Do you have a **favorite charity** that needs **financial support**?

The main purpose of life insurance is to provide a death benefit in the event of an early death. But that benefit can work for more than just your loved ones – it can work for a charity of your choosing, as well.

Many individuals wish to provide a special bequest to a charitable organization after they have passed on, but they don’t want to use complicated strategies. A life insurance death benefit paid to a charity is a simple method that can provide your favorite charity with additional funds to help the charity continue with its purposes.

Let’s look at the types of strategies available and how they may be able to help you leave a death benefit for your chosen charity.

1. **Naming a charity as a beneficiary on an existing life insurance policy that you own**

   If you currently own a life insurance policy, your family may no longer have a need for the entire death benefit. If that is the case, you could simply change the beneficiary of the policy and name your chosen charity as the beneficiary of all or part of the death benefit. Even though you cannot income-tax-deduct the life insurance premium when you own the policy, the death benefit is included in the insured’s taxable estate upon death, but your estate would receive an estate tax deduction for the amount of the death benefit paid to the charity.

2. **Key donor life insurance owned by the charity**

   With this strategy, the charity purchases life insurance on your life, since you have been established as a key contributor to their charity.

   However, you would be responsible for the premium payments on the policy itself and could receive an income-tax deduction, subject to IRS limitations, for the cash gifts to the charity to pay the premium. Alternatively, the charity may wish to pay the policy premiums.

   With strategy 1 or 2, you have created a legacy for the charitable cause through life insurance, and the amounts of your gift could be leveraged if the insured dies before life expectancy. In addition, the death benefit goes directly to charity without the delay of probate. Individuals with modest means can use life insurance to make a more sizable gift, with a death benefit ultimately paid to the charity.

3. **Naming a charity as your IRA beneficiary or as beneficiary of a charitable trust, and creating a life insurance wealth replacement trust**

   In this scenario, you would benefit your charity with some property you own other than life insurance. You could name the charity beneficiary of your IRA or of a charitable trust you would create, or make a bequest in your will of other assets to charity. To assist your family, as a replacement of that property, you would purchase a life insurance policy, generally in an irrevocable life insurance trust.
**CHARTABLE GIVING STRATEGIES WITH**

**STRATEGY: NAME A CHARITY AS A BENEFICIARY ON YOUR LIFE INSURANCE POLICY**
- **YOU (OWNER) OWN A LIFE INSURANCE POLICY.**
- **LIFE INSURANCE POLICY**
- **THE DEATH BENEFIT FROM YOUR POLICY GOES TO YOUR CHARITY AT THE TIME OF YOUR DEATH.**
- **YOUR CHARITY HAS FUNDS FROM THE DEATH BENEFIT TO HELP CARRY ON THE WORK YOU SUPPORTED.**

**Advantages to this strategy include:**
- It’s simple, easy, and flexible.
- Allows you the ability to continue owning the policy and control any potential cash value accumulation, while leaving you the option to change the beneficiary again if so desired.

**Disadvantages, however, include:**
- You would receive no income tax deduction today and your family would no longer receive the entire death benefit.
- There is no additional tax benefit. The death benefit is generally income-tax-free to the beneficiary. Charity generally receives any gifts income-tax-free.
- The death benefit is in your taxable estate, but you should receive an estate tax deduction for the portion paid to the charity.
- Charity does not own the policy and has no rights to it or any potential cash value accumulation.

**STRATEGY: KEY DONOR LIFE INSURANCE**
- **YOU (OR THE CHARITY) PAY THE PREMIUM FOR THE LIFE INSURANCE POLICY.**
- **LIFE INSURANCE POLICY**
- **A CHARITY (OWNER) PURCHASES A LIFE INSURANCE POLICY ON YOUR LIFE, BECAUSE YOU HAVE BEEN ESTABLISHED AS A KEY DONOR TO THEIR ORGANIZATION.**
- **UPON DEATH, YOUR CHARITY RECEIVES THE LIFE INSURANCE DEATH BENEFIT, SUPPLEMENTING THE CONTRIBUTIONS YOU REGULARLY MADE.**
- **YOUR CHARITY ALSO HAS ACCESS TO ANY POTENTIAL CASH VALUE ACCUMULATION THROUGH LOANS AND WITHDRAWALS.**

**Advantages to this strategy include:**
- It’s fairly simple to provide your charity with a potentially large endowment of a death benefit.
- You could potentially receive an income tax deduction for your payment of the premium.

**Disadvantages, however, include:**
- The possibility of reducing your current contributions and, thus, reducing the current cash flow to the charity if you decide to reduce your other annual cash gifts.
- Most life insurance companies limit how much life insurance a charity can purchase on the life of a key donor. That death benefit limit is generally five to 10 times the annual gifts that the individual makes to the charity.
- The charity must have an insurable interest in your life, which is subject to state insured interest laws. Check with your local attorney on this.

---

1 Policy loans and withdrawals will reduce the available cash value and death benefit and may cause the policy to lapse, or affect guarantees against lapse. Withdrawals in excess of premiums paid will be subject to ordinary income tax. Additional premium payments may be required to keep the policy in force. In the event of a lapse, outstanding policy loans in excess of unrecovered cost basis will be subject to ordinary income tax. If a policy is a modified endowment contract (MEC), policy loans and withdrawals will be taxable as ordinary income to the extent there are earnings in the policy. If any of these features are exercised prior to age 59½ on a MEC, a 10% federal additional tax may be imposed. Tax laws are subject to change and you should consult a tax professional.
The following hypothetical examples demonstrate the advantages and disadvantages of leaving a death benefit for your favorite charity.

**Life insurance** serves many purposes and can play a valuable role in your charitable giving plans. Your attorney can discuss some of the more complex charitable giving strategies with you.

Please see your financial professional to determine how life insurance can play a part in your plans for a favorite charity.

**Advantages to this strategy include:**
- Because the charity is tax-exempt, there is no income tax to the charity when it receives those assets from your IRA, your charitable trust, or from your will.
- When the IRA or other assets pass to a charity after your death, there is a charitable estate tax deduction under Internal Revenue Code Section 2055(a) if the charity qualifies.
- If established and administered properly, the life insurance death benefit paid to the ILIT should not be included in your taxable estate.

**Disadvantages, however, include:**
- The potentially complex nature of these strategies.
- The likelihood that you’ll incur additional attorney’s fees to establish these trusts.
- The gifts to the ILIT and, if applicable, to the charitable trust are subject to federal and possibly state gift taxes.

**A trust** is a legal structure where one party holds property for the benefit of another party.

**The owner** is the person or organization that establishes the life insurance policy and has rights to name the beneficiary and all other policy rights.

**A key donor** is a charitable contributor whose financial gift is counted on to help continue facilitating charity services.

**A beneficiary** is the person(s)/organization(s) who receive distributions from a life insurance policy after the insured dies.
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so you can be true to yours.

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The charitable remainder trust

Benefit a charity while receiving income
The charitable remainder trust

A way for you to transfer assets to your favorite charity while receiving income from those assets.

When properly set up and administered, a charitable remainder trust (CRT) can do all of these things:

- Benefit your favorite charity.
- Provide you with income for life, or for a set term of years (up to 20 years).
- Give you an income-tax charitable deduction for the value of the remainder interest that goes to the charity.
- Defer your capital gains tax on the transfer of an appreciated capital asset to the trust.
- Change an illiquid asset (i.e., one that is not readily salable) into a diversified portfolio without immediate tax consequences.
- Reduce your estate tax bill (if you have an estate over the federal estate tax exemption amount).

If you could benefit from most or all of these features, this type of trust may be appropriate for you.

However, you should note that there are costs to using this strategy. To fund the CRT, you must give substantial assets irrevocably to the trust. That means those assets will not be available to you should your situation change.

There will also be attorney’s fees to set up the trust, along with annual administration fees to operate the trust.

So before you enter into a charitable remainder trust arrangement, you should first discuss all the costs and benefits with your estate-planning attorney and tax advisor.

As an alternative, there are simpler and less expensive ways to benefit your favorite charity, including:

- Outright donations of cash or assets to the charity during life.
- Naming a charity as death beneficiary of an IRA or nonqualified annuity.
- Charitable bequests in your will of specific assets or cash.
- Donations to a private or public foundation, or donor-advised fund.
How does a charitable remainder trust work?

1. You first adopt an irrevocable CRT in accordance with your estate planning attorney’s advice. You can choose a CRT that pays you income for life or for a term of up to 20 years.

2. You irrevocably transfer assets to the charitable remainder trust. The best choice of asset is generally a “low-basis” (i.e., low original cost) capital asset – for example, a piece of real estate that has appreciated in value.

   **Tax advantages:** You don’t have to pay capital gains tax upon the transfer of the property to the CRT. The property is removed from your taxable estate, which can lower your federal estate taxes if the value of your estate is otherwise over the federal estate tax exemption. And you’ll get an income-tax charitable deduction that year, based on the estimated value of what the charity will receive when the trust ends (see the hypothetical example below).

3. The trustee of the CRT can sell the asset and reinvest in an income-generating portfolio.

4. The trustee pays a specified income to you for life, or for the set term of years. (We discuss the income payments below.) At the end of each year, the CRT will report these payments to you on a K-1 statement, and you may have to report the income on your tax return. Each payment to you is taxed under a 4-tier scheme:

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<td>Tier 2</td>
<td>Capital gains</td>
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<tr>
<td>Tier 3</td>
<td>Tax-exempt income</td>
</tr>
<tr>
<td>Tier 4</td>
<td>Tax-free basis</td>
</tr>
</tbody>
</table>

   a. **Tier 1** is the first money out; this is the CRT’s ordinary income, and is taxed as ordinary income to you. Highest tax into ordinary income class is considered out first.
   b. **Tier 2** is the second money out; this is the CRT’s capital gains, and is taxed as capital gain to you. Here is where you will pay the capital gains tax from when the CRT sold the illiquid asset you donated. Short-term capital gains are considered out before long-term capital gains.
   c. **Tier 3** is tax-exempt income if the CRT holds any municipal bonds.
   d. **Tier 4** is tax-free return of basis (trust corpus).

5. When the trust ends at your death or after the term of years, the CRT distributes all the remaining assets to the charity you designated in the trust. You do not have to include the value of the CRT in your taxable estate.

**Income payments for more than one person**

You can choose a charitable remainder trust that pays income for your single life or a joint life with your spouse or another. You can even choose a CRT that pays income during your life, then your child’s life, before it pays out to the charity.
The two kinds of charitable remainder trusts

Charitable remainder unitrust (CRUT)

A CRUT promises to pay you a set percentage of assets from the trust as they are valued each year. The payment will therefore go up if the value of the assets increases, or go down if the value of the assets decreases.

