

Understanding ANNUITIES



An Overview for Your Retirement



PACIFIC LIFE

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Get Ready for Retirement

Are you ready for retirement? Whether you are approaching the start of your retirement years—or have already reached them—you need to ensure that your portfolio is prepared.

Annuities are designed to be both a savings vehicle and a source of retirement income. They offer a number of choices for you to grow and protect your income in a way that best meets your needs.

With life expectancy growing each year, receiving an income stream for as long as you live is an important consideration. The lifetime income stream, guaranteed by an insurance company, is a valuable benefit that only an annuity can provide.

What Is an Annuity?

An annuity is a contract between you and an insurance company; you put money into the contract (purchase payments) and in return, it can provide a lifetime income stream. There are many different types of annuities, but the common benefits among all annuities are that they (1) help individuals accumulate money for retirement through tax deferral, (2) provide monthly income that can be guaranteed to last for as long as they live, or (3) both.

Guarantees, including interest rates and subsequent income payouts, are backed by the claims-paying ability of the issuing company. However, these guarantees do not protect the value of the variable investment options, which are subject to market risk.

Think of an annuity as a personal retirement strategy that can help your money grow and make it last longer when you retire. Your money grows faster because you don't pay taxes on earnings until you actually withdraw them or until they are distributed to you.

Who's Who in an Annuity

How you structure your annuity will affect its income payouts and death benefits. The following are the parties involved in an annuity contract.

Insurance Company

An insurance company issues the contract, provides contract information, allocates the money as instructed by the owner, and is responsible for the payout guarantees.

Owner

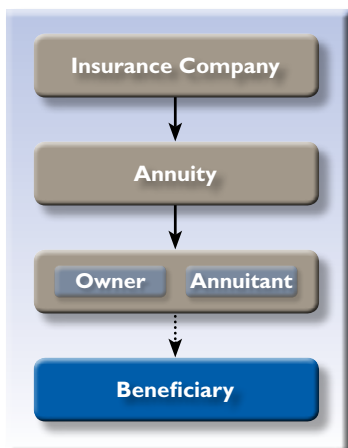
The owner makes the decisions about the annuity, such as how much money to invest and how it should be allocated. The owner also names the annuitants and the beneficiaries.

Annuitant

The owner and the annuitant may or may not be the same person. Either way, it's the annuitant's life expectancy that is used to set the dollar amount of future annuity income.

Beneficiary

Depending on the contract, if the owner or annuitant dies before income payouts begin and there are no surviving owners, usually, the beneficiary is the one who may have the right to receive the death benefit. After annuity payouts begin, if the owner dies and the annuitant is still living, the beneficiary receives the payments. Naming a beneficiary is an important detail that is surprisingly overlooked by some contract owners. If you don't name one, the money in your annuity could end up going to your estate or being subject to probate. In this case, the distribution of your assets may have to be determined in court. In general, beneficiaries can be changed on a contract at any time, so it is important to keep this information current.



Types of Annuities

Single vs. Flexible-Premium Annuities

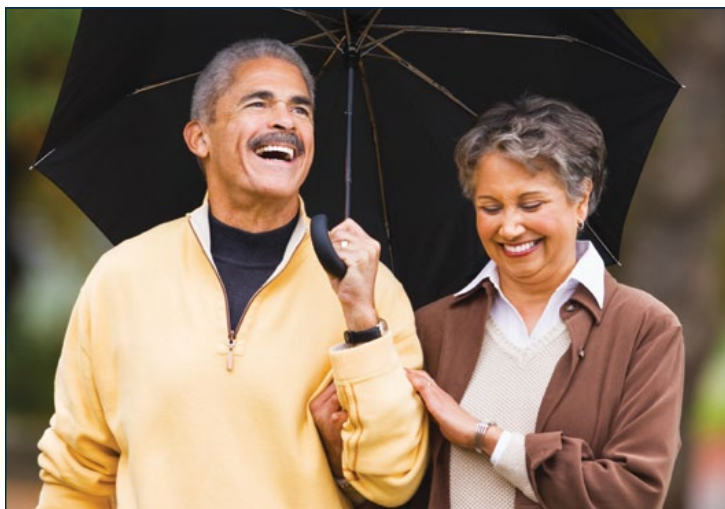
You may purchase an annuity with a lump-sum payment (a single-premium annuity) or make an initial purchase payment with subsequent contributions (a flexible-premium annuity).

Fixed vs. Variable Annuities

There are two basic categories of annuities you can purchase: fixed or variable.

If you are thinking about purchasing an annuity, some of the things you should consider include:

- ✓ What is your risk tolerance? How comfortable are you with market fluctuation?
- ✓ How soon will you need income?
- ✓ What are the fees associated with the contract?
- ✓ What guarantees are associated with the annuity?
- ✓ What is the claims-paying ability of the insurance company backing the annuity?
- ✓ When do you need access to the funds?



Deferred vs. Immediate Annuities

Many people purchase annuities because they want their money to grow tax-deferred while they save for retirement. These types of annuities are known as deferred annuities because you are allowing your money to grow before taking income.

