



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

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# Leveraging a trust-owned annuity

Today’s increasingly complex economic landscape makes the responsibilities of a trustee more challenging than ever. Trustees have fiduciary duties, which may include selecting trust investments that help drive growth, preserve assets and 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.

Let’s consider the 2024 income tax rates. A married couple filing jointly doesn’t reach the highest tax bracket of 37% until their taxable income exceeds \$731,200. But a non-grantor trust reaches the top income tax bracket when its taxable income exceeds \$15,200. Therefore, 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%		
<b>\$731,201 and over</b>	<b>37%</b>	<b>\$15,201 and over</b>	<b>37%</b>

\*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 keeping the income in the trust, which would subject that income to the compressed trust income tax brackets, and distributing the income to a trust beneficiary, which may be impermissible or imprudent under the terms of the trust.

However, 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.<sup>1</sup> This deferral allows the annuity investment to grow tax-deferred, which may result in a larger inheritance for trust beneficiaries.

## 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 1999050151<sup>2</sup>, 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. Regardless of the reason for the transfer, 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.



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## Case study:

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

The following hypothetical example illustrates how leveraging a trust-owned annuity can help create a legacy that goes above and beyond.

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

The trustee of the B trust purchases a nonqualified annuity with Megan as the annuitant.<sup>3</sup> Helen could trigger a distribution from the annuity by directing the trustee to make a withdrawal, but she chooses not to do so.<sup>4</sup>

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.<sup>5</sup>

Megan can continue to defer taxes until she takes income from the annuity. This results in several tax benefits, including the ability to control the amount of income taken each year, and to recognize that income at her individual tax bracket.

**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.



Gary passes away and the **B trust is funded**.



The trustee of the B trust purchases a nonqualified annuity.



**Owner:** Trust

**Annuitant:** Megan

**Beneficiary:** Trust



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



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 high-net worth 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.



## Connect with us

Trust-owned annuities can be a powerful planning strategy to support your clients' legacy and estate planning goals.

Connect with the MassMutual Ascend sales team for more information.



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<sup>1</sup>Annuities owned by trusts that benefit non-natural entities, businesses, or charities will not receive tax deferral.

<sup>2</sup>A PLR only applies to the taxpayer who requested the ruling and cannot be used as legal authority. But, PLRs do provide insight and guidance into how the IRS may rule in similar situations.

<sup>3</sup>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.

<sup>4</sup>Under Internal Revenue Code Section 72(q), any taxable distribution from an annuity is subject to an additional 10% federal tax.

<sup>5</sup>IRS PLR 199905015 says that an annuity owned by the credit shelter trust is deemed to be owned by a living person, and when the trust dissolves, the retitling of the annuity contract from the trust as owner to the annuitant as owner doesn't trigger a taxable event.

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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