Because additional contributions are possible and the payments can increase as assets increase – and thus provide an inflation hedge – the CRUT is far more popular than its alternative, the CRAT (see next section).

If you have a less immediate need for income – for example, if you’re more interested in income after retirement – you could consider a net income with make-up CRUT, also called a NIMCRUT. With a NIMCRUT, each year you’re paid the lesser of trust income or a fixed percentage (at least 5%) of the annual value of trust assets. In later years, the NIMCRUT can pay you more to make up for any income shortfalls of earlier years.

Charitable remainder annuity trust (CRAT)

A CRAT promises to pay you a flat dollar amount each year for life or a term of years (not exceeding 20 years). Since no additional contributions are permitted and payments are a flat dollar amount, there is no opportunity for increased payments as asset values rise.

Under IRS rules, you’re limited on the percentage of income you can choose in a CRUT or a CRAT. This is to ensure that the trust won’t be completely depleted by payments back to you, and that there will be something left for charity. However, your income rate will be at least 5%.

These examples are hypothetical and are for illustrative purposes only.
Hypothetical example of the income-tax deduction

Suppose a 75-year-old donor put $1,000,000 into a CRUT promising a 5% annual payment. The donor would get a one-time estimated income-tax charitable deduction of $602,120\(^1\) (based on the estimated value of the remainder that the charity will receive when the trust ends). If the donor put the $1,000,000 into a 5% CRAT, the remainder value and estimated income tax charitable deduction would be $549,892.\(^1\)

Keep in mind that you can deduct only 30% of your adjusted gross income each year if you contribute certain appreciated property to the charitable remainder trust—or 60% of your adjusted gross income if you contribute cash and the trust meets other IRS regulations. Any unused deduction can be carried forward for an additional five years.

Please note: If you have a low income and transfer a large amount of assets to the CRT, you might not get the full value of the deduction. If you can’t get full use of the deduction, you might want to consider one of the alternative charitable options discussed earlier. Itemized deductions are subject to phase-outs for high-income taxpayers. See your tax advisor for more information.

How an annuity can turn CRT income on or off

An annuity is a contract between you and an insurance company that may help you reach your long-term financial goals. In exchange for a premium payment, the insurance company provides you with income, either starting immediately or at some time in the future.

Today’s annuities offer a range of features and benefits that may help you accumulate assets for your retirement, preserve what you’ve accumulated, turn those assets into a guaranteed stream of income, and help pass on a financial legacy to your loved ones.

If the trust document allows, a charitable remainder trust can purchase a nonqualified annuity. The CRT would own the annuity and you would be the annuitant. All annuity withdrawals would go to the CRT, not directly to you. However, the CRT can use these funds (alone or with funds from other investments) to make the payments to you. The best approach is to avoid having the annuity the sole asset in the CRT. If the annuity is the sole asset, the trust may incur withdrawal or surrender charges to get the funds to make the required payments. It is important to understand how the annuity will be valued each year for CRT purposes.

If you want to delay income from the trust until you retire, by choosing a net income with make-up CRUT (NIMCRUT) that’s funded with a nonqualified deferred annuity, the trustee can control the timing and amount of the income distribution to you.

In this case, the trustee does not withdraw funds from the annuity, so the NIMCRUT does not have income to distribute to you. Instead, the trustee keeps track of the amounts it has not paid out (based on the set yearly percentage) in a “make-up” account.

When you are retired and ready for NIMCRUT income, the trustee takes annuity partial withdrawals based on the trust’s income payment rate, and also pays you funds from the make-up account.

It’s best that the trustee of a CRT does not rely only on an annuity to make the income payments to you. That’s because a time could come when the allowed annuity withdrawal falls short of the income payment promised to you. If that’s the case, the CRT trustee might incur a surrender charge to withdraw enough to make the payment. In addition, the CRT could fail to qualify under IRS rules if there is nothing left in the CRT to give to the charity. To avoid this, it helps to have other assets besides the annuity to make the income payment. Also, it is important for the trustee to understand how the various withdrawal options in an annuity contract operate, including why annuitization payments and lifetime income riders may not work well and may cause rule violations for a charitable trust and may put the qualification of the CRT as a tax-exempt trust under Internal Revenue Code Section 664(c)(1) at risk.

For high-net-worth individuals, a charitable remainder trust can provide you with an income, and benefit the charity of your choice. **Find out more by asking your estate-planning attorney and tax advisor.**

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\(^1\) These numbers would change monthly with changes in interest rates. Here we assume a 3.0% applicable federal rate. Your tax advisor must calculate your deduction at the time you transfer the property to the CRT.
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(R-5/2018)
Gifting to an annuity for retirement savings

Helping to ensure your gift is used the way you intend
Will your children (or grandchildren) have enough for their retirement?

With fewer and fewer employers providing defined benefit pension plans, and with concerns about the future of Social Security, the retirement of today’s younger adults will be very different from that of the baby boomer generation. Tomorrow’s retirees will likely have to rely on their contributions to employer-sponsored plans (such as 401(k) plans) and personal savings to fund their lifestyle – and hope those assets are enough.

But you can help your child save for retirement (and reduce the size of your estate) by gifting cash to help with the purchase of a nonqualified annuity.

An annuity can provide your child with many valuable benefits, including a guaranteed, steady income in retirement – in some cases, guaranteed lifetime income through purchase of an optional additional-cost rider. In this way, an annuity could help your future retiree avoid outliving his or her retirement savings.

How gifting to a nonqualified annuity can help provide long-term retirement savings

The gifting process to a nonqualified annuity strategy is very simple.

1. You make cash gifts as a payment to a nonqualified deferred annuity contract owned by your adult child (or adult grandchild). This child is owner and annuitant of the contract.

2. The child should be deterred from taking money out of the annuity due to the potential Internal Revenue Service (IRS) federal additional tax if your child is under age 59½, and annuity contract surrender charges.

3. Once the child reaches age 59½ and the annuity surrender charge period expires, the child accesses annuity values at retirement without a 10% federal additional tax or surrender charges. However, ordinary income taxes will apply to any gain included in amounts withdrawn.
Using trust ownership to provide additional controls on a nonqualified annuity

This strategy can help if you're concerned about the child withdrawing funds before retirement. If the child is a minor, the annuity would have to be owned either in a trust for the benefit of the child or in a custodial account under the Uniform Gifts to Minors Act (UGMA) or Uniform Transfers to Minors Act (UTMA).

1. You would meet with an attorney who would draft the irrevocable trust.

2. The trust is named the owner and beneficiary of the annuity. The child is the annuitant.

3. If all of the beneficiaries of the trust are individuals, the taxation of the annuity accumulation value may be income-tax-deferred. Your attorney would determine whether the annuity contract owned by the trust would qualify for tax-deferred status.

4. The terms of the trust would indicate that annuity distributions could be taken and distributed to your child after reaching age 59½ or older, and after the surrender charge period. You would choose that date, and your attorney would draft the trust provisions providing for that.

5. Having a trust own the annuity may limit options that would be available to an individual owning an annuity.

Please note: Allianz requires a Non-Individual Ownership form to be signed by the attorney, tax professional, or professional trustee.

Income taxes can significantly deplete your principal over a 25-year period.

See the hypothetical examples on the following pages.
The advantage of tax-deferred investing: a hypothetical example

**Tax-deferred investment (after-tax starting value $100,000)**

This chart is illustrating a hypothetical tax-deferred nonqualified investment with an after-tax starting value of $100,000, using a 6% interest rate over 25 years, and withdrawn at an ordinary income tax rate of 32%, to demonstrate the net ending principal. No other payments are made to this investment. The total cost basis is the initial payment of $100,000. The investment is liquidated after 25 years and income tax paid at that time. The examples do not include any state income tax rate that may apply, which would further reduce values.

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The hypothetical rate of return is for illustrative purposes only and is not meant to represent the past or future returns of any specific investment or investment strategy, or to imply guaranteed earnings. It is not attempting to represent the actual return of a nonqualified annuity. Assumes a 32% ordinary income tax assessed yearly on taxable investments and at period end on tax-deferred investments. Actual tax rates and tax treatment of earnings may vary from the illustration for different taxpayers and assets (e.g., capital gains and qualified dividend income, which may impact comparative results). Actual performance of your investment will also vary. Hypothetical returns are not guaranteed and do not represent performance of any particular investment. If a withdrawal or distribution is taken, the tax-deferred investment would be reduced by income taxes on any gains, and if taken prior to age 59½, a 10% federal additional tax may apply. This example does not reflect the deduction of mortality and expense risk charges or investment fees and expenses associated with an annuity. It does not take into consideration the impact of withdrawals to pay your financial professional. Had they been reflected, the results for the tax-deferred option would be lower. 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 tax-deferred and taxable investment shown. Consider your personal investment horizon, risk tolerance, and income tax brackets, both current and anticipated, when making an investment decision.
Taxable investment (after-tax starting value $100,000)

This chart is illustrating a hypothetical annually taxable nonqualified investment with an after-tax starting value of $100,000, using a 6% interest rate over 25 years, and at an ordinary income tax rate of 32%, to demonstrate the net ending principal. No other payments are made to this investment. The interest is taxable each year. The after-tax interest is then added to the principal each year, and the cost basis is increased by that amount.

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A TAX-DEFERRED net principal $323,847
B TAXABLE net principal $271,758

With the tax-deferred investment, you would have accrued an ADDITIONAL $52,089

$100,000 after-tax starting principal
6% interest rate
25 years
32% income tax rate

The higher the starting principal, the greater the potential tax advantage

Again, these hypothetical examples use the same 25-year period, the same 6% interest rate, and the same 32% income tax rate.

<table>
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<th>Starting Principal</th>
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<th>Taxable investment</th>
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Why this gifting strategy may be appropriate for you

- It helps your children or grandchildren save for their future retirement.

- It uses the 2018 annual gift tax exclusion of $15,000 per recipient or $30,000 for married couples without incurring federal gift taxes. If the gifts will be made to an irrevocable trust, the trust must contain special provisions to qualify the gifts for the annual exclusion. Please consult the attorney who drafts the trust.

- It takes advantage of the federal gift tax exemption of up to $11.18 million per donor, or $22.36 million for a married couple, with no gift tax for gifts in 2018, indexed for inflation. The federal gift tax exemption is currently unified with the federal estate tax exemption.

- It avoids problems of cash gifts in savings accounts that are easily accessible to the child.

- It can deter the child from accessing cash, due to income taxation on withdrawals, a 10% federal additional tax for early withdrawals, and annuity surrender charges.

