

Pursuing Higher After-Tax Portfolio Returns

How a low-cost deferred variable annuity can increase tax efficiency

Typically, high-net-worth investors (those with household liquid assets of at least \$1 million) and sometimes upper-tier mass affluent investors (at least \$500,000) hold the bulk of their liquid investments in taxable accounts, rather than tax-advantaged accounts such as 401(k) plans, IRAs, 529s, etc. These investors are usually also subject to relatively high marginal income tax rates, which means most could benefit greatly by deferring taxes on any investment that generates large distributions that can be taxed at ordinary income rates, such as short-term capital gains and/or certain types of interest and dividends.

One way to defer these taxes is by replacing those investments held in taxable accounts with suitable alternatives held in tax-advantaged accounts. Of course, to the extent that you can fund employer plans, IRAs, and similar accounts, it probably makes sense to do so before considering other options. But if you have most of a client's portfolio invested in taxable accounts, these accounts can only go so far, because of certain limitations on tax-advantaged accounts. Even if your client is eligible to make contributions to a tax-advantaged account, the investment options they offer may not be comparable to what is offered in a taxable account.

A tax-deferred variable annuity such as the Fidelity Personal Retirement Annuity^{®1} (FPRA), however, may give your clients investment options you want them to have with the tax-deferred advantages they need. Best of all, there are no IRS limits on contributions, so your clients can save as much as they want.²

¹ Fidelity Personal Retirement Annuity (Policy Form No. DVA-2005 et al.) and, for New York residents, Personal Retirement Annuity (Policy Form No. EDVA-2005 et al.). **Fidelity Brokerage Services, Member NYSE, SIPC**, and Fidelity Insurance Agency, Inc., are the distributors.

² Fidelity reserves the right to limit contributions.

Insurance products are issued by Fidelity Investments Life Insurance Company (FIL) and, in New York, by Empire Fidelity Investments Life Insurance Company,[®] New York, N.Y. FIL is licensed in all states except New York. The contract's financial guarantees are solely the responsibility of the issuing insurance company.

This material should not be considered investment, tax, or legal advice. You should consult with your financial, tax, and/or legal advisor to assess your individual situation.

Inside:

Five questions to help you determine whether the Fidelity Personal Retirement Annuity [®] could be right for your high-net-worth clients.	2
A guide to the potential tax efficiency of equity investments	3
The importance of low annuity costs for tax-efficient redistribution	3
How much could the Fidelity Personal Retirement Annuity potentially save your clients?	4



Five questions to help you determine whether the Fidelity Personal Retirement Annuity® could be right for your high-net-worth clients.

1. Do your clients have large holdings in tax-inefficient assets? New research shows that certain investors with “highly tax-inefficient assets” may benefit greatly from a low-cost tax-deferred annuity. Tax-inefficient assets can be defined as those that tend to deliver most or all of their total return in forms that are heavily taxed. Some examples are shown in the following chart.

TAX-INEFFICIENT ASSETS:

Most fixed-income investments	Almost all fixed-income investments other than municipal bonds and U.S. Savings Bonds are highly tax inefficient. Potentially higher-returning, more volatile types of fixed-income investments (such as U.S. high-yield bonds and emerging markets debt) are the most tax inefficient.
Certain equity investments	While some equity investments are very tax efficient, with minimal distributions over long periods, others, especially those with large and regular distributions that are taxed as ordinary income, like short-term capital gains, would be considered very tax inefficient. The chart on the next page describes equity investments that might benefit from transitioning into a low-cost tax-deferred annuity, like the Fidelity Personal Retirement Annuity.

2. Are your clients subject to a high marginal income tax rate? Generally speaking, the higher the marginal income tax rate, the more likely a client should consider the potential benefit from the tax deferral offered by a tax-deferred investment such as the Fidelity Personal Retirement Annuity. As a rule of thumb, clients in the two top federal income tax brackets (currently 33% and 35%) may fit this description. Also, in some cases—depending on the states where your clients live—even those in the lowest federal tax bracket may still be subject to a combined marginal income tax rate that is relatively high. Residents of New York City, for example, often fit this description.

In addition, allocating assets to a tax-deferred annuity may help reduce a client’s yearly income taxes, which may help him or her avoid the alternative minimum tax.

3. Do your clients expect lower income taxes in retirement? There are many reasons why clients may be looking at lower income taxes in retirement, including:

- Plans to move or retire to a state that has much lower taxes than their current state
- Expecting to earn less ordinary income than in previous years

If either of these situations applies to your clients, then an annuity could potentially not only defer but also help reduce taxes over the long run—especially if they plan to make Roth 2010 IRA conversions from qualified retirement accounts, in which case distributions would be tax free in retirement.

4. Do you hold significant liquid assets for clients in taxable accounts? If you have a significant amount of your clients’ liquid assets in taxable accounts, or are likely to see sizable increases in their taxable accounts in the future, they may benefit from tax deferral.

5. Are your clients at least 10 years away from taking income in retirement? Of course, the advantage of tax deferral is proportional to the amount of time available before the assets are withdrawn from the deferred account. In general, if your clients have at least 10 years remaining before retirement, they may be good candidates for the Fidelity Personal Retirement Annuity. However, if you are planning to use an income bridge for a client (such as a bond ladder or period-certain annuity) to cover all expenses during the early part of his or her retirement, that client may benefit from a Fidelity Personal Retirement Annuity even if retirement is closer than 10 years away.

