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ADVANCED PLANNING

Trust-owned annuities for a dynamic legacy

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Trust-owned annuities for a dynamic legacy

Are you interested in safeguarding your legacy as you create and pass wealth to your heirs? Protection from creditors and predators is key, and so is managing income and estate taxes. Building a diversified wealth portfolio and generating guaranteed income can be key success factors.

Why annuities?

Trusts are often part of a well-rounded estate plan for many individuals and families. However, income taxes can be a major problem for trusts. That's where annuities come in. Deferred annuities offer the power of tax-deferred growth. This allows values to grow without being reduced by the strict income tax rates applicable to many irrevocable trusts.

With a deferred annuity contract, your trustee can toggle income on and off in the annuity contract to effectively manage income and taxes. This compares favorably to many other types of investments such as stocks and bonds where current income may be difficult to avoid.

How does it work?

Your trust purchases a deferred annuity contract. This is done by your trustee, who makes investment decisions and is responsible for managing trust assets for your beneficiaries. At the time of purchase, the trustee submits a trust certification form to AuguStar® Retirement.

To receive estate tax savings and enhanced creditor protection, your trust could be an irrevocable trust. This type of trust generally places assets beyond your reach but, in doing so, also places them beyond the reach of creditors and estate taxes. Irrevocable trusts are a time-honored estate planning tool for passing and preserving multi-generational wealth.

Passing it on tax-deferred

Consider purchasing a trust-owned annuity contract for each of your trust beneficiaries. Each beneficiary would be the annuitant (the measuring life) of a separate annuity contract. At death, your trustee can distribute the annuity to each beneficiary without current taxation based on IRS Private Letter Rulings (PLRs).[1] This is called a distribution "in kind." AuguStar offers this strategy to potentially preserve ongoing tax deferral and legacy planning.

Additional considerations

A trust-owned annuity is not for everyone. It tends to work best for wealthy individuals or those in a high-risk profession who want to protect their legacy from creditors and transfer taxes.

Work carefully with your attorney and tax professional when purchasing a trust-owned annuity. Your trustee will have several factors to consider including applicable state laws and the language in your trust. In many cases, annuities are part of a well-balanced approach and will not be the only trust asset.

Not all trust-owned annuities qualify for tax deferral. Your trust should benefit individuals (not charities, family foundations, or other entities). It might be best to create one trust (or sub-trusts) for each beneficiary. At AuguStar, we require the trustee to sign a certification acknowledging their ability to seek independent tax advice regarding the trust-owned annuity contract and that AuguStar makes no representations or warranties regarding the tax treatment of the annuity.

Your trust may not be eligible for an exception to the additional 10% tax on early withdrawals from non-qualified annuities, so this strategy tends to be appropriate only as a long-term legacy or inheritance.[2] If guaranteed income for a current beneficiary is important, your trustee might instead consider a single premium immediate annuity (SPIA), as immediate annuities are exempt from the 10% early withdrawal penalty.[3]

Why are income taxes a problem for trusts?

Certain types of trusts known as "non-grantor trusts" face harsh income tax brackets when income is retained by the trust. Consider the example below using 2026 income tax rates. You'll see a married filing jointly couple doesn't hit the highest income tax bracket of 37% until they earn over $768,700 of taxable income. For a non-grantor trust, on the other hand, it hits the highest income tax bracket at over $16,000!

Married filing jointly (MFJ)		Trusts and estates	
Tax rate	**Taxable income**	**Tax rate**	**Taxable income**
10%	$0 to $24,800	10%	$0 to $3,300
12%	$24,801 to $100,800	24%	$3,301 to $11,700
22%	$100,801 to $211,400	35%	$11,701 to $16,000
24%	$211,401 to $403,550	**37%**	**Over $16,001**
32%	$403,551 to $512,450		
35%	$512,451 to $768,700		
37%	**Over $768,700**		

Table source: Internal Revenue Service. Please note this chart has been simplified and does not include a breakdown of the flat amount owed in each bracket.