People who would like to receive their income stream right away may be more interested in an immediate annuity. An immediate annuity can provide you with a guaranteed stream of income for life or a specified period of time, whichever you decide.

Deferred

Fixed

A deferred fixed annuity offers a guaranteed minimum interest rate for the life of the contract. Additionally, the annuity may offer a higher interest rate guaranteed for an initial period, such as one, three, six, or 10 years. Generally, after the initial guaranteed period expires, a renewal rate will be declared by the insurance company. Declared renewal rates will always be set at the contract's guaranteed minimum interest rate or higher.

There are a variety of deferred fixed annuities available:

Book Value—a type of annuity that pays a declared rate of interest for a specified period.

Market Value Adjusted—also pays a declared rate of interest for a specified term, but full or partial withdrawals of the contract value (in excess of the specified free withdrawal amount) before the end of the guaranteed term will be adjusted upward or downward according to a formula that takes into account current interest rates.

Indexed—Offers a variable rate of interest based on how the selected index or combination of indexes performs, but with no loss of principal if the index(es) perform poorly. The amount of interest that can be earned may be capped at a fixed percentage.

Variable

A deferred variable annuity is a long-term investment that is designed to help you grow your retirement assets and provide retirement income. It offers a range of investment options from professional money managers. The value of your variable annuity contract will vary depending on the performance of the investment options you choose. The investment options for a variable annuity are typically portfolios that invest in stocks, bonds, money market instruments, or some combination of all three. Variable annuities offer the flexibility of investing in one product with multiple investment options.

Variable annuities also allow you to transfer assets among variable annuity investment options without having to pay taxes on gains. This allows you to make changes to help achieve your investment goals without current tax consequences. Some transfer limits may apply.

In a variable annuity, you can transfer among investment options or rebalance your assets to help achieve your long-term goals—without current tax consequences.

Immediate

An immediate annuity can be purchased with a single lump-sum contribution and can help to maximize and protect income for the rest of your life.

In return for your contribution, the insurance company provides you a pension-like stream of guaranteed, consistent income for your lifetime or for a specified period of time. You may choose to receive your first income payment anytime within the first year, and despite market fluctuations, you can be confident that your income amount will never vary because of market performance.

You can customize your income to meet your retirement planning needs by choosing from a variety of payment options. Income payments will differ based on several factors, including your age, gender, and the amount you contribute. Once the contract is issued, the income option and frequency selected cannot change. While some immediate annuity income options do offer you some access to your money, it should be noted that immediate annuities are less liquid than deferred annuities.

Nonqualified vs. Qualified

You can purchase an annuity either with after-tax or pretax dollars.

Nonqualified

- ✓ Nonqualified annuities are purchased with after-tax dollars. This means that when you are ready to take annuity income payments, you won't owe tax on the portion that's considered a return of your original principal. You only pay taxes on earnings.
- ✓ Distributions from a deferred annuity (prior to annuitization) generally are taxed on a last in, first out (LIFO) basis. That is, any gain within the contract will be distributed before principal.
- ✓ Withdrawals during the income phase (annuity payments) will be taxed on an exclusion ratio basis. That is, each annuity payout will consist of a portion that is earnings and a portion that is a return of after-tax principal.
- ✓ There are no government-imposed limits to the amount of money you can contribute to your nonqualified annuity. However, there may be some company-imposed limits. Your contract will state a date by which you must begin to receive annuity income payments. For deferred annuities, it's typically a specific age, usually around age 95.

Qualified

- ✓ Annuities that fund IRAs and qualified plans are typically purchased with pretax dollars. Qualified contracts and IRAs are subject to IRS contribution limits and other restrictions.
- ✓ Qualified plans are generally set up by employers for employees under the Internal Revenue Code—for example, 401(k) and 403(b) plans. It's important to know that qualified plans, as well as IRAs, are already tax deferred. Therefore, a deferred annuity contract should be used to fund an IRA or qualified plan to benefit from the annuity's features other than tax deferral. The other benefits of using an annuity to fund a qualified plan or an IRA include the lifetime income and death benefit options. A variable annuity offers optional living benefits and the ability to transfer among investment options without sales or withdrawal charges. In fact, Congress has recognized the use of annuity contracts, particularly with respect to funding IRAs, in the Internal Revenue Code [Section 408(b)].
- ✓ With a qualified contract or an IRA, when you are ready to retire and take money out, you will owe taxes on both the pretax amount you invested and the earnings.



Understanding Fees

A fixed annuity typically does not impose direct expense charges on the contract owner other than a surrender charge. A variable annuity, on the other hand, has several types of expenses: investment management fees for the underlying investment portfolios and annual insurance charges in addition to surrender charges.

Surrender Charge

If a contract owner decides to surrender the contract or take withdrawals from a deferred annuity during the early years of the contract, surrender charges may apply. These charges typically range from 5–9% of the annuity value and generally decline to zero over a period of time, such as three to nine years.

Investment Management Fees

Investment management fees are charged for the management of the different funds within the variable annuity subaccounts. These fees will vary depending on the type of investment options you choose.

