



Advanced
Capital & Investments

ADVANCED CAPITAL & INVESTMENTS · THE ANNUITY DRAG SERIES · NO. 3

Annuity Rescue

Nos. 1 and 2 showed the drag: capped upside, missing dividends, rider fees and income tax on every dollar of gain. This piece asks the question a trapped owner eventually asks: why not trade the cap and the tax for guarantees and no tax?

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Two paths at 60

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Year by year

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The picture

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If he dies before 85

05

Things to know

\$444,882

to his family in year one with the rescue, against \$210,795 staying put

\$601,628

to his family at 85, against \$454,454 staying in the trap

5.03%

tax-free return on the premiums at 85, against 3.59% in the annuity after tax

01 THE RESCUE Two paths at 60

Same owner as Nos. 1 and 2: a 60-year-old man with \$200,000 in an indexed annuity that credits the S&P 500 price index, 0% floor, 8% cap, with a 1% income rider. Both paths run through the same 1999–2023 market.

Stay in the trap

- Keep the annuity and the 1% income rider
- Upside capped at 8%, dividends left out
- All gain taxed as ordinary income when it comes out
- At death, heirs owe income tax on the gain
- No guarantee beyond the floor and the rider

The rescue

- Drop the income rider and its 1% fee
- Withdraw \$15,000 a year for 15 years, plus the income tax on any gain withdrawn, and pay it into whole life
- Whole life: male 60, preferred plus, \$247,689 base face, dividends buy paid-up additions, no premiums after year 15
- The rest stays in the annuity as a side bucket, still at the 8% cap
- Death benefit is generally income-tax free; cash value grows tax-deferred and is guaranteed

What the whole life adds

\$248,338

death benefit from the first premium, generally income-tax free

\$208,871

guaranteed cash value at 85; \$471,944 at the current dividend scale

\$225,000

total premiums, \$15,000 a year for 15 years, then none

Where the money comes from. The annuity pays the premiums. Withdrawals come out gain first, so some are taxable; we withdrew enough extra to cover that tax (\$14,702 in total over 15 years). Total taken from the annuity: \$239,702.

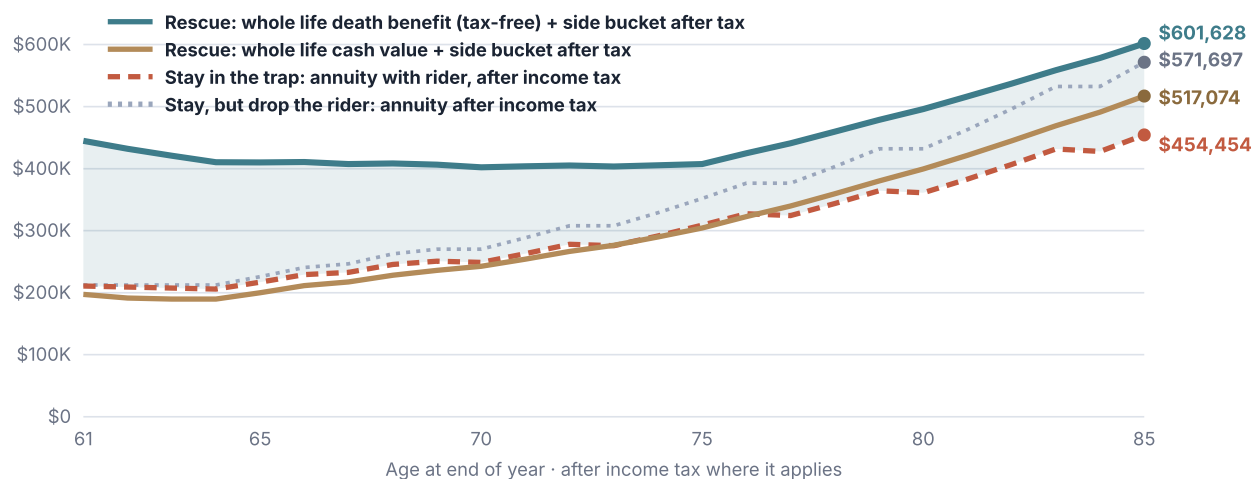
02 YEAR BY YEAR The rescue next to staying put

