



## From Service to Savings: Memorial Day Lessons for Retirement

On Memorial Day, we recognize those who lost their lives in service to our country. For families honoring a loved one on this day, memories of home and family may be especially poignant. How can you help clients build plans that make staying in their homes for life an option?

A recent client case of a family who lost a son in wartime highlights the importance of being able to age gracefully in a beloved home without needing to downsize or move in with other family members. Home is where the family memories were made, making that home especially meaningful.

The case involved a couple whose son died serving in Iraq. Memorial Day always meant a visit to the nearby cemetery to place freshly cut peonies on their son's grave. While the red poppy is the traditional Memorial Day flower, peonies were a favorite flower of his.

The ritual had been an important remembrance for many years. As the couple aged, nieces and nephews helped maintain the garden's peonies and cut them for the remembrance bouquet. If the couple could not attend for health reasons, other family members delivered the bouquet and took photos. When the husband passed away, the wife was able to age in place, staying in their home. Their work with a financial professional enabled her to stay in her home through several more Memorial Day remembrances until she passed away.

How was she able to do this? Part of her ability to successfully keep her home was consistent increases in income. These increases provided her with more spendable income to afford assistance in her home and also helped her portfolio's sustainability.

### Flexible Tax-Free Guaranteed Retirement Income

As clients age, many may want or need additional income. Typically, these clients are also concerned about taxes that reduce spendable income. Partial annuitization of a nonqualified annuity can offer both flexibility in the amount of retirement income payments and provide a stream of income that is partially tax-free.

Imagine a client has \$500,000 in a nonqualified deferred annuity purchased "just in case" additional income might be needed. The client wants some of the guaranteed income the annuity provides but not enough to require annuitizing the full annuity contract value. The client is also concerned that more income will mean more taxes.

The client may be able to partially annuitize the nonqualified annuity contract. For example, the client might use \$100,000 of the annuity to create a stream of income payments that are part return of principal and part gains. If the rules for such a transaction are followed, the client will receive the [exclusion-ratio tax treatment](#), and the portion of each payment that is considered a return of principal is not subject to income taxes since the money used to purchase the annuity has already been taxed. This means a lower amount to report on IRS Form 1099 and, likely, a lower tax bill even though the earnings will be taxed at ordinary income tax rates.

All annuity product guarantees are subject to the claims-paying ability and financial strength of the issuing insurance company.

Insurance products can be issued in all states, except New York, by Pacific Life Insurance Company and in all states by Pacific Life & Annuity Company. Product/material availability and features may vary by state.

**No bank guarantee • Not a deposit • May lose value  
Not FDIC/NCUA insured • Not insured by any federal government agency**

What if the client would like additional income in the future? Going forward a client can annuitize an additional amount. This can allow the client to create additional retirement income later.

### Partial Annuitization

There are two options the client might use for partial annuitization. The client might choose to partially annuitize based on the terms of the annuity contract. That is, the client can instruct the insurance company to take \$100,000, for example, and create guaranteed income based on a life expectancy and/or for a period of 10 years or more. The insurance company will use the terms of the annuity contract to create the income stream.

Another option is for the client to use a 1035 exchange to execute a partial transfer to a single-premium immediate annuity (SPIA), if allowed under IRS guidelines. The transfer must be direct from one insurance company to another, between like-kind contracts, and a thorough review of both contracts should be conducted to determine if a 1035 exchange would be beneficial for the client.

### Rules for Exclusion-Ratio Tax Treatment

For the annuity income payments to receive exclusion-ratio tax treatment, there are some rules to follow:

- **Payment options.** The payment option must include a life-expectancy payment and/or a period of at least 10 years.
- **Waiting period for the remaining amount.** After the initial partial distribution, no additional amounts can be annuitized/distributed from the remainder of the contract value for 180 days. If there is a distribution during that period, both the income stream and the remaining contract value will be treated as one for tax purposes. Exclusion-ratio treatment will no longer apply.

If the above requirements are met, the retiree will have a source of partially tax-free guaranteed lifetime income. Keep in mind, if an annuity contract has additional or optional benefits, such as a beneficiary benefit or an income benefit, a partial annuitization may affect the value of those benefits.

### This Memorial Day, Help Clients Stay in Their Homes and Keep Memories Alive

Establishing a source of guaranteed lifetime income that is available later in life may help clients stay home longer. Managing the tax treatment of income might also reduce clients' tax bills, helping to create more spendable income and, in addition, helping with portfolio sustainability.

#### ACTIONS YOU CAN TAKE RIGHT NOW

- **Identify clients in their 60s who might need an additional source of income later in life.**
- **Evaluate whether each client might need help with income tax management.**
- **Meet and determine whether a partial annuitization strategy might be appropriate.**

Optional benefits are available for an additional cost. A beneficiary benefit is referred to as a death benefit in the contract summary or prospectus.

## Additional Resources and Links

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[Three Questions to Start 2023 Tax Planning](#)

[Tax-Deferred Annuities: Three Tips and a Trap](#)

[Understanding Taxes](#)

**For more information about retirement planning,  
please contact our Retirement Strategies Group at  
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Annuity withdrawals and other distributions of taxable amounts, including beneficiary benefit payouts, will be subject to ordinary income tax. For nonqualified contracts, an additional 3.8% federal tax may apply on net investment income. If withdrawals and other distributions are taken prior to age 59½, an additional 10% federal income tax may apply. A withdrawal charge and a market value adjustment (MVA) also may apply. Withdrawals will reduce the contract value and the value of the beneficiary benefit, and also may reduce the value of any optional benefits.

Partial annuitization and withdrawals will reduce the contract value and the value of the beneficiary benefit, and also may reduce the value of any optional benefits. Partial annuitization is treated as a withdrawal and will reduce the contract value by the amount that is annuitized. Additionally, for contracts that hold an optional living or beneficiary benefit rider, partial annuitization may reduce the benefits guaranteed under the rider, depending on each rider's features and the amount that is annuitized.

Under current law, a nonqualified annuity that is owned by an individual is generally entitled to tax deferral. IRAs and qualified plans—such as 401(k)s and 403(b)s—are already tax deferred. Therefore, a deferred annuity should be used only to fund an IRA or qualified plan to benefit from the annuity's features other than tax deferral. These features include lifetime income and beneficiary benefit options.

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