- More controls and oversight can be added when the annuity is owned by an irrevocable trust (but some options that would be available to an individual owning an annuity may not be available to a trust owning an annuity).

- It provides deferral of income taxes on growth in the nonqualified annuity when owned by the child or by a properly structured irrevocable trust.
Special considerations for nonqualified annuities

- If the child is a minor, the annuity would have to be owned either in a trust for the benefit of the child or in a custodial account under the Uniform Gifts to Minors Act (UGMA) or Uniform Transfers to Minors Act (UTMA). However, please be aware that with an UGMA or UTMA gift, depending on state law, the child generally has full control of the annuity at age of majority.

- Drafting and maintaining an irrevocable trust will involve attorney’s fees and trustee fees.

- Your attorney should consider the issue of how the “acting as agent for a natural person” rule would affect tax-deferral eligibility of the annuity contract when owned by a trust. The trust should be drafted so that tax deferral is available for the annuity contract.

- With the irrevocable trust as owner of the annuity, the trust terms cannot be changed, and you as the grantor would not have access to the annuity values.

- If gifts will be made to multiple children, it may be advisable that separate annuities be purchased for each child and that a separate trust is established for each child.

- Federal gift tax laws may change again in the future. There is a potential that if the prior gifts exceed the estate tax exemption in the year of death when they are added back into the estate at date-of-gift value, they could increase federal estate taxes due.

- Use of the federal gift tax exemption or making “split gifts” using the annual exclusions of both spouses requires the filing of a federal gift tax return.

- Since the child would be the owner of the contract, the child would have the rights of an owner, such as the ability to complete a 1035 exchange into a different nonqualified annuity contract, or to use the nonqualified annuity as collateral for a loan.

- Gifting of an existing contract. If you currently own a nonqualified annuity contract and are considering giving the annuity to a child or grandchild, or to a trust, please be aware that the gift of a nonqualified annuity triggers taxable income to you if there are any earnings in the contract. Exceptions to this rule may apply for the gift of an annuity to your spouse. You should discuss the tax issues of the gift of an existing annuity with your professional tax advisor.

1 Change of ownership may also terminate certain riders or death benefits. Please read the contract terms carefully.

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so you can be true to yours.

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While we are proud of our financial strength, we are made of much more than our balance sheet. By being true to our commitments and keeping our promises we believe we make a real difference for our clients. It’s why so many people rely on Allianz and Allianz Life of NY today and count on us for tomorrow — when they need us most.

Guarantees are backed by the financial strength and claims-paying ability of the issuing company. Variable annuity guarantees do not apply to the performance of the variable subaccounts, which will fluctuate with market conditions.

Follow Allianz Life Insurance Company of North America at:

(T-5/2018)
Increasing Wealth Transfer Using Deferred Annuity Distributions

Do you have clients like this?

- Ages 60–85
- Own deferred annuities, but they are not needed for retirement goals
- In a high income tax bracket with a desire to pass maximum wealth to beneficiaries
- Have a desire to provide beneficiaries with wealth replacement to cover annuity assets lost to estate and income taxes

Sandra

Age: 65 years old
Profile: Three grown children; nearing retirement; sufficient income from pension, Social Security and other investments. Doesn’t need her annuity for retirement income.
Goal: Transfer annuity to her children at death.
Deferred Non-Qualified Annuity Value: $700,000
Initial Annuity Deposit: $600,000

Problem

Double taxation in the form of estate and income taxes will significantly reduce the value of the annuity passed on to Sandra’s beneficiaries. The forecasted value of Sandra’s annuity upon her death at life expectancy at age 89 is $2,834,254, based on an assumed rate of return of 6%. There is the potential of the IRS taking 59% of this value, based on projected estate and income tax rates. This would result in $1,669,923 owed to the IRS.

See Page 3 for Important Footnote Information.
A Potential Solution

Reposition Sandra’s deferred annuity asset and purchase life insurance.

How it works:

• Sandra takes an annuity withdrawal of $52,618 ($34,202 after tax, assuming a 35% tax bracket) for 24 years.²
• After-tax annuity withdrawals are gifted to Irrevocable Life Insurance Trust (ILIT). The ILIT purchases a life insurance policy with initial Face Amount of $1,700,000.
• Upon death, the death benefit is paid to the ILIT and, structured properly, will be income-tax-free and not included in Sandra’s taxable estate.
• The ILIT assets then pass to the beneficiaries per trust provisions. Any unused annuity balance passes to designated beneficiaries. These assets are included in Sandra’s taxable estate and any growth is subject to income taxation when distributed to her beneficiaries.

By using the Annuity Maximization Strategy, Sandra is able to use an unneeded, “double tax” asset to pay for a life insurance policy that helps her transfer wealth untouched by taxes. In doing so, she would be able to transfer an additional $870,526 to her children if she were to pass away at her life expectancy of age 89.³

The Client has considered any guaranteed benefit features or guaranteed life annuity options under any annuity contract owned and also other sources of funds for estate planning strategies where the annuity has been identified as a good candidate as a source of funds.

Current Plan at Death

• IRS ($1,669,923) 59%
• Beneficiaries ($1,164,332) 41%

Proposed Plan at Death

• IRS ($145,747) 7%
• Beneficiaries ($1,935,965) 93%

See Page 3 for Important Footnote Information.
Based on the 2008 CSO Table.

2 This rate is assumed to be after-tax and is no guarantee of future growth. When using this strategy, clients should expect fluctuations in return that may affect the amount available for withdrawal. There is no guarantee that the variable annuity will provide the necessary premium to fund the life insurance policy. This example ensures the withdrawals from the annuity are all growth, which is income taxable; any return of premium withdrawn from a non-qualified annuity is not taxable.

3 The policy premium and death benefit amounts used for this case are intended only to help demonstrate the planning concept discussed and not to promote the sale of a specific product. The rates are broadly representative of rates that would apply for a policy of this type and size for Insureds of good health in the ages mentioned. To determine how this approach would work with your clients, individual illustrations should be prepared or requested for your review. If different rates were used, there might be significantly different results.

Existing annuity provisions should be reviewed prior to taking a withdrawal. Annuities are long-term investments designed for retirement. Withdrawals will reduce the death benefit and any optional benefits. Values are based on the assumptions previously stated and are not guarantees or indications of future performance. The existing annuity values assume no contract fees or surrender charges.

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IU-122691 (2/17) (Exp. 2/19)
INTRODUCTION

Most of our working clients dream of the freedom of retirement—freedom to travel, freedom to spend time pursuing personal interests and the freedom to live a life of financial security independent from a job.

For many, the transition into retirement is a time of unexpected stress. The change in lifestyle and the disappearance of the work social network can cause anxiety and depression. The pressures can make our clients susceptible to making bad financial choices at a critical time.

For those who are participants in defined benefit or money purchase pension plans, making the right choice between the various pension payout options can mean the difference between a comfortable retirement and one that is financially tight. Financial professionals are often needed to help make sensible decisions.

Married couples, where one spouse is retiring as a participant in a money purchase or defined benefit plan, must choose between getting payments for the lifetime of the participant, or receiving smaller payments for the lifetimes of both spouses. The retiree must grapple with many questions:

1. What is the likelihood that the retiring spouse will die first?
2. Is the difference between the single life benefit and the joint life benefit enough to justify the risk of choosing the higher benefit?
3. What strategies are available to mitigate the risk of choosing a single life benefit?

Those struggling to answer those questions should consider the possibility of choosing the pension maximization (pension max) strategy. The financial professional needs to be prepared to help decide whether pension max works.

THE PENSION MAX CONCEPT

Defined Benefit Plan

A defined benefit plan is a type of pension plan in which the employer promises each eligible employee a specified monthly benefit at retirement. The retirement benefit is defined in that it is based on a formula that is set forth in the plan document.

The formula used might be based on the employee’s average earnings, or highest earnings. Generally, the defined benefit retirement benefit begins at a specific age, and is paid until the employee’s death.
Defined benefit plans are typically funded only with employer contributions.

At retirement, the defined benefit is typically calculated based on the participant being single. However, federal law requires, in the case of a married participant, that the pension be paid in the form of joint and survivor annuity.

**Money Purchase Plan**

Most money purchase plans use a benefit formula requiring an employer contribution that is a flat percentage of each employee’s allowable compensation. Percentages up to 25% may be used.

When an employee reaches retirement age, the retirement benefit is payable. Money purchase plans usually provide that the participant’s account balance is converted to an annuity at retirement, based on the plan’s annuity rates.

A money purchase plan, like a defined benefit plan, must provide a joint and survivor annuity as the automatic form of benefit. The participant, with the consent of the spouse, may elect a different benefit option.

**The Joint and Survivor Options**

The joint and survivor annuity must provide the survivor a benefit of between 50% and 100% of the initial benefit. It is possible for the participant’s spouse agrees to waive the survivor benefit, and the parties can choose the single life benefit instead.

Some plans offer several options for married participants. For example, the pension might give a choice between:

1. single life,
2. 100% joint and survivor,
3. 66 2/3% joint and survivor, and
4. 50% joint and survivor.

Electing a joint and survivor option protects the participant’s spouse and assures an income as long as either spouse survives. The protection does come at a cost—the reduction in income compared to a single life option for as long as both spouses are alive.

The size of the reduction depends upon three factors:

1. the age of the parties,
2. the percentage of initial benefit preserved for the surviving spouse, and
3. whether or not the company sponsoring the plan subsidizes the survivor benefit.

How much might a reduction be? For a prospective retiree, the monthly benefit might be $2,000 for life only, as contrasted with $1700 per month for a joint and 50% survivor annuity, or $1500/month for a 100% joint and survivor benefit.
Underwritten or Guaranteed Issue Life Insurance?

It makes intuitive sense that if a plan participant is choosing between a life only benefit and an income stream that will last for two lives, the life only benefit should pay more. What retirees sometimes fail to grasp is that if they choose a joint and survivor benefit, they are essentially buying life insurance coverage on the retiree with the difference between the benefits. Since no medical underwriting is involved, the insurance coverage is guaranteed issue coverage.

What if a healthy retiree could choose fully underwritten life insurance coverage? Could the pension benefits be increased? Those are the key questions in the pension max concept. Pension max is a strategy in which the plan participant elects a life only annuity and uses some part of the additional benefit to purchase a fully underwritten life policy.

Suppose in our joint and 50% survivor example above, adequate protection could be provided to the participant’s spouse through purchase of a life policy costing, say, $100 per month. This would give an additional income of $200 per month while still fully protecting the needs of the surviving spouse. That’s how a good pension max implementation should work.

