLE FOR?

- A retiree needing increased monthly cash flow
- Someone with no heirs, or unconcerned about leaving an estate
- Someone who has set aside other funds to leave to heirs
- A retiree who wants fixed payments and to avoid the maintenance of self-directed investing

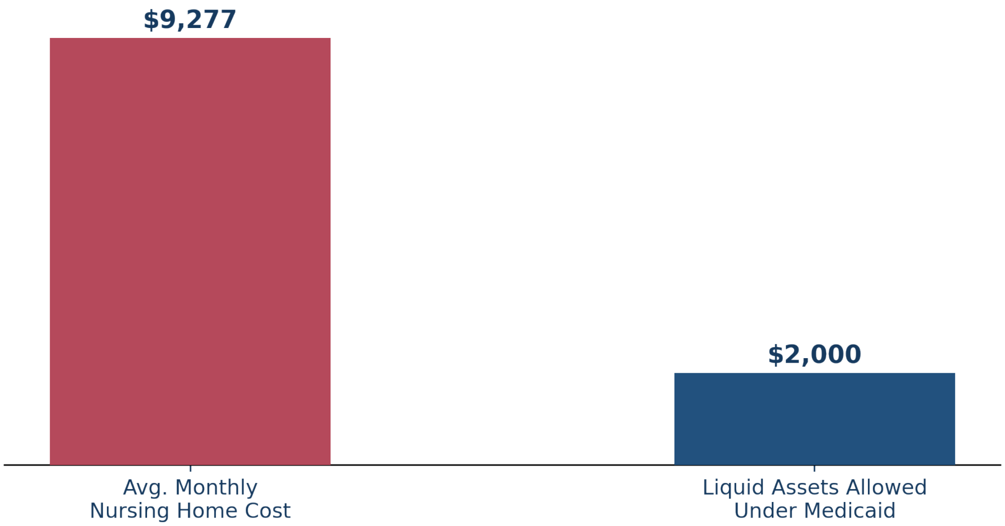
## LIFETIME VS. TERM-CERTAIN PAYOUTS

| Payout Option | Pros | Trade-off |
|---|---|---|
| Lifetime Income | Income guaranteed no matter how long you live | Insurer keeps remaining balance if you die early |
| Term-Certain (e.g. 20 yrs) | Heirs receive remaining payments if you die early | Payments stop after the term, even if you're still living |

SECTION SIX

# Annuities Can Help Provide Insurance for Long-Term Care

More than half of people over age 65 will need some form of long-term care — not medical care, but help with daily living: shopping, meal preparation, bathing, and more. Medicare generally does not pay for this kind of care.




*Genworth Cost of Care Survey 2024 (semi-private room) vs. typical state Medicaid liquid-asset limit.*

Depending on your state's Medicaid rules, you may be required to spend down to as little as $2,000 in liquid assets before assistance begins (spouses may retain additional assets). Transfers to relatives within a **60-month look-back period** are still counted toward your spend-down requirement.

There are ways to shelter assets and still qualify for Medicaid. One option is placing funds in an immediate annuity — when structured in compliance with Medicaid rules, payouts may be treated as an exempt asset (rules vary by state). Speak with someone knowledgeable about Medicaid procedures in your state before acting.

## KEY TAKEAWAYS

- ✓ Financial and retirement planning can affect your estate, even a modest one.
- ✓ Find an advisor knowledgeable in senior-specific financial matters.
- ✓ Find an advisor who answers the questions you haven't thought to ask.
- ✓ Find an advisor who points out opportunities and cautions you about risk.

ABOUT YOUR ADVISOR

# David Peters

Starting in 1994, David built his foundational experience helping clients invest and manage portfolios while working at a Wall Street firm. He works with a diverse clientele, ranging from private individuals and families to business and retirement plans. Demonstrating his entrepreneurial spirit, David founded Alliance Advisors Financial Services in November 1999, and ultimately the Registered Investment Adviser, Alliance Advisors Wealth Management. A graduate of the University of North Carolina with a degree in Economics, David maintains his comprehensive credentials, including a Series 65 securities license, as well as Life, Health, Accident, Property, and Casualty insurance licenses.

## About Alliance Advisors Wealth Management

We are committed to helping individuals and families take control of their financial future with customized strategies and clear guidance. Our services span advanced tax planning, financial planning, long-term care solutions, and retirement planning — designed to simplify the complex and provide clarity at every life stage. We journey with our client families through their retirement years, offering the insights, resources, and tools needed for confident decisions and lasting peace of mind.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