Age	From annuity	Side bucket	WL CV guar.	WL CV current	WL death benefit	Rescue: CV + side, after tax	Rescue: to family	Stay: after tax
61	\$15,000	\$199,800	\$0	\$649	\$248,338	\$197,193	\$444,882	\$210,795
62	\$18,256	\$181,544	\$7,616	\$9,957	\$250,580	\$191,501	\$432,124	\$209,127
63	\$15,000	\$166,544	\$18,468	\$23,111	\$254,216	\$189,655	\$420,760	\$207,476
64	\$15,000	\$151,544	\$30,495	\$38,215	\$258,953	\$189,759	\$410,497	\$205,841
65	\$15,000	\$147,468	\$43,090	\$54,811	\$264,993	\$199,875	\$410,057	\$217,041
66	\$17,403	\$140,469	\$56,253	\$73,120	\$272,583	\$211,300	\$410,763	\$229,015
67	\$17,289	\$126,876	\$68,518	\$91,130	\$281,225	\$217,193	\$407,288	\$232,660
68	\$15,813	\$119,948	\$81,153	\$110,181	\$290,552	\$228,174	\$408,545	\$245,715
69	\$16,955	\$106,629	\$94,176	\$130,348	\$300,619	\$236,177	\$406,448	\$250,747
70	\$15,800	\$90,829	\$107,606	\$151,662	\$311,421	\$242,491	\$402,250	\$248,680
71	\$15,000	\$81,895	\$120,860	\$173,692	\$323,071	\$254,253	\$403,632	\$262,844
72	\$16,335	\$70,805	\$134,508	\$196,987	\$335,582	\$266,639	\$405,234	\$277,988
73	\$16,154	\$54,652	\$148,589	\$221,651	\$348,961	\$276,303	\$403,613	\$275,648
74	\$15,000	\$42,824	\$163,158	\$247,784	\$363,246	\$289,910	\$405,372	\$291,678
75	\$15,698	\$29,296	\$178,294	\$275,471	\$378,422	\$304,290	\$407,241	\$308,817
76	—	\$31,640	\$181,544	\$291,949	\$394,146	\$322,596	\$424,793	\$327,142
77	—	\$31,640	\$184,756	\$309,073	\$410,278	\$339,720	\$440,925	\$324,311
78	—	\$34,171	\$187,937	\$326,878	\$426,835	\$359,499	\$459,456	\$343,709
79	—	\$36,904	\$191,087	\$345,389	\$443,835	\$380,142	\$478,588	\$364,448
80	—	\$36,904	\$194,203	\$364,621	\$461,295	\$399,374	\$496,048	\$361,244
81	—	\$39,857	\$197,274	\$384,579	\$479,233	\$421,635	\$516,289	\$383,197
82	—	\$43,045	\$200,289	\$405,266	\$497,671	\$444,809	\$537,214	\$406,670
83	—	\$46,489	\$203,249	\$426,735	\$516,655	\$468,964	\$558,884	\$431,766
84	—	\$46,489	\$206,114	\$448,961	\$536,249	\$491,190	\$578,478	\$427,889
85	—	\$50,208	\$208,871	\$471,944	\$556,498	\$517,074	\$601,628	\$454,454

Age at the end of each policy year. From annuity: premium plus income tax on the taxable part. Side bucket: what remains in the annuity, 8% cap on the price index, no rider. Rescue columns take income tax off the side bucket's gain; whole life cash value and death benefit are shown without tax (cash value accessible through withdrawals to basis and policy loans, generally income-tax free if the policy is not a MEC). Stay: the annuity with its rider, less income tax on the gain, the same amount whether he cashes out or his heirs inherit it.

03 THE PICTURE

What the family gets, every year



\$147,174

more to his family at 85 with the rescue than staying in the trap

Age 77

when the rescue's cash value plus side bucket passes the trapped annuity after tax, and stays ahead

\$153,570

more to his family if he dies at 70

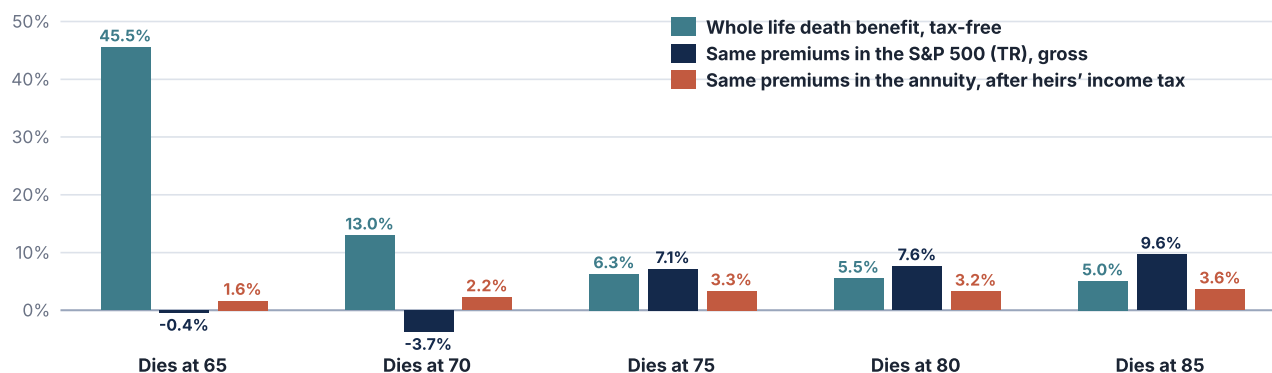
At 85 the question is what the family receives

