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The Basics of a Fixed Annuity

Tax Deferral and Guaranteed Interest

What is a Fixed Annuity?

A fixed annuity is basically a contract between you and an insurance company under which you agree to make payments to the insurance company—known as purchase payments—in exchange for which the insurance company agrees to apply a minimum guaranteed interest rate¹ to your annuity contract and make payments to you at a later time. There is no limit to how much you can contribute², and your purchase payments can be a single payment or flexible payments over the course of many years. You can receive your distribution from a fixed annuity in one lump sum, or you can choose to annuitize. If you annuitize, the insurance company pays you a regular income, usually on a monthly basis. Whatever payout option you select, the interest gains and payment amounts are guaranteed¹ by the insurance company. Fixed annuities generally carry a surrender charge for early withdrawals that usually declines to zero after a specified number of years.

The Tax Advantage

Unless made to a qualified retirement plan such as a 401(k), 457(b) or 403(b) plan, contributions are not tax deductible, but all earnings accumulate tax-free until money is withdrawn. Whenever money is taken out, it is taxed as ordinary income. However, for payouts from a fixed annuity held outside of a qualified retirement plan, only the portion of the payout that is considered income is taxed.

Interest Rate Crediting

Insurance companies typically apply a number of different interest rates over the life span of a fixed annuity. Many offer a higher interest rate in the first year. After that, rates are periodically readjusted based on market conditions, often with an underlying guaranteed minimum rate. A fixed annuity contract might also feature extra interest crediting during the surrender period or for new premiums. See the graphic above for an illustration of how these types of interest are applied to a typical fixed annuity contract.

Other Fixed Annuity Features

Fixed annuity contracts may include provisions for loans to the contract holder or partial withdrawals with no penalty imposed by the insurance company. However, tax considerations would still apply. Other features often found in fixed annuity contracts include:

- A guaranteed return of purchase payments or principal¹ upon surrender or as a death benefit
- Special provisions if you are admitted to a nursing home or diagnosed with a terminal illness
- A guaranteed lifetime income option^{1,3}

1. Guarantees and benefits are subject to the claims-paying ability of the underlying insurance company.
2. When used in a qualified retirement plans such as a 401(k), 457(b) or 403(b) plan, contributions to a fixed annuity are subject to an annual limit set by the IRS.
3. Other income options available. Restrictions apply.

Hypothetical Life Span of a Fixed Annuity

YEARS 1-7							
INTEREST RATE:	5%	— ADJUSTS PERIODICALLY, MINIMUM 2% —					
YEAR:	1	2	3	4	5	6	7
SURRENDER FEES:	7%	6%	5%	4%	3%	2%	1%

YEARS 8-15							
INTEREST RATE:	— ADJUSTS PERIODICALLY, MINIMUM 1% —						
YEAR:	8	9	10	11	12	13	14
SURRENDER FEES:	0%	0%	0%	0%	0%	0%	0%

For Illustration Purposes Only



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All information should be carefully considered before investing. Withdrawals from annuities, including partial withdrawals and surrenders, may be taxable. If you take a taxable withdrawal before age 59½, you may have to pay a 10 percent penalty to the IRS in addition to your normal income taxes. Purchasing an annuity within a retirement plan that already offers tax deferral results in no additional tax benefits.

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