What if a joint and survivor benefit is chosen and participant’s spouse dies shortly after retirement? Under those circumstances a participant would be “paying” for protection that is no longer needed. A few plans will allow the participant to go back and re-elect life only under these circumstances, but in most cases, the participant is stuck with the smaller monthly benefit for life.

A pension max plan is more flexible than the survivor annuity choice. If the participant’s spouse predeceases the participant, the participant could then cancel the insurance and keep the entire extra benefit, or alternatively, keep the insurance and provide a death benefit to the children.

SPECIAL CONCERNS

Pension max seems like a pretty simple concept—and it is. The key question is this: Can the client buy a life policy that will adequately support the surviving spouse using the difference in benefit between the single life retirement income election and the joint and survivor alternative? There are a few nuances that a client must consider in evaluating the choices.

Role of Interest Rates, Death Benefit, and Survivor’s Assumed Life Expectancy

If the pension plan participant dies before the spouse, the pension max strategy relies on the insured’s death benefit to replace the spouse’s retirement income. There are three ways to make that happen:

1. Exchange the death benefit for an immediate annuity based on the surviving spouse’s life (annuitization solution).
2. Manually create an income stream by investing the death benefit, and using as much income and principal as may be needed for the surviving spouse’s benefit (income and principal solution).
3. Plan to keep the death benefit principle invested, and use the income earned only to support the surviving spouse’s needs (income only solution).

All three of the alternatives rely heavily on the assumed interest rate to determine the amount of initial death benefit needed to make pension max work.

Here’s an example. Say that a client is trying to decide between a $2000/month single life benefit and a $1500/month 100% joint and survivor benefit. If the client wants to evaluate the pension max alternative, she needs to figure out how much death benefit is needed to produce $1500/month, or $18,000 in a year.

If the client is comfortable assuming a 5% rate of return on the death benefit invested, the amount of death benefit needed is $360,000. If the client wants to assume a 3% rate of return on investment, the initial death benefit needs to be $600,000.

Of the three alternatives, the income only solution will generate a need for a higher death benefit than the other two. That’s because the clients intend for the death benefit principal to be preserved for family at the death of the surviving spouse.

Finally, if one of the first two solutions is chosen, the survivor’s assumed life expectancy plays a key role in determining the death benefit need for the pension max solution. If the survivor’s life expectancy is ten years, less initial death benefit is needed to support retirement income than if the expectancy is, say, thirty years.

Extra Pension Benefits

Some pension plans add extra benefits that make the pension max calculation a little harder.

For example, some plans include an automatic cost of living adjustment (COLA) for both single life and joint and survivor benefits. Often the COLA amount is adjustable, based on an outside published index. If a client is trying to evaluate pension max, it means that she and her advisor will have to guess at the COLA increases to make a comparison.

Some pension plans require that a joint and survivor option be chosen in order for retiree health benefits to cover a surviving spouse after the participant’s death. If that is the case, the cost for continuing such benefits must be accounted for in the pension max calculation.

With all the unknowns, comparing pension max to the joint and survivor annuity is not an exact science. Those working with clients should work with their customers to determine the conservative assumptions that will be used for the pension max discussion.

Start Early

Pension max cases don’t always work. The key question is whether the right amount of insurance can be purchased with the difference in monthly benefit between the life only plan and the joint and survivor plan.

Whether pension max makes economic sense for a particular client depends upon many factors:

- the tax ramifications of taking a higher or lower pension payout,
For life professionals, the biggest issue often is timing. Unfortunately, most prospective clients aren’t approached with a pension max proposal until shortly before retirement.

If the agent waits until shortly before retirement to propose pension max, he or she is faced with writing a new life policy on, say, a 65 year-old male. At that point, the prospect may be uninsurable or insurable only on a rated basis. Even if insurable at standard rates, the premium on a cash value policy adequate to provide the desired protection may kill the deal. Term rates may initially be acceptable but will rise rapidly as the prospect ages.

Contrast this with pension max started five or ten years prior to normal retirement age. The life insurance rates will usually be much lower and the chances of getting a standard or preferred rating much better. The life professional might propose a cash value policy ten years prior to retirement to be funded over the remaining working years. This plan would provide the spouse with death protection not only after retirement, but prior to retirement also.

At retirement, the cash value of the policy could be sufficient to carry the policy without further premium payments, thus ensuring that the participant can elect a life only pension, receive the higher benefit, and still be assured of death protection for the spouse. The entire increase in pension benefit is available for living expenses without any reduction for life insurance premiums.

If the cash value is high enough, the couple may be able to increase their retirement income even further via policy loans or partial surrenders. If the participant’s spouse dies first, the participant has the option of surrendering the policy for its cash value or continuing the policy to provide a death benefit to children or other beneficiaries.

EXAMPLES

Here are two brief examples—one which describes a good implementation of pension max, and another that shows where it isn’t a fit.

How It Works

Joe and Pearl are a married couple who are five years away from retirement. They have three adult children.

Joe and Pearl are each 60. Joe is a participant in a defined benefit plan at his current employer. Joe has asked his employer for the projected retirement benefits that will be paid by the plan. The employer said that if Joe picks the life only option, he will be entitled to $3000/month. If he chooses the 100% joint and survivor benefit, he and Pearl will get $2000/month.

Joe has asked his financial professional to evaluate whether pension max might work for his situation. They discussed the situation and decided that a 3% interest rate is a comfortable assumption. Joe has also asked about the possibility that some benefit from the plan be preserved for his kids, if possible.
Joe’s advisor recommends that Joe consider a permanent life plan with guaranteed death benefit with a face amount of $800,000. Assuming Joe’s early post-retirement death, the policy will make $800,000 available to Pearl. If the money is invested and it earns 3% interest, it will generate $2000/month for Pearl—exactly equal to the joint and survivor benefit.

Pearl would also have access to the policy’s death benefit to supplement her needs during lifetime. If Joe’s pension has automatic COLAs, the death benefit principal would be available for Pearl to help offset that. Any amount left at her death would be available for their children.

If Pearl dies before Joe, Joe can surrender the policy and get the life only pension amount. Or he can choose to continue the policy and increase his kids’ inheritance.

Because Joe is in good health, he can buy the insurance coverage for $750/month. Even though the premiums begin pre-retirement, the flexibility that the plan offers—as well as the enhanced benefit for himself and Pearl beginning at retirement—may make it attractive.

How It Works NOT

Take the example above, but assume it’s five years later. Joe is at his retirement date. The pension numbers are identical to those projected at Joe’s age 60.

Say that in addition to being older, Joe has had a medical episode that will substantially increase the cost of guaranteed permanent insurance coverage. Even if he uses all of the $1000/month difference between the life only and joint and survivor benefit, he can only buy $300,000 of death benefit.

Does it make sense for Joe and Pearl to choose pension max?

Say that Joe uses all the $1000/month difference for life insurance. If he does that, he has no cushion for COLA that he might otherwise have been entitled to.

If Joe dies, say, five years after getting started, the policy would pay its $300,000 death benefit to Pearl. Assuming Pearl continues to enjoy good health, her life expectancy might be 20 years after that. If Pearl annuitizes the $300,000 death benefit based on her life expectancy and a 3% assumed interest rate, the monthly payment would be $1658. That’s less than the pension’s joint and survivor option.

Under these circumstances based on the assumptions given, Joe and Pearl should probably decide NOT to do pension max.

CONCLUSION

At its core, pension max is a simple idea. The client chooses a life only pension benefit, and uses the extra monthly benefit to buy a life policy designed to protect the surviving spouse.

Pension max is not a fit for every situation. It works best where

- the percentage difference between the life only benefit and joint and survivor benefit is high,
• the non-participant spouse has a short life expectancy compared to the participant spouse,
• there are no valuable benefits that an employer provides that hinge on choosing the joint and survivor benefit, and
• the participant spouse is healthy and insurable at a reasonable price.

Even if pension max is not a fit, financial professionals may be able to help supplement their clients’ retirements with other tools. If you start talking with clients early in their retirement planning process, you can help maximize their retirement income potential—and help yourself along the way.

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Making the right choice between the various pension payout options can mean the difference between a comfortable retirement and one that is financially tight.

Married couples, where one spouse is retiring as a participant in a pension or defined benefit plan, must choose between getting payments for the lifetime of the participant, or receiving smaller payments over the lifetimes of both spouses.

The retiree must grapple with many questions:
1. What is the likelihood that the retiring spouse will die first?
2. Is the difference between the single-life benefit and the joint-life benefit enough to justify the risk of choosing the higher benefit?
3. What strategies are available to mitigate the risk of choosing a single-life benefit?

Those struggling to answer these questions should consider the possibility of choosing the pension maximization (Pension Max) strategy.

**The Situation**

Let’s take a look at Bill and Karen to see how Pension Max may be the right strategy for them. Bill and Karen are age 60 and are five years away from retiring. They have three adult children. Bill is a participant in a defined benefit plan at his current employer. He has asked the employer for the projected retirement benefits that will be paid by the plan.

If Bill picks the life-only option, he will be entitled to $3000/month. However, upon Bill’s death, that $3000/month ceases. If Bill chooses the 100% joint and survivor benefit, he and Karen will receive $2000/month while at least one of them is still living. For example, if Bill dies, Karen will continue to receive the $2000/month while at least one of them is still living. For example, if Bill dies, Karen will continue to receive the $2000/month while at least one of them is still living. For example, if Bill dies, Karen will continue to receive the $2000/month while at least one of them is still living. For example, if Bill dies, Karen will continue to receive the $2000/month while at least one of them is still living. For example, if Bill dies, Karen will continue to receive the $2000/month while at least one of them is still living.

<table>
<thead>
<tr>
<th>Bill's monthly income at retirement at age 65</th>
<th>Life Only Benefit with No Survivorship</th>
<th>100% Joint and Survivor Benefit</th>
</tr>
</thead>
<tbody>
<tr>
<td>$3,000/month</td>
<td>$2,000/month</td>
<td></td>
</tr>
</tbody>
</table>
A Strategy

Bill’s advisor recommends that he consider taking the larger payout, $3,000 per month, and using a portion of the extra amount to purchase a permanent life plan on Bill’s life. His advisor has projected that if Bill were to die at age 65, a death benefit of $338,000 would be able to provide Karen with $2,000\(^1\) per month until her age 90, 25 years. Each year Bill lives beyond age 65 reduces the years between Karen’s current age and age 90. As a result, if Bill were to die in a later year, the initial life insurance amount would support a potentially greater annual withdrawal for Karen, ensuring funds available beyond her age 90 or provide an additional legacy for Bill’s and Karen’s heirs.\(^2\) Bill is in good health and can buy the insurance coverage for $431/month. Assuming Bill’s early post-retirement death at age 65, the policy would provide the following options:

- A $338,000 lump sum death benefit that would be available to Karen should she need it, or
- Generate $2,000\(^1\)/month for Karen — exactly equal to the joint and survivor benefit identified above (assuming a 3% interest rate on the invested death benefit) for 25 years,
- Provide Karen with cash for supplemental income during her lifetime if she would rather take a lump sum instead of monthly income at a future date,
- Any amount left at Karen’s death would be available for their children, something that wouldn’t be available with the pension benefit.