By 85 he is planning for his heirs, not for cash. Even if he had simply dropped the rider and stayed, his heirs would receive \$571,697 after the income tax on the annuity gain. The rescue leaves \$601,628: the whole life death benefit, income-tax free, plus the side bucket after tax. That is \$29,931 more than dropping the rider alone, and \$147,174 more than staying in the trap.

The rescue leaves more to the family at every age from 61 to 85, against either way of staying. The trade is in the early years of cash value: whole life costs something up front, so the cash value plus side bucket trails the trapped annuity until about 77. With the rescue the cash value has a guaranteed floor (\$208,871 at 85) and can be reached without income tax when taken properly.

04 IF HE DIES BEFORE 85 Return on the same premiums

The same \$15,000 premiums, three ways. What his family receives if he dies at 65, 70, 75, 80 or 85, and the yearly return on what was paid in.



Dies at	Premiums paid	WL death benefit	WL return, tax-free	S&P 500 (TR) value	S&P return, gross	Annuity, after tax	Annuity return
65	\$75,000	\$264,993	45.52%	\$74,206	-0.35%	\$78,771	1.64%
70	\$150,000	\$311,421	12.96%	\$122,924	-3.65%	\$169,588	2.22%
75	\$225,000	\$378,422	6.26%	\$408,181	7.14%	\$294,641	3.30%
80	\$225,000	\$461,295	5.46%	\$613,612	7.61%	\$343,173	3.23%
85	\$225,000	\$556,498	5.03%	\$1,271,599	9.63%	\$429,457	3.59%

Early deaths: whole life wins by a wide margin. At 65 the death benefit returns 45.5% a year tax-free; the same premiums in the S&P 500 had lost money after 2000–2002, and the annuity earned 1.6%.

Longer lives: by 75 the S&P 500 gross pulls ahead, with full market risk and before any tax. The annuity trails whole life at every age, after its income tax, at 3.3% to 3.6%.

Returns are internal rates of return on the premiums paid at the start of each year. S&P 500 shown gross, no fees or taxes, using 1999–2023 total returns. Annuity: price index, 0% floor, 8% cap, 1% rider; heirs pay income tax at 22% on the gain. Whole life at the current dividend scale.

05 BEFORE YOU DECIDE Things to know

- **Surrender charges.** The 10% free withdrawal covers \$15,000 in the first years. From about age 66 the withdrawal is more than 10% of the shrinking annuity, so the rescue works best once the surrender period has ended (often 7 to 10 years from purchase).
- **Dropping the rider ends its guarantee.** The income base and any guaranteed lifetime income go with it. A single premium immediate annuity can often provide similar income later without an annual rider fee.
- **Whole life requires underwriting.** This case is preferred plus. A different health class means different values.
- **Dividends are not guaranteed.** Current values use the carrier's current scale; the guaranteed cash value at 85 is \$208,871 and the guaranteed base death benefit \$247,689.
- **Accessing cash value.** Withdrawals up to basis and policy loans are generally income-tax free if the policy is not a MEC. Loans accrue interest and reduce the death benefit.
- **Taxes on the withdrawals.** Annuity withdrawals come out gain first and are taxed as income; here that was \$14,702, withdrawn along with the premiums.

CAUTION

A rescue into indexed or universal life is not the same rescue

Some annuity "rescues" move the money into indexed universal life (IUL) or universal life (UL) instead of whole life. Look closely before you do:

- **IUL brings the cap back.** Index crediting with a cap, a floor and the price index: the same drag this series measured, now inside a policy.
- **Insurance charges rise every year.** The cost of insurance in UL and IUL climbs with age, steeply after 80, and is taken from the cash value.
- **Little is guaranteed.** Cash value is not guaranteed the way whole life's is. If crediting falls short of the illustration, late-life charges can drain the policy and it can lapse, with the coverage and the tax advantage lost when they are needed most.

See how this plays out in [The Back-End Squeeze: whole life vs. indexed UL →](#)

The Annuity Drag Series: No. 1, The index vs. what gets credited · No. 2, The lost opportunity cost · No. 3, Annuity rescue



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