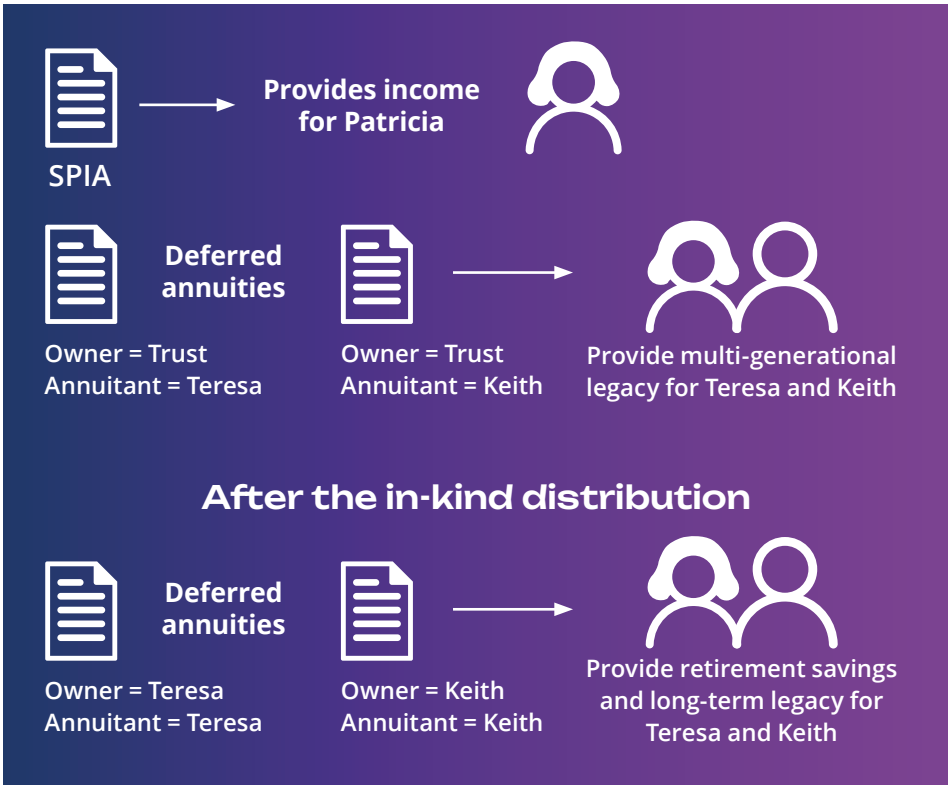
Case Study

Patricia is the income beneficiary of a family trust her husband created before his death. Their two children, Teresa (age 34) and Keith (age 29), are the remainder beneficiaries of two separate sub-trusts.

The trustee purchases a single premium immediate annuity (SPIA) structured as a life annuity to benefit Patricia. This provides her with guaranteed annual income for her lifetime and protects her as the income beneficiary. The trust has other assets to cover expenses, taxes, and obligations in the trust.

The trustee also purchases two deferred annuity contracts for Teresa and Keith. They are each the annuitant on two separate annuity contracts (one for each sub-trust). The annuity carrier permits in-kind distributions.

At Patricia's death, the trustee submits an ownership change request form, distributing the deferred annuity contracts to Teresa and Keith, respectively. It is a non-taxable event based on PLRs. The annuity contracts continue to grow on a tax-deferred basis for Teresa and Keith. This powerful planning technique saves estate and transfer taxes (via the irrevocable trust) and helps Teresa and Keith establish their own retirement savings and long-term legacy planning on a tax-deferred basis.



Powerful benefits

Estate tax management. Assets in properly structured irrevocable trusts are not subject to estate taxes. This extends to trust-owned annuity contracts.

Income tax management. Income taxes can be a major problem for irrevocable trusts. With a trust-owned annuity, the trustee can toggle income on and off when appropriate to manage taxable income.

Tax deferral. Deferred annuities receive tax-deferred growth. Trust-owned annuities generally continue to qualify for tax deferral when the trust is properly structured and is set up for the sole benefit of a natural person beneficiary (not charities or other entities).

Creditor protection. Irrevocable trusts are a time- honored planning technique for asset protection. They can be used to help shield assets from creditors, predators, and even future ex-spouses of your beneficiaries. Consult your attorney as creditor protection laws vary by state.

Control and asset management. You may have beneficiaries who need asset management and protection – sometimes even from themselves. Your trustee manages trust assets and can only make distributions based on your instructions in the trust.

Does this describe you?

Concerned about estate taxes. Your net worth is significant, and you are facing a potential estate tax challenge (federal or state).

High-risk professional. You work in a profession with high-stakes liability or are otherwise concerned about potential creditors. You are interested in carving out a portion of your wealth for asset protection.

Your heirs need retirement savings of their own. Your heirs could benefit from the tax-deferred growth of an annuity contract. Your trust could purchase an annuity contract for each trust beneficiary now. At your death, your trustee can distribute your AuguStar annuity contract to the annuitant/trust beneficiary to help jump-start their retirement savings.

Diversified trust portfolio. You recognize a well-balanced portfolio contains a variety of assets. Annuities can be designed to include guarantees to be part of a balanced investment approach.

Legacy planning matters to you. You are interested in leaving a long-term legacy for your heirs.

Get ready to launch

Trusts and annuities are two powerful planning techniques. In the right situation, pairing the two together can create dynamic results and a multi-generational legacy.

[1] This strategy is based on IRS Private Letter Rulings (PLRs). A PLR only applies to the taxpayer who requested the ruling and cannot be used as legal authority. Still, PLRs often serve as guidance for estate and tax planners because they give a glimpse into what the IRS is thinking and how it may handle similar cases. You should always work with your own tax and legal professionals in your particular case.

[2] In particular, PLR 202031008 indicated that certain trusts known as "non-grantor" trusts would not qualify for an exception to the additional 10% tax on early withdrawals at death of the annuitant) because a non-grantor trust has no age, disability status, or life expectancy.

[3] IRC Sec. 72(q)(2)(I).

This flyer provides general information that should not be construed as specific tax or legal advice nor the law of any particular state. You should seek the advice of a qualified tax or legal professional for your specific situation.

Annuities are long-term investment vehicles designed to accumulate money on a tax-deferred basis for retirement purposes. Upon retirement, annuities may provide an income stream or a lump sum. If you die during the accumulation or payout phase, your beneficiary may be eligible to receive any remaining Contract Value.

There is no additional tax-deferral benefit for contracts purchased in an IRA or other tax-qualified retirement plans because such retirement plans already have tax-deferred status. An annuity should only be purchased in an IRA or qualified plan if the contract owner values some of the other features of the annuity and is willing to incur any additional costs associated with the annuity.

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