If Karen dies before Bill, he can surrender the policy and continue to get his “life-only” pension amount, supplement his pension with the policy’s cash values, or he can choose to continue the policy and increase his childrens’ inheritance.

<table>
<thead>
<tr>
<th>Years</th>
<th>Life Only Annual Pension Increase over J &amp; S Benefit</th>
<th>Premium Per Year</th>
<th>Death Benefit(^2)</th>
<th>Potential Monthly Withdrawal Amount(^1)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>$12,000</td>
<td>$6,137</td>
<td>$338,000</td>
<td>0</td>
</tr>
<tr>
<td>5</td>
<td>$12,000</td>
<td>$6,137</td>
<td>$338,000</td>
<td>$2,000/month</td>
</tr>
<tr>
<td>10</td>
<td>$12,000</td>
<td>$6,137</td>
<td>$338,000</td>
<td>$2,000/month</td>
</tr>
<tr>
<td>15</td>
<td>$12,000</td>
<td>$6,137</td>
<td>$338,000</td>
<td>$2,000/month</td>
</tr>
<tr>
<td>20</td>
<td>$12,000</td>
<td>$6,137</td>
<td>$338,000</td>
<td>$2,000/month</td>
</tr>
<tr>
<td>25</td>
<td>$12,000</td>
<td>$6,137</td>
<td>$338,000</td>
<td>$2,000/month</td>
</tr>
</tbody>
</table>

Even though the premiums begin pre-retirement, the flexibility that the plan offers — as well as the enhanced benefit for Bill and Karen at retirement make Pension Max a good strategy for them.

1 Before Tax Equivalent assuming a 28% Tax Bracket.
2 This is a supplemental illustration and must be read in conjunction with the basic illustration. The basic illustration contains values using the same underwriting assumptions as this supplement at both guaranteed charges and guaranteed interest rates and contains other important information. The values represented here are for a $338,000 BrightLife Protect\(^\circ\) Policy with level death benefit on a 60-year-old man preferred non-smoker and assumes current charges. If they were to receive a 0% gross rate of return and maximum charges were assessed on the policy, the policy would fail in year 30, by which point $184,110 of cumulative premium would have been paid. The values here are intended to offer a hypothetical representation based on illustrated rates when this marketing item went to print in May 2017. Actual results will vary based on the underwriting classification and crediting rate offered when an illustration is on a different date. Please review a basic illustration containing values based on your own individual age and underwriting class containing both guaranteed charges and guaranteed interest rates as well as other important information. Your financial professional can provide you a copy of the basic illustration.
Pension Max is not a fit for every situation. It works best where:

- Clients are in the 55–60-year-old (pre-retirement) age group where there is a defined benefit pension benefit.
- There is a significant difference between the single-life and joint-life benefit amounts.
- The participant spouse is healthy and can buy insurance at a reasonable price.
- Only a portion of the single-life benefit amount will be needed for life insurance.
- The life insurance on the plan participant can be purchased at a reasonable price.
- There are no valuable benefits that an employer provides that hinge on choosing the joint and survivor benefit.

Is Pension Maximization Right for You?

It depends on a number of factors, such as your financial situation, health, objectives, and the options and benefits you have under your employer’s retirement plan. Your financial, legal and tax advisors can assist you with your decisions and in developing the strategy that is most appropriate for you.

IMPORTANT NOTE

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The policy premium and death benefit amounts used for this case are intended only to help demonstrate the planning concept discussed and not to promote the sale of a specific product. The rates are broadly representative of rates that would apply for a policy of this type and size for Insureds of good health in the ages mentioned. To determine how this approach would work with your clients, individual illustrations should be prepared or requested for your review. If different rates were used, there might be significantly different results.

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enhancing our benefits with pension maximization
Decisions...Decisions!
The first option maximizes the retirement income from your pension or profit-sharing plan while you're alive, but benefits cease upon your death. Should you elect this option at retirement and die shortly thereafter, your spouse may be left with no source of continuing income.

The second option provides a smaller retirement benefit while you are both living, but ensures that your spouse receives an income in case you die first. But in many instances, if your spouse dies before you, you will continue to receive the lower pension benefit for the rest of your life, even though your spouse never received any income.

Neither choice sounds very appealing, does it? Fortunately, there may be an additional choice called Pension Maximization.

Important note
At retirement, the spouse must sign a waiver to make it clear that a single life pension is acceptable.

Pension Maximization: What You Need to Know
The Pension Maximization technique combines purchasing a life insurance policy with electing the “maximum pension benefit with no survivor benefit” option for your pension. With this technique, you may be able to:

• Maximize your pension benefits during your lifetime.
• Help provide for your spouse’s financial independence through the life insurance coverage.
• Use existing savings to help supplement your retirement income with a tax-deferred product.

This concept can work if the insurance is purchased at the time of retirement (ideally, the premiums are lower than the pension gained by taking a “single life” option), but you should note, it may not work if there are any health problems at that time. Therefore, it is generally better to ensure that the proper insurance is in place to help provide a secure retirement income for your spouse.
How Pension Maximization Works
This graph illustrates how pension maximization works while both you and your spouse are living, or when only one of you is living.

Pension Maximization in Action
Carl Robinson, age 52, married to Catherine, age 50, has been working for Company XYZ for the past 25 years and is planning to retire at age 65. Recently, Carl received an estimate from his representative in Human Resources who told him that at age 65, he would receive $2,500/month from his pension plan, provided he doesn’t elect a survivorship benefit. Carl is concerned that if he dies first, Catherine will not see any of his remaining pension benefit. Without survivor benefits, Carl’s early death would mean that most of his pension will be wasted.

If Carl elects the survivorship benefit, his payments will be reduced to $2,100/month, but Catherine will receive a predictable income of $1,050/month (based on a 50% survivorship benefit) after his death. The problem with choosing a survivorship benefit is that if Catherine lives for a short period of time and dies before Carl, Carl will face a lifetime of reduced pension income, even though Catherine and he never received any financial benefit from electing this option. If they both live full lives and die within a year or so of each other, little benefit is ever realized after years of a reduced pension.

Alternatively, Carl can choose to take the maximum pension benefit ($2,500) with no survivor benefit and purchase a life insurance policy prior to his retirement. It is recommended that Carl select an amount that would provide Catherine with a similar income benefit to what it would have been if he had chosen the survivorship benefit ($1,050/month).

The life insurance premiums can be paid while Carl works, or paid using discretionary income. As previously mentioned, it is better for Carl to purchase the life insurance policy sooner than later to reduce the cost of insurance and to take advantage of his current good health. If Carl continues to work and accrue benefits, he needs to consider whether the life insurance policy will be large enough to provide a real choice upon actual retirement at a later date.

In this scenario, the advantages are:
- Carl and Catherine receive larger pension benefits while Carl is alive.
- If Catherine dies first, Carl can surrender the policy for cash surrender or leave a death benefit to his children.
- If Carl dies prior to retirement, Catherine gets the face amount of the insurance policy.
- Catherine controls how the death benefit is invested if Carl dies first.
- A portion of the death benefit proceeds (payable in monthly installments) will be income-tax-free if the death benefit is used to buy an annuity. Typically, pension income is fully taxable.
- Loan capability may be available on the life insurance policy, but, if outstanding, will reduce the net death benefit payable.
- Flexibility to change the beneficiary under the life insurance policy that you may not have under the pension benefit.

<table>
<thead>
<tr>
<th>Carl’s Monthly Income at Retirement (age 65)</th>
</tr>
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<tbody>
<tr>
<td>With No Survivorship Benefit</td>
</tr>
<tr>
<td>---------------------------------</td>
</tr>
<tr>
<td>$2,500</td>
</tr>
</tbody>
</table>
Points to Consider about Pension Maximization:

• If your pension annuity payments have a cost-of-living adjustment, you will need to factor the cost to purchase a much larger amount of insurance in order to provide your spouse with a comparable retirement income.

• By not electing the reduced pension survivorship benefit, in some cases your spouse may lose all rights to any retiree medical coverage if your employer sponsors the coverage. Sometimes this coverage is linked to receiving pension benefits, which would terminate when Carl died if he selects the maximum pension benefit.

• The person on whom the insurance would be issued must be able to qualify for the purchase of life insurance before any further analysis is done.

• You may want the spouse who signs the waiver to own the life insurance in order to ensure the insurance policy remains in effect.

• Failure to keep the life insurance in force up to the insured’s death will result in no death benefit proceeds for the spouse.

Is Pension Maximization Right for You?
It depends on a number of factors, such as your financial situation, health, objectives, and the options and benefits you have under your employer’s retirement plan. Your financial, legal and tax advisors can assist you with your decisions and in developing the strategy that is most appropriate for you.

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Cat. #133784 (4/17)
Social Security: How Life Insurance Can Assist Clients In Meeting Their Future Needs
Introductory Comments

A few words about Social Security and where Social Security planning fits into a client’s overall planning. For most Americans, income during their retirement years will be addressed by three assets groups:

- Retirement Plan assets (to include Company provided pensions, IRAs and 401(k) plans)
- Social Security benefits
- Personal assets.

While important, the first two may not be able to replace personal savings. Company provided pension assets have diminished in importance for many retirees. 85% of American workers in the private sector (i.e., non-government jobs) were covered by a defined benefit pension plan in 1975, compared to only 16% in 2013.¹

Concerns also exist regarding the viability of the Social Security Program

- According to many studies, the Social Security trust fund will be able to cover its retirement and disability obligations for the next 30 years or so, after which there will be a shortfall of about 22 percent²
- The Senate Special Committee on Aging figures funds will fall short in 2037.

Sections of this guide will talk about how clients might be able to use life insurance, and the protection it offers families, as a way to help supplement these two items as part of a personal asset accumulation approach.

¹ National Institute on Retirement Security
Social Security may and can be an integral part of your client’s planning. While it may not be central, it remains a cornerstone of many retirement plans. In some cases it can be used by a client as part of a wealth transfer strategy. An assessment of your clients’ needs, and a comparison with available resources can help identify any shortfalls that may exist. The earlier the process begins, the more viable the opportunity to arrange their personal estate and reallocate assets to help address future needs.

