



Beyond Annuities:
Taking clients' legacies above and beyond with trust-owned annuities

Leveraging a trust-owned annuity

Trustees have fiduciary duties, which may include selecting trust investments that:

- Help drive growth
- Preserve assets
- Maximize tax efficiency

A **trust-owned annuity** can be a powerful planning strategy to help satisfy these duties and take your clients' legacies above and beyond.

Trusts and tax drag

Trusts are a common estate planning tool for passing and preserving wealth.

However, income tax can be a major problem for non-grantor trusts due to the compressed income tax brackets that apply to trusts.



Trusts and tax drag

A non-grantor trust may owe substantially more income tax on the same taxable income relative to the income tax owed by a married couple filing jointly. **This can create a large “tax drag” on trust asset growth, which reduces the amount of assets available to trust beneficiaries.**

| Married (filing jointly) | | Estates & trusts | |
|---------------------------|------------|--------------------------|------------|
| \$0-\$23,200 | 10% | \$0-\$3,100 | 10% |
| \$23,201-\$94,300 | 12% | \$3,100-\$11,150 | 24% |
| \$94,301-\$201,050 | 22% | \$11,151-\$15,200 | 35% |
| \$201,051-\$383,900 | 24% | | |
| \$383,900-\$487,450 | 32% | | |
| \$487,451-\$731,200 | 35% | | |
| \$731,201 and over | 37% | \$15,201 and over | 37% |

*Source: Internal Revenue Service. Information is current as of 1/31/24, and subject to legislative changes.

Why use annuities in trusts?

This tax drag can create a dilemma for the trustee, who must choose between:

1. Keeping the income in the trust, which would subject that income to the compressed trust income tax brackets, and
2. Distributing the income to a trust beneficiary, which may be impermissible or imprudent under the terms of the trust.



Why use annuities in trusts?

Under Internal Revenue Code Sec. 72(u)(1), a trust that solely benefits living individuals can purchase an annuity and take advantage of tax deferral.

This deferral allows the annuity investment to grow tax-deferred, which may result in a larger inheritance for trust beneficiaries over time.



The pass-in-kind opportunity

A **pass-in-kind annuity strategy** is a way to transfer an annuity contract from a trust to a beneficiary of that trust without a taxable event.

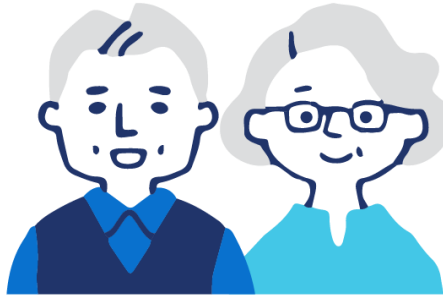
Under Private Letter Ruling 19990501512¹, the IRS allowed a non-grantor trust to **transfer ownership of a deferred annuity in-kind** to a trust beneficiary when the distribution is permitted by the trust.

If the beneficiary is a living person with a beneficial interest in the trust, **no tax reporting** is required for this change in annuity ownership.

¹ Only the taxpayer who obtains a PLR can rely upon it as legal authority. However, PLRs do provide insight into how the IRS may rule in similar situations.

Case study:

Using the annuity pass-in-kind strategy with a credit shelter trust



Gary and Helen create an estate plan that includes an A/B trust.

A credit shelter trust, or a “B” trust, is a sub trust that may be funded after the death of the first grantor spouse for estate and tax planning purposes.

Case study:

Using the annuity pass-in-kind strategy with a credit shelter trust

When Gary dies, the B trust may be funded, with Helen as the income beneficiary and their daughter, Megan, as the remainder beneficiary.

Helen has a right to trust income during her lifetime. However, Gary and Helen hope for the money to grow and benefit Megan once Helen passes.



Gary passes away and the B trust is funded.

Case study:

Using the annuity pass-in-kind strategy with a credit shelter trust

The trustee of the B trust purchases a nonqualified annuity with Megan named as the annuitant.² Helen could trigger a distribution from the annuity by directing the trustee to make a withdrawal, but she chooses not to do so.



The trustee of the B trust purchases a nonqualified annuity.



Owner: Trust
Annuitant: Megan
Beneficiary: Trust

² If the trust were to name Helen as the annuitant, distributions from the annuity would be required on Helen's death by Internal Revenue Code Sec. 72(s). Naming Megan as the annuitant would make it less likely that distributions from the annuity to the trust will be required.

Case study:

Using the annuity pass-in-kind strategy with a credit shelter trust

Under the provisions of the trust, when Helen dies the trust terminates and the annuity contract will **“pass-in-kind”** to the remainder beneficiary, Megan.

At that time, the annuity contract is retitled from the trust as owner to Megan as owner. This transfer is not a taxable event and thus tax deferral may continue.



Helen passes away, but because Megan is the annuitant, no death benefit is triggered.

Case study:

Using the annuity pass-in-kind strategy with a credit shelter trust

Megan can continue to defer taxes until she takes income from the annuity.

This results in certain tax benefits, including:

- The ability to control the amount of income taken each year
- The ability to recognize that income at her individual tax bracket.



Ownership of annuity transferred to Megan; full tax deferral maintained.

Put a trust-owned annuity to work for your clients

While the pass-in-kind strategy doesn't work for every trust, it could benefit individuals who desire the control and flexibility to pass their legacy on to their heirs as tax efficiently as possible.

Clients should work carefully with their attorney and tax professional to determine whether a trust-owned annuity makes sense for their specific situation.



At MassMutual Ascend, we are committed to going above and beyond – so when it comes to your clients' financial futures, the impossible feels possible.

Talk to your clients today about how a trust-owned annuity can be a powerful planning strategy to support their legacy and estate planning goals.

The above information is illustrative only. It has not been tailored for any individual and does not constitute a recommendation to engage in or refrain from a particular course of action.

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