Insurance Charges

Insurance charges generally include administrative and distribution charges, and mortality and expense risk charges.

The administrative and distribution charges pay for all the services involved in the maintenance of variable annuity contracts, such as the preparation of the contract statement, mailings, and other customer services. Some variable annuities also impose an annual contract fee.



Why Choose an Annuity?

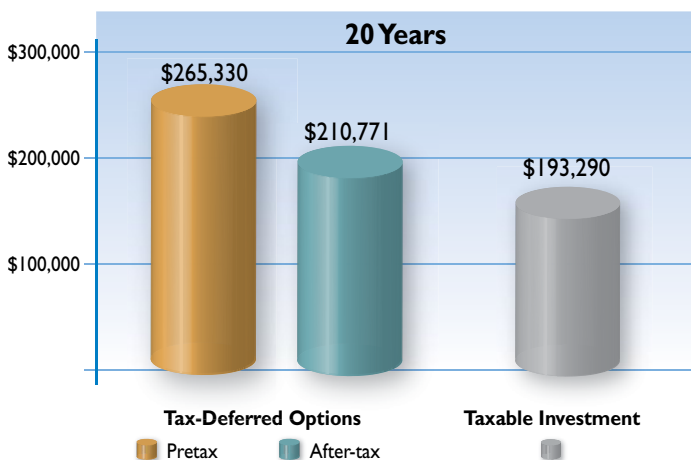
Tax Advantages

If you purchase an annuity with after-tax dollars, a portion of the income you receive once the contract has been annuitized (converted to annuity income payouts) will be a nontaxable return of your investment until all of the principal has been received. Or, if you purchase an annuity with pretax dollars, all the income you receive is taxable.

For deferred annuities, the power of tax deferral allows your money to grow faster because any earnings will compound without current income tax. Whether you purchase your annuity with after-tax (nonqualified) or pretax (qualified) dollars, you have the benefit of tax-deferred compounding.

The Power of Tax Deferral

This chart illustrates just how effective tax deferral can be. A \$100,000 initial purchase payment, compounded at 5% annually, grows with taxes deferred. Once taxes are paid on the lump-sum distribution after 20 years, the amount would be more than the amount accumulated in a taxable investment over the same time frame. Taxes are just one of the factors you should consider when making an investment selection.



Assumes a 33% ordinary income tax rate, assessed yearly on the taxable investment and at period-end on the tax-deferred investment. Actual tax rates may vary for different taxpayers and assets from that illustrated (e.g., capital gains and qualified dividend income). Actual performance of your investment also will vary. Lower maximum tax rates on capital gains and dividends would make the investment return for the taxable investment more favorable, thereby reducing the difference in performance between the investments shown. Consider your personal investment time horizon and income tax brackets, both current and anticipated, when making an investment decision. Hypothetical returns are not guaranteed and do not represent performance of any particular investment. If annuity charges were included, the tax-deferred performance would be significantly lower.

Lifetime Income Payout Option

This feature helps alleviate the fear that you will outlive your income. It's an important benefit that only annuities provide.

Guaranteed Death Benefit

If you die before you begin to receive lifetime income or any other annuity payout option, your beneficiaries will typically receive at least the amount you originally invested, minus an adjustment for any withdrawals. Death benefit payouts will be subject to ordinary income tax.

Optional Living Benefit Riders

Optional living benefits include principal protection, withdrawal, and income benefits for an additional charge. These optional features have greatly increased the flexibility and appeal of annuities as an option for retirement planning.

Flexible Withdrawal Options

What if you need to take money from your deferred annuity before you convert it to supplemental retirement income? An annuity provides a number of withdrawal options. However, it's important to be aware that withdrawals and other distributions of taxable amounts may reduce the value of the death benefit and any optional benefits. In addition, withdrawals and other distributions may be subject to income taxes and, if taken prior to age 59½, a 10% federal tax penalty may apply. Withdrawal charges and a market value adjustment also may apply.

To learn more about annuities and whether an annuity is a good investment strategy for you, talk to your financial advisor.

Why Pacific Life?

The Power to Help You Succeed®

It's essential for you to choose a strong and stable company that can help you achieve your future income needs. For generations, individuals and their families have relied on the strength of Pacific Life to protect their financial security.

- ✓ Pacific Life Insurance Company is organized under a mutual holding company structure and operates for the benefit of its policyholders and contract owners.
- ✓ We have achieved ongoing recognition for high-quality service standards.
- ✓ We offer products that address market environments during all stages of your life.
- ✓ We maintain strong financial strength ratings from major independent rating agencies.

Ratings may change and do not apply to the safety or performance of the underlying investment options. For more information and current financial strength ratings, please visit our website.

Pacific Life has more than 140 years of experience, and we remain committed to providing quality products, outstanding service, and stability to meet your needs today and throughout your lifetime.



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You should carefully consider a variable annuity's risks, charges, limitations, and expenses, as well as the risks, charges, expenses, and investment objectives of the underlying investment options. This and other information about Pacific Life are provided in the product and underlying fund prospectuses. These prospectuses are available from your financial advisor or by calling the toll-free numbers listed below. Read them carefully before investing.

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