This guide will show three ways to look at a client’s overall planning and offer three strategies that can help enhance, supplement or use Social Security to achieve their retirement or wealth transfer goals:

1. For many clients, Social Security will represent a major portion of their retirement resources and they may benefit from strategies to maximize what they are entitled to receive, perhaps by delaying the receipt of their benefits. See “The Social Security Bridge;”

2. Some clients will need to plan for personal assets to fill the retirement income gap that will exist between their needs and what Social Security and retirement plan assets will provide See “Supplementing Retirement Income;”

3. Other clients will not need Social Security for their retirement needs, but it may be helpful in addressing their legacy plans. See “Maximizing Social Security for Legacy Planning.”

Sadly, however, recent surveys indicate that less than 30% of all Americans have any idea of what they may be entitled to receive from Social Security. They will have no idea of the significance that Social Security may still play in their retirement and estate plans. If they wait too long, it may be too late to maximize the role Social Security might play in their retirement.

The Social Security Administration website offers substantial general benefit information, as well as, personal planning tools to access an individual’s own benefit profile and benefit projections. See: http://www.ssa.gov/myaccount/materials.html#&a0=0

Consider the following three situations where life insurance may provide assistance to your clients in conjunction with your review of their Social Security benefits and retirement and estate planning goals.
Strategy One – The Social Security Bridge

Do you have clients who would like to get the maximum benefit amount their Social Security profile can provide? This approach will show how life insurance can be integrated into an overall protection plan, and allow a client to maximize their overall Social Security benefits.

This approach may be right for clients who:
- Want to maximize their Social Security benefit
- Can delay Social Security benefits until age 70 to get increased monthly benefits
- Want to retire earlier than Social Security full retirement age
- Clients who have a need for life insurance
- Wish to leave a legacy to their children

An important part of any financial plan is planning for retirement. Setting aside money in various retirement accounts will help achieve retirement goals. When assessing retirement need, one income source that you’ll need to consider is the amount of Social Security benefits that will be available, based on an individual’s personal profile and projected retirement age or date.

For most future recipients, “normal” Social Security full retirement age will be between 66 and 67. However, clients can access these funds as soon as they reach age 62. Conversely, they can defer receipt of Social Security benefits until age 70. Accelerating benefits, taking them prior to their full retirement age, will result in reduced benefits. Delaying receipt will result in enhanced benefits. Although timing and amounts will vary from client to client based on their birth year, on average it is about an 8% per year reduction or growth.

This can be a critical element in a client’s planning. At its heart, Social Security is a fixed annuity. For clients that can defer receipt of their Social Security benefits, during the deferral period they will see year over year compounded growth at about 8% per year. Few financial instruments in 2018 are offering 8% growth.

Retiring early can mean a 30% reduction in Social Security benefits. Retiring later, however, can increase your benefits 8% a year.
Case situation
Chris and Linda’s Challenge

THE SITUATION

Chris and Linda recently met with their financial advisor. They are married, both 45-years-old, with two children and want to retire early. Based on today’s Social Security benefits schedule, Chris would qualify for the maximum Social Security benefit if he retired at the full retirement age of 67. However, he wants to retire at age 62, a point where Social Security benefits would be substantially reduced. Chris is looking for a strategy that would allow him to have access to an amount that is equal to what he would receive from Social Security at full retirement age 67, yet allow him to retire at 62 and delay triggering his actual Social Security benefit until age 70.

A cash value life insurance policy may be an excellent way to help provide for additional funds to help “bridge” the Social Security Gap. By tapping into the policy cash values in strategic years, between age 62 to age 70 (just 8 years), clients can obtain the equivalent value of their Social Security benefit. They can let their Social Security benefit grow and take their maximum benefit at age 70. All along their family has death benefit protection and later, a possible legacy.

Using life insurance, Chris and Linda are able to retire when they want, and still delay Social Security benefits in order to get the maximum amount available to them.

4 Calculation: Benefit of $32,000 per year; 85% taxed at 40% income tax rate ($27,200 x 40% = $10,880 tax); $32,000 - $10,880 = $21,120 after tax amount of projected benefit at FRA.
WHY IT WORKS

• Life insurance is not always just about estate planning and taxes. It can be an effective tool to help provide supplemental retirement income in addition to leaving a legacy to beneficiaries.

• Chris will be able to defer taking his Social Security benefit to become eligible to receive a higher benefit amount at age 70. By taking his full retirement age Social Security benefit equivalent from the life insurance policy at his early retirement age of 62, life insurance helps “bridge the gap” between an early retirement and an increased Social Security benefit.

• All along, Chris retains the choice to change his retirement date and still have cash value life insurance protection.

THE STRATEGY

• It is projected that Chris will be eligible for a Social Security benefit of $32,000 per year at his full retirement age of 67 and eligible for a $40,000 annual benefit if he delays until age 70.

• Chris and Linda need to purchase a $500,000 life insurance policy to protect their family if something happened to Chris. A cash value life insurance policy, on Chris’ life, meets both personal protection needs and helps to fund a “supplemental income stream” at Chris’ age of 62.

• They will pay policy premiums for 16 years, from Chris’ age 45 through his age 62. (Annual premium of $8,809 for 16 years)

• At age 62 and until he reaches 69, Chris will plan to take $21,120 in funds from the life insurance values, an amount equal to the “after tax” amount he could receive from Social Security at age 67, “normal retirement age” in a 40% Tax Bracket.

• At age 70 Chris can trigger his delayed Social Security benefit of $40,000.

• Chris and Linda can leave a legacy to their two children with the remaining policy death benefit.

• Along the way, Chris can always change his mind and work longer, and they will still have cash value in their policy to enhance their retirement beyond age 70.

<table>
<thead>
<tr>
<th>Joint Age</th>
<th>After-Tax Social Security Equivalent from Policy</th>
<th>Cash Value³</th>
<th>Life Insurance Benefit</th>
<th>Delayed Social Security Benefit at Age 70</th>
</tr>
</thead>
<tbody>
<tr>
<td>62/62</td>
<td>$21,120</td>
<td>$187,695</td>
<td>$676,732</td>
<td>$0</td>
</tr>
<tr>
<td>65/65</td>
<td>$21,120</td>
<td>$152,726</td>
<td>$613,372</td>
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</tr>
<tr>
<td>69/69</td>
<td>$21,120</td>
<td>$98,221</td>
<td>$528,191</td>
<td>$0</td>
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<tr>
<td>70/70</td>
<td>$0</td>
<td>$104,635</td>
<td>$527,616</td>
<td>$40,000</td>
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</table>

³ This is a supplemental illustration authorized for distribution only when preceded or accompanied by a basic illustration from the issuer. The basic illustration contains values using the same underwriting assumptions as this supplemental at both guaranteed charges and guaranteed interest rates and contains other important information. The values represented here are for a $500,000 BrightLife® Grow SIUL policy on a 45-year-old male preferred non-smoker and a 45-year-old female preferred non-smoker. The values represent the cost of 16 years of premiums. The values represented here are non-guaranteed and assume current charges and a current interest rate of 5.81%. If guaranteed rates and charges are used, the policy would fail in year 20. Your values will be different based on your gender, age and health. Work with your financial professional to create an illustration that is tailored to your specific situation.
Strategy Two – Supplementing Retirement Income

Do you have clients whose projected Social Security benefits and “traditional retirement assets” may fail to meet their retirement income needs? This approach will show how life insurance can be integrated into an overall retirement planning strategy and allow a client to coordinate their Social Security benefits, traditional retirement benefits, and personal savings with their life insurance protection.

This approach may be right for clients who:

- Are 10 or more years away from retirement
- Have projected Social Security and “traditional retirement assets” that won’t meet their retirement needs
- Are looking for retirement planning solutions
- Are healthy and have a life insurance need
- Would like to leave a financial legacy.

Retirement protection is often a central goal for most clients. They have worked for many years and want to feel confident that they have accumulated enough wealth to maintain their standard of living in their non-working years. How much is enough? People are living longer than in previous generations. It used to be that 70% of your salary at retirement was a good rule of thumb to gauge how much people should save. But for many this number is no longer a valid indicator. In the early years of retirement, your clients might lead a much more active life with travel, visiting grandchildren, hobbies and other activities. Whereas in the later years, they might be less active, but the cost of living could have increased. Also consider that in the working years there may be a need for a source of emergency funds.

Given current health trends and an increasing dependence on personal savings, clients need to properly prepare for retirement. Consider the economic downturn. Millions of Americans either lost their jobs, their nest eggs, or both! Assets that were set aside for retirement, such as real estate or securities, were quickly reduced to a fraction of their previous value and in some cases had to be liquidated all together. Yet the need for future retirement income remains. In addition, inflation rates have been slowly rising. Would a 3% average annual inflation rate jeopardize the value of your client’s current retirement portfolio?

WHY LIFE INSURANCE

Life insurance cash values may help with many of these planning issues. A life insurance policy that builds cash value can accomplish two goals. First, it can provide essential life insurance coverage for the family. Second, it can be another source of supplemental income for the client and their spouse in retirement. Like a 401(k), life insurance can build value, tax-deferred. What’s more, when you’re ready to access this cash, you can do it potentially tax-free.

Under current federal tax rules, clients generally may take federal income tax-free withdrawals up to their basis (total premiums paid) in the policy or loans from a life insurance policy that is not a Modified Endowment Contract (MEC). Certain exceptions may apply for partial withdrawals during the policy’s first 15 years. If the policy is a MEC, all distributions (withdrawals or loans) are taxed as ordinary income to the extent of gain in the policy, and may also be subject to an additional 10% premature distribution penalty prior to age 59½, unless certain exceptions are applicable. Loans and partial withdrawals will decrease the death benefit and cash value of their life insurance policy and may be subject to policy limitations and income tax. In addition, loans and partial withdrawals may cause certain policy benefits or riders to become unavailable and may increase the chance the policy may lapse. If the policy lapses, is surrendered or becomes a MEC, the loan balance at such time would generally be viewed as distributed and taxable under the general rules for distribution of policy cash values.
Case situation
Gary and Darlene’s Challenge

THE SITUATION
Gary and Darlene are married and both age 45. They have two high-school-aged daughters who are looking at colleges. Although they have been contributing to their employers’ 401(k) plans, their financial professional has made them aware of the limitations on funding these plans. They also know that Social Security provides only a limited supplemental benefit. So, they are looking for other ways to save in a way that is tax-efficient.

