

*a. Deemed Payments Resulting from Gifts*¹⁵

An owner who assigns or pledges a portion of the value of the PPVA will be treated as receiving an unscheduled, non-annuity distribution under the contract.¹⁶ If an owner of the PPVA transfers it without receiving full and adequate consideration, the owner will generally be treated as receiving the excess of the cash surrender value of the PPVA over the holder's investment in the PPVA as an unscheduled, non-annuity distribution.¹⁷ An exception applies for transfers between spouses or transfers incident to a divorce.

3. 10% Penalty for Early Withdrawal

If a distribution is made prior to the date that the owner of the PPVA reaches the age of 59 ½, an additional 10% tax penalty will be imposed on the amount includible in gross income.¹⁸ Certain exceptions apply. For example, the penalty does not apply if the distribution is made on or after the death of the holder (or, if the holder is not an individual, the death of the primary annuitant). The penalty also does not apply to a payment upon the total and indefinite disability of the recipient. An exception also exists for distributions that are part of a series of substantially equal periodic payments made for the life of the taxpayer or the joint lives of the taxpayer and his beneficiary. In such cases, the 10% penalty also does not apply.

4. Required Distributions upon Death of Owner

If an owner of the PPVA dies before the annuity starting date, under section 72(s) of the Code the entire interest must be distributed within either (1) five years after the death of the owner, or (2) the life of the designated beneficiary or a period not extending beyond the life expectancy of such beneficiary, but only if the owner's interest is payable to or for the benefit of a designated beneficiary. An exception exists for a spouse that is the designated beneficiary. In such case, no distribution is required and the spouse is treated as the holder of the annuity contract.¹⁹ If the owner of the annuity dies on or after the annuity starting date and before the entire interest on the annuity has been distributed, the remaining amount due on the annuity must be distributed at least as rapidly as under the method of distributions being used as of the date of death.²⁰

5. Gain or Loss upon Sale of PPVA

Gain or loss is generally recognized if an owner of a PPVA sells or otherwise disposes of the annuity other than by electing a settlement option.²¹ An exception exists for certain exchanges of an annuity contract for another annuity contract involving the same annuitant through section 1035 of the Code.

¹⁵ Pledging an annuity as collateral for a loan could also have tax consequences but such a pledge is not anticipated for the PPVAs.

¹⁶ I.R.C. § 72(e)(4)(A).

¹⁷ I.R.C. § 72(e)(4)(C)(i).

¹⁸ I.R.C. § 72(q).

¹⁹ I.R.C. § 72(s)(3).

²⁰ I.R.C. § 72(s)(1)(A).

²¹ I.R.C. § 1001(a).