Five unexpected ways to use an annuity

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Many people looking to grow their retirement savings and turn that nest egg into an income stream in the future choose to add annuities to their overall retirement income plan. These insurance contracts offer growth potential and the option for guaranteed income. While annuities are traditionally used as a reliable source of retirement funds, there can be other ways to use this money. Whether you want to access your savings before retirement or no longer need supplemental income as a retiree, here's a look at surprising uses for an annuity.

Can I cash out an existing annuity?

It is possible to cash out or withdraw money from many annuities, especially if income payments have not yet begun. But withdrawals may come with a fee. Some retirees may have other reliable income sources or want flexibility and must maintain access to their funds. However, depending on a person's age and how close they are to retirement, taking early withdrawals or cashing out an annuity could hinder future goals. Options for accessing funds from an annuity include:

Withdrawals

Some annuities offer an annual penalty-free withdrawal amount[1], while others have specific features that can trigger additional liquidity options if certain conditions are met, like an extended nursing home stay.

Loans

Instead of cashing out an annuity, a loan against the cash value of the annuity contract may be an option. A loan may be needed for an emergency, medical expenses, or home repair.

Surrender

Someone may terminate their annuity contract before the payout period. However, there may be a fee if funds are withdrawn before a predetermined date, known as the surrender period.

Other uses for an annuity

Along with providing retirement income, an annuity can be a versatile solution that can help meet several other needs. A retiree may no longer need to supplement their retirement income plan and wish to find other uses for their annuity. Annuities can be used for long-term considerations like life insurance or healthcare and to secure a stable legacy for potential heirs and causes close to their heart.

Gifting an annuity to loved ones or a good cause

A charitable gift annuity is a contract between a donor and a qualified charity and can be an option for someone who wishes to donate to a favorite cause. Often called a "split gift," part of the donation is used by the charity and part of the gift is set aside to provide income payments to the donor and/or their beneficiary for the rest of their lives. A charitable gift annuity may be a good choice if a person is looking for a charitable tax deduction but also wants to have retirement income they can count on later in life. It's important to speak with a tax professional about this strategy's tax deductions and possible benefits.

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Gifting an annuity to a family member

An annuitant may also have the option to gift their annuity, or change the owner of the contract, to a family member or other beneficiary. The new owner takes control of the annuity and its benefits. If the annuity is in the accumulation phase when it is gifted, taxes on any gains will likely need to be paid. However, waiting until the annuity's payout phase before it is gifted can provide a tax-free source of lifetime income for the recipient.

Gifting an annuity can be a generous and beneficial gesture, but it's important to approach it with careful consideration and to seek professional advice to ensure it's the right choice for both you and the recipient.

Placing an annuity in a trust

As part of a comprehensive estate planning strategy, placing an annuity in a trust can provide control over how the annuity proceeds are distributed and protected and may help minimize estate taxes. This can be particularly useful for ensuring the funds are used for specific purposes, such as providing for a beneficiary's long-term financial security or ensuring they receive regular income.

Repurposing an annuity for long-term care

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Thinking through an annuity for Medicaid planning

Certain types of annuities are considered Medicaid compliant, where income from that annuity is not counted toward the asset limit to qualify for Medicaid. To be eligible for Medicaid long-term care, applicants must have a limited amount of assets. A Medicaid Compliant Annuity (MCA) is one planning option that can potentially lower total assets, where countable assets are converted into non-countable or exempt assets. Since this money is turned into an income stream, it does not count against the asset limit to apply for Medicaid.

Opting for an annuity maximization strategy

To maximize annuity dollars, one strategy is to purchase a life insurance policy with the annuity funds. The beneficiaries of the policy would then be paid a generally tax-free death benefit and avoid the taxes associated with inheriting annuity funds. Annuities are subject to income taxes and estate taxes after the owner dies, so the annuity cash value could be severely reduced after beneficiaries are hit with tax liabilities. Life insurance, on the other hand, provides a generally income tax-free death benefit and can be structured to be excluded from the taxable estate — helping to maximize the value to one's heirs.

Understanding annuities

Annuities can be a valuable solution that meets a variety of needs and helps round out a comprehensive financial plan. On top of providing guaranteed income for retirement, annuities can grow assets to pass on to beneficiaries and potentially offer funds for unexpected events. A financial professional can help you explore your options and how to address more complex needs to get you on your way to a happy retirement.

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Ratings are subject to change.

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[1] Withdrawals taken prior to age 59 1/2 may be subject to IRS penalties.

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