THE STRATEGY
• Their financial professional has suggested that Gary and Darlene consider a Survivorship IUL policy.
• If they were both to die, the policy would provide an immediate source of cash for the girls’ current and future financial needs.
• While they’re alive, the policy cash value could continue to grow over time to create a source of supplemental income for their retirement years.
• Assuming they pay policy premiums of $15,000 a year for 20 years, at a 5.81% gross rate of return (which is not a guaranteed rate), their life insurance policy could provide approximately $47,000 for 20 years, beginning when they’re age 66. (In a 35% income tax bracket, $47,000 after-tax would equate to approximately $72,000 of before-tax income.)

WHY IT WORKS
• Cash value life insurance, single life or survivorship life insurance policies, can provide a cost-efficient means to accumulate assets.
• During the time prior to their retirement years, there is a life insurance benefit of $1,000,000 to provide financial protection for their daughters.
• When they need retirement income, the policy cash values can be accessed via loans or withdrawals, as a source of supplemental income. Policy loans and withdrawals will reduce the face amount and cash value of the policy. Clients may need to fund higher premiums in later years to keep the policy from lapsing.

5 This is a supplemental illustration authorized for distribution only when preceded or accompanied by a basic illustration from the issuer. The basic illustration contains values using the same underwriting assumptions as this supplemental at both guaranteed charges and guaranteed interest rates and contains other important information. The values represented here are for a $528,157 BrightLife® Grow SIUL policy on a 45-year-old male preferred non-smoker and 45-year-old female preferred non-smoker. The values represent the cost of 20 years of premiums. The values represented here are non-guaranteed and assume current charges and a current interest rate of 5.81%. If guaranteed rates and charges are used, the policy would fail in year 25. Your client’s values will be different based on your gender, age and health.
Section 3: Wealth Transfer-Legacy Planning with Social Security Max

Do you have clients with substantial wealth who will not need or rely on Social Security for their own financial needs? They may be able to use life insurance to leverage this personal benefit amount and enhance the legacy they leave for their children, grandchildren, or favorite charities.

This approach may be right for clients who are:

- Healthy and have a life insurance need or capacity for life insurance purchases
- Age 62 or older
- Qualified to receive Social Security, but do not need Social Security for retirement income
- Would like to enhance or create a financial legacy

Most clients will use their Social Security benefits to support their retirement income needs. However, some clients may have been fortunate enough to amass a comfortable retirement nest egg. Perhaps they’ve not even considered their Social Security benefits as a source of income when they are retired. If these benefits are “excess,” the after tax funds will merely be added to the client’s portfolio. As a result they may be subject to taxes on investment growth and, possibly increase their estate or other wealth transfer taxes. Legacy planning with life insurance can offer a more effective use of these excess benefits.

If your clients have children, grandchildren, or charities that are important to them, some or all of their Social Security benefits could instead be used towards a life insurance policy. This can be a very simple way to create a legacy for their family or charities.
Case situation

Bill and Debbie’s Legacy

THE SITUATION

Bill and Debbie are working with their financial professional on their retirement plans. They are both turning 66 at the end of this year. During their working years, they accumulated substantial assets and both have employer provided pensions. They never even considered Social Security as a necessary source of retirement funds. They’re not even sure how much they are eligible to receive.

• During their recent planning discussions with their financial professional, they uncovered that they are both eligible to receive the Social Security maximum benefit at their retirement’s “normal retirement age” 66. After taxes, their financial professional estimated that together they will have a total of $64,000 in pre-tax benefits. This equates to approximately $40,000 in after-tax dollars available to them.

THE STRATEGY

• Bill and Debbie decide to use half of the after tax amount available to them from Social Security, or $20,000, as premium for a life insurance policy on their lives, to provide a benefit for their 4 grandchildren.

• They can purchase a range of policies. Depending on each client’s situation one approach may be better than the others.
  – A survivorship life policy
  – A single life policy on either Bill or Debbie
  – Two single life policies, one on Debbie’s life and one on Bill’s life

They elected to purchase an indexed universal life policy on Debbie’s life.

[Diagram showing the flow of Social Security Benefits, Bill and Debbie, IUL Protect policy, Grandchildren, and Taxes]
A COMPARISON

Here is comparison of their legacy that shows the advantage of placing $20,000 in a life insurance policy insuring Debbie’s life.

<table>
<thead>
<tr>
<th>Approach</th>
<th>Annual Contribution</th>
<th>Over 20 ** years</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gift</td>
<td>$20,000</td>
<td>$400,000</td>
</tr>
<tr>
<td>Invest*</td>
<td>$20,000</td>
<td>$554,764*</td>
</tr>
<tr>
<td>Insure6</td>
<td>$20,000</td>
<td>$1,000,000**</td>
</tr>
</tbody>
</table>

* Projected return is 5% before tax, 3.02% after tax.
** Assume Social Security amounts contributed to life insurance in all years

WHY IT WORKS

- Bill and Debbie did not need their Social Security benefit for living expenses
- They only used a portion of the funds from Social Security for life insurance
- They can still make annual gifts to family members or charities with the remaining benefit
- They are able to leverage their legacy with use of a life insurance policy

OTHER CONSIDERATIONS

Please remember Cash Value life insurance does have many other considerations clients should review carefully before selecting a life insurance policy. Please keep these important point in mind:

- Clients must keep paying the required premiums for the entire premium payment period, missing or skipping premiums will negatively impact the amount of loans and withdrawals available. A life insurance policy like Bright Life Grow and Protect generally takes years to build up a substantial cash value, to be effective the policy should be held until death.
- This idea is based on a hypothetical scenario based on certain rates and charges in the policy. The rates and charges are not guaranteed and thus the actual results your client will receive will be different.
- Clients must qualify both medically and financially for the life insurance.
- How much life insurance your client can purchase and the price they pay will depend on the medical and financial underwriting.
- Generally, there are many additional charges associated with a BrightLife Grow or Protect SIUL policy including but not limited to a front end load, monthly administrative charge, monthly segment charge, cost of insurance charge, additional benefit rider costs and a 15 year surrender charge.

6 This is a supplemental illustration authorized for distribution only when preceded or accompanied by a basic illustration from the issuer. The basic illustration contains values using the same underwriting assumptions as this supplemental at both guaranteed charges and guaranteed interest rates and contains other important information. The values represented here are for a $1,000,000 IUL Protect Individual policy on a 66-year-old female preferred non-smoker. The values represented here are non-guaranteed and assume current charges and a current interest rate of 6.05%. If guaranteed rates and charges are used, the policy would fail in year 25, (age 90, via the No Lapse Guarantee). Your values will be different based on your gender, age and health. Work with your financial professional to create an illustration that is tailored to your specific situation.
Closing Comments

Social Security is an important consideration for most of your clients as they plan for their ultimate retirement goals. However, its impact will vary widely for each client. Additionally, not all US citizens are eligible to participate in the Social Security system.

Most eligible participants do not realize the scope of their own Social Security benefits. They are not aware that the maximum Social Security benefit in 2017 available at “full retirement” age is only $2,687 per month* or $32,244. The majority of eligible Social Security recipients receive less than half that amount. Although important, Social Security, along with qualified pensions, will only address a portion of retirement needs for many of your clients. Personal assets, to include life insurance, will be needed to address any shortfall.

Opening up a discussion with clients on retirement needs and Social Security long before their retirement years makes good sense. Life insurance, either single life or survivorship life, can be an invaluable planning tool for you to consider. Also, take time to review AXA’s 1040 Overlay program. It can provide another method of opening up the planning discussion.

* https://faq.ssa.gov/
Appendix: Social Security Planning with Life Insurance Sales Guide

As mentioned within this document, recent surveys indicate that many Americans have little idea of what they may be entitled to receive from Social Security. Those clients will have no idea of the significance that Social Security may play in their retirement and estate plans or the gap that might exist. If they wait until it is too late, they will be unable to effectively address their ultimate retirement needs.

What follows is a “primer” of the major points to consider when addressing the impact of Social Security with your clients.

Qualifying for Social Security Benefits?

Not all workers qualify to receive Social Security benefits. Those who have been employed by the Federal Government or State Governments may be covered by other retirement funding arrangements. This group generally includes teachers in the public school systems. As a general rule, American citizens and resident aliens who have contributed into the US Social security system during their working years can qualify for Social Security benefits. Workers who have “40 quarters” (10 years) of participating years can qualify for some benefit amount on their own. Spouses and divorced spouses may also be eligible for benefits through their spouse or former spouses. Identifying your clients’ occupation, work history, employer and marital history can be helpful in assessing their Social Security profile and eligibility for benefits.

Understanding the Basics

During working years, both covered workers and their employers contribute to Social Security on a covered worker’s behalf. Currently 6.2% of earned income, up to the annual “Social Security Contribution Base”, is withdrawn from each paycheck along with state and Federal income taxes. Employers and covered workers contribute a like dollar amount on behalf of the employee. Self-employed persons contribute to both the employer and employee portions, 12.4%.
Understanding the Process

In working with Social Security, there are certain basic terms that someone needs to know in accessing and understanding Social Security retirement benefit amounts.

– Full Retirement Age:

Full or normal retirement age (FRA) refers to the age at which the participant will be eligible to receive 100% of their Social Security benefit. The FRA varies based on the date of birth of the participant. As example, for a covered worker born between 1943 and 1954, age 66 is the FRA. If a covered worker was born after 1960, their FRA is age 67. For birth years between 1955 to 1960, the age at which full retirement benefits are payable increases gradually to age 67. The following chart provides full retirement for given ages and demonstrates the phase for those gap years. As you can see, a covered worker becoming age 66 this year is entitled to receive 100% of their “primary insurance amount.”

– Primary Insurance Amount (PIA):

The “primary insurance amount” (PIA) is the benefit a covered worker would receive if they elect to begin receiving retirement benefits at their “full retirement age”, FRA. If benefits begin at the full retirement age, the benefit amount is neither reduced for early retirement nor increased for delayed retirement. A special calculation formula is applied to the income levels that a covered worker was taxed on during their working years. The formula indexes the income amounts for inflation to arrive at the PIA. In 2018, the maximum PIA amount is $2,681 per month or $32,169 per year.

– Early Entry:

If a covered worker applies for Social Security benefits before their Full Retirement Age (FRA), their benefit will be less than 100% of the amount available at their FRA. A covered employee’s benefit is reduced by about one-half of one percent for each month they start to receive their Social Security benefit before their FRA. For example, if a covered employee’s full retirement age is 66, and they sign up for Social Security when they are 62, they would only get 75 percent of their primary insurance amount.