A guide to the potential tax efficiency of equity investments

While no indicator of the future tax efficiency of equity investments can be 100% accurate, the list below is generally reliable. Of course, you should always consider the potential tax implications of selling a client's assets in a taxable account to purchase a tax-deferred annuity, as redemptions from the taxable account may result in capital gains, and those taxes may overwhelm any potential deferral benefit. Please note: Deferred variable annuities have additional expenses not found in taxable accounts, which can impact performance.

EQUITY TYPE	TAX EFFICIENCY
Real Estate Investment Trusts (REITs) and REIT funds	Since REITs are required to distribute nearly all of their earnings and they're distributed in the form of ordinary income, REITs and REIT funds are generally among the most tax inefficient of all equity investments. They should be among the very first equity assets considered for replacement in a tax-deferred annuity.
Small-cap funds relative to large-cap funds	Because small stocks that grow tend to leave small-cap indexes and therefore need to be sold by small-cap funds, as a rule small-cap funds see higher levels of capital gain distributions—and thus lower levels of tax efficiency than do otherwise similar large-cap funds.
High-yielding equities and funds (future tax considerations)	Although most high-yielding common stocks, such as utilities, are currently tax efficient, the scheduled expiration of the 2002 tax law that created qualified dividends could change that—and investments such as utilities funds would likely then become very tax inefficient.
Indexed and tax-managed equity funds	With few exceptions, indexed equities are very tax efficient. However, REIT index funds are very tax inefficient, and small-cap index funds tend to be less efficient than large-cap funds. Explicitly tax-managed equity funds also tend to be fairly tax efficient.
Separately Managed Accounts (SMAs)	If an SMA is managed with an eye to tax efficiency, it's certainly possible to harvest tax losses and use these to offset gains. Otherwise they may be no more tax efficient than an ordinary actively managed equity mutual fund.

Note: Lower maximum tax rates on capital gains and dividends would make certain equity funds less tax inefficient, and reduce the potential deferral benefit of investing in a tax-deferred account.

The importance of low annuity costs for tax-efficient redistribution

In the past, advisors may not have considered a deferred annuity as an option to gain more tax efficiency for their clients because of the high fees associated with these types of investments. Today, the Fidelity Personal Retirement Annuity is changing that thinking.

While the industry average deferred variable annuity still has an annual annuity charge of 1.37% in addition to the fund fees, the Fidelity Personal Retirement Annuity has an annual annuity charge of just 0.35%. (Of course, annuities should not be compared on their fees alone, especially to the extent that death benefits and living benefits are important to the investor. One reason Fidelity Personal Retirement Annuity's fees are lower is that, unlike some other deferred annuities, FPRA does not provide a guaranteed minimum death benefit.) The effect of this difference in fees on the tax deferral, however, is significant. In all cases, the benefit of deferral is reduced by fees, but in some situations, and particularly with lower-yielding investments, some of the benefits gained through the use of a deferred annuity may be reduced or even totally overwhelmed by the effects of fees when the industry-average 1.37% fee level is applied. Obviously, a fee of only 0.35% could make a big difference in an annuity's total return, especially when compounded over time.

How much could the Fidelity Personal Retirement Annuity potentially save your clients?

This report summarizes new research that shows that, in the right circumstances, selling tax-inefficient assets within a taxable account and using the proceeds to invest in similar funds within a variable annuity can be an effective part of an overall plan to increase the tax efficiency of a client's portfolio. It also explains how costs associated with that annuity can have a significant impact on the overall effectiveness of this effort. How much your individual clients could save with the right annuity will depend on their particular circumstances.

Of course, if you choose to seek greater tax efficiency for your client by purchasing an annuity, you'll want to be sure that the annuity you choose has the appropriate investment options available to replace the tax-inefficient assets held in your client's taxable account. So with more than 50 investment options in 15 different asset classes available to you, there's even more reason to give the Fidelity Personal Retirement Annuity a closer look.*

The bottom line? If you have clients with substantial assets in taxable accounts, we can show you how you may be able to gain significant tax savings for them by increasing the tax efficiency of their portfolio through our low-cost Fidelity Personal Retirement Annuity. Speak with your Fidelity Advisor Relationship Management Team today at 800.910.7899.

For more information on how a tax-deferred annuity could potentially help your clients, please contact your Fidelity Advisor Relationship Team at **800.910.7899**.

Fidelity Investments
Life Insurance Company



900 SALEM STREET
SMITHFIELD, RI 02917

Before investing, consider the investment objectives, risks, charges, and expenses of the fund or annuity and its investment options. Call or write to Fidelity or visit Fidelity.com for a free prospectus containing this information. Read it carefully.

***Note that while a fund in an annuity may be in a similar category as the fund sold from a taxable account, it will almost certainly not be the same fund and therefore its pretax performance will differ, potentially by a significant margin.**

Before purchasing the Fidelity Personal Retirement Annuity, there are a number of important factors that need to be reviewed with a licensed agent to determine if a deferred variable annuity is suitable.

Principal value and investment returns of a variable annuity will fluctuate and there may be a gain or loss when money is withdrawn.

Bond prices rise when interest rates fall, and vice versa. This effect is usually more pronounced for longer-term securities.

Lower-quality or high-yield securities carry greater risk than investment-grade securities. Equity investments involve more risk because their value will fluctuate according to their performance. Investing in small-cap stocks may have a greater risk because they are subject to abrupt or erratic price fluctuations.

For investment professional use only.

534365.2.0

1.905561.100