Additionally, it is important to note that if a covered employee starts receiving benefits prior to their FRA and they continue to work, not only are their benefits reduced for early entry into the system, their benefit may also be reduced $1 for each $2 dollars earned until they reach their FRA, if their earned income exceeds an earnings threshold. In 2018 that earnings threshold is $17,040.
**Deferred Entry:**

In contrast to early entry, if a covered employee defers receipt of their benefit to a year after FRA, up to age 70, their benefit will be increased by 8% of their PIA at their FRA for each year deferred. How much it will differ depends on the number of gap years. As an example, if normal retirement age is 67, applying for a benefit at age 62 results in a reduction of benefit amount by 30%. In contrast, delaying receipt of a benefit until age 70 will increase the benefit to 124% of the primary insurance amount.

### Percentage of Social Security Benefits

<table>
<thead>
<tr>
<th>Eligible Retirement Age</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>62</td>
<td>70%</td>
</tr>
<tr>
<td>63</td>
<td>75%</td>
</tr>
<tr>
<td>64</td>
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<td>68</td>
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<tr>
<td>69</td>
<td>116%</td>
</tr>
<tr>
<td>70</td>
<td>124%</td>
</tr>
</tbody>
</table>
Divorced spouses
Divorced spouses may also have rights to a “spousal benefit” through any of their former spouses, where the divorced spouse:

- Had been married for 10 years
- Is unmarried at the time of filing for benefits,
- Is age 62 or older,
- Has divorced for two years or more from the eligible participant,
- Has an ex-spouse who is entitled to Social Security retirement benefits, and
- The benefit they are entitled to receive based on their own earnings record is less than the benefit they would receive based on their ex-spouse’s benefit base referred to as the Primary Insurance Amount (PIA).

Where you are working with divorced clients who fit the profile listed above, these rules can be important to you as part of the overall retirement plan.

Earned income & its effect on early social security benefits
Earned income will not have a direct impact on the SS benefit amount of an eligible recipient that continues to work after their Full Retirement Age (FRA). However, if someone has earned income and elects to begin their Social Security retirement benefit prior to their FRA, their benefits may be subject to an additional reduction until they do reach their FRA.

As an example, for someone born between January 2, 1943, through January 1, 1955, their FRA for Social Security retirement benefits is age 66. Someone who reaches normal retirement age or is older, may collect 100% of their Social Security benefit amount, no matter how much they earn. However, for those triggering a benefit prior to normal retirement age and have not yet reached their FRA, there is a limit to how much they can earn and still currently receive full Social Security benefits.

During 2018, those who:
- are receiving Social Security retirement benefits, and
- have not yet reached their FRA, and
- have earned income in excess of $17,040.

Their annual benefit will be reduced $1 for each $2 they earn above the $17,040 threshold (2018). If they reach FRA during 2018, the reduction changes to a $1 reduction for every $3 earned in excess of $45,360 [or $3,780 per month]. The year following their FRA the reduction no longer applies at all.
Income Taxation of Social Security Benefits

Some recipients of Social Security retirement benefits will have to pay Federal income taxes on their Social Security benefits themselves. This will occur if they have other substantial income (such as wages, self-employment, interest, dividends and other taxable income that must be reported on your tax return) in addition to their Social Security benefits. Note: Life insurance accumulations can be accessed through withdrawals and loans and properly structured will not trigger current income taxes.

It should be noted that earned income delays the receipt of some benefit amounts. But once the participant reaches FRA, the Administration will re-calculate their benefit amounts and give them credit for the benefit amounts withheld.

If a Social Security recipient:

Files a Federal tax return as an “individual” and their “combined income” is:

• between $25,000 and $34,000, they may have to pay income tax on up to 50 percent of their benefit amount.
• more than $34,000, up to 85 percent of their benefits may be taxable.

Files a joint return, and they and their spouse have a “combined income” that is:

• between $32,000 and $44,000, they may have to pay income tax on up to 50 percent of your benefits
• more than $44,000, up to 85 percent of their benefits may be income taxable.

No one pays Federal income tax on more than 85 percent of his or her Social Security benefits based on Internal Revenue Service (IRS) rules.

Consider the following sample cases.
Social Security Planning Case Studies

Case Study #1 Benefit Timing – can be affected by a client’s age, income from unrelated sources

a. Eligible Participant Profile
   • Mark is 60 and reviewing his Social Security options with his financial advisor.
   • He is married and currently both he and his spouse are both working.
   • His “full retirement” age is 66.
   • His “primary insurance amount” at NRA is projected to be $2,500 per month, $30,000 per year.

b. Timing
   If he starts benefits at age 62, his benefit will be reduced below the PIA amount by 25%, to $22,500 per year. If he defers until age 70, his benefit will increase by 32% of the PIA, to $39,600 per year.

c. Taxation
   Mark’s Social Security benefits may be subject to income tax if they exceed the stated income thresholds.
   For an eligible participant that is married filing a joint return and the couple has a combined income that is:
   • Between $32,000 and $44,000 of income, they will have to pay income tax on up to 50 percent of their benefits
   • More than $44,000, up to 85 percent of their benefits may be taxable.

Mark plans to continue to work after his FRA. The couple’s “combined income” is expected to be $100,000 which exceeds the higher $44,000 threshold. At this income level $25,500 of Mark’s $30,000 annual benefit would be subject to income tax. That is 85% of the $30,000 because of his income level. Assuming a 25% marginal income tax bracket, Mark’s after tax benefit is reduced to from $30,000 to $23,625.

d. Earned Income reduction for benefits received prior to FRA
   What if Mark triggers his Social Security benefits at age 62, prior to his FRA and continues to work? His PIA amount is $30,000 at age 66.
   • At age 62 his benefit would be reduced to $22,500.
   • Since 62 is less than his FRA, all earned income in excess of the annual threshold, will be reduced $1 for every $2 earned. The income threshold in 2015 is $15,720. In Mark’s case we will assume earned income of $50,000.
   His Social Security benefit received at age 62 would be reduced by $17,140( $50,000 - $15,720 = $34,280; $34,280/2 = $17,140) leaving him with only $5,360 for the year or $ 446 per month before tax ($22,500 - $17,400 = $5,360).

It becomes obvious that taking an early benefit while still working will not increase Mark’s cash flow significantly and may not make sense.

Case Study #2 A Spouse’s View

It is not uncommon to find spouses who did not work outside of the home or did not have the required 40 quarters of covered earnings.

A spouse of an eligible recipient can receive up to 50% of the primary worker’s income benefit. This is in addition to the benefit received by the eligible recipient themselves.

In many cases, a spouse is fully insured under Social Security, but they are entitled to the larger of their own benefit or 50% of a spouse’s benefit.
Let's look at Bob and Sally:

a. Eligible Participant Profile

Bob and Sally are the same age and they have reached their normal retirement age

- Bob’s PIA is $2,200.
- Sally’s benefit based on her own work and earnings history is $700.
- Sally’s spousal benefit is $1,100, or 50% of Bob’s, so she will be eligible to receive $1,100, the spousal benefit, instead of $700.
- So, under these facts, Bob will receive $2,200 each month and Sally an additional $1,100 in Social Security Benefits. In addition, if Bob were to die, Sally would receive Bob’s higher benefit amount of $2,200.

b. Where a Spouse’s Own Benefit is larger

- Assume that Sally was actually entitled to $1,400 based on her own work history. Since $1,400 is greater than ½ of Bob’s benefit of $1,100 she can be qualified to receive the $1,400 monthly benefit. In addition, if Bob were to die prior to Sally, she would still be eligible to receive Bob’s higher benefit amount of $2,200 instead of her own benefit of $1,400.

Case Study #3 Divorcee’s View

Divorced spouses may also have rights to a “spousal benefit” through any of their former spouses. Mary is 66 and has reached her “full retirement age.” She has been married twice. Her second husband Jim died last year. She was married to her first husband Bill for 12 years.

- Mary’s PIA would be $1,100.
- Jim’s PIA would be $1,200.
- Bill is 66 but has not filed for Social Security. His PIA amount would be $2,663.

Mary meets the criteria for a divorced spouse to benefit from their ex-spouse’s Social Security account:

- She was married for more than 10 years to Bill
- Divorced from Bill more than 2 years ago
- She is currently unmarried
- Age 62 or older
- Her ex-spouse, Bill, is entitled to Social Security retirement and
- The benefit she is entitled to receive based on her own work is less than the benefit they would receive based on their ex-spouse’s PIA.

Mary’s Social Security benefit will either be $1,100, her PIA survivor benefit of $1,200 based on Jim’s account or $1,331, the spousal benefit as an ex-spouse on Bill’s account. She needs some guidance from her financial advisor on how to proceed in gathering the facts and applying for her Social Security benefit.

How to get started?

Hopefully these brief facts and case examples were helpful to getting your thinking on track for your clients. The Social Security Administration website offers substantial general benefit information, as well as personal planning tools to access an individual’s own benefit profile and benefit projections. See: http://www.ssa.gov/myaccount/materials.html#a0=

To understand the Social Security benefits procedure start with a review of your client’s projected Social Security retirement benefits.
Why AXA?

Life insurance is about peace of mind, security and providing for the people you care about. But we at AXA believe it’s larger than that — it’s about possibilities. Finding the right life insurance can mean finding financial protection as well as financial opportunities to help you reach your goals.

Your goals are as individual as you are. That’s why we’re committed to understanding your needs and concerns — so we can help you find strategies that are just the right for you. And we’re here to help you take the small, manageable steps that lead to financial security for you and your family.

Experience and innovation

AXA has a long history of engineering innovative financial strategies. We have been providing stability and reliability to our clients since 1859 to help them live their lives with confidence, and enable them to realize dreams for their loved ones and their legacy.

AXA Equitable and MLOA are members of the global AXA Group, one of the world’s largest insurance and wealth management organizations with assets under management totaled $584.9 billion.

The secret to AXA’s heritage of innovative strategies and dedicated client service is our talented community of employees who reflect the diversity of the world we live in. As our greatest asset, these employees are committed to understanding clients’ needs, building advanced solutions and supporting those needs with personalized next steps.

Financial strength

You want the confidence that the insurance company you choose has the financial strength to fulfill its obligation to you now and in the future. AXA Equitable Life Insurance Company (AXA Equitable) and MONY Life Insurance Company of America (MLOA), premiere providers of life insurance products, have been helping individuals reach their most important goals.

The guarantees provided in our life insurance and annuity contracts are based on the claims paying ability of the issuing insurance company either AXA Equitable Life Insurance Company or MONY Life Insurance Company of America, an Arizona Stock Corporation with its main administration office in New York, NY. AXA Equitable has consistently earned high marks by independent companies that rate insurance companies for their financial strength.