

# Important Information About Variable Annuities

## Introduction

A variable annuity is a contract between an investor and an insurance company. Variable annuities combine some of the features commonly found in life insurance and mutual fund investments, and also have additional unique features. In general, an annuity allows you to invest money with an insurance company on a tax-deferred basis, and arrange for a regular stream of income payments, usually after you reach retirement age. Annuities can also provide guaranteed payments to your spouse or beneficiary upon your death.

Many Americans have used variable annuities as part of their overall retirement and investment strategy. A variable annuity is not the right investment choice for everyone, however. When you buy a variable annuity, there are a number of features and options that can be used to help you address your financial goals. These features also carry associated costs that can affect the value of your investment. Variable annuities are often invested in the stock market, and the value of your investment will vary depending on the performance of the investment options you choose. Although they come with certain guarantees, annuity investments involve investment risk, including the possible loss of principal.

Before you invest, you should take the time to learn about the features of variable annuities so you can decide whether a variable annuity is right for you. In particular, you should understand how you will benefit from the particular features of an annuity, and how the various risks, fees, and expenses could affect your investment over time. In this guide, you'll find information that we hope will be helpful when it comes to investing in variable annuities. You'll find a general description of variable annuities and some of the features associated with them, such as the fees and share classes, as well as important questions to ask and some resources you can consult for additional information.

The information in this guide is intended only to provide a general background on variable annuity products, and should not be relied upon in connection with the purchase of any particular product. H.D. Vest offers a wide variety of annuity products from many different insurance companies, and each of these products has unique features. Important information about specific annuity products, including share classes, investment and payout options, the risks involved, and the fees, expenses and other costs that can affect the performance of your investment, can be found in the annuity contract and the product prospectus. Many insurance companies make these documents available on their websites, and they are also available from your H.D. Vest Advisor or directly from the insurance company. These documents contain important disclosures, and you should read and carefully consider this information before investing.

You should also compare the costs and features of the annuity to other variable annuities and to other types of investments, such as mutual funds. Your H.D. Vest Advisor will be glad to provide you with assistance if you have any questions.

## How Does a Variable Annuity Work?

There are a number of ways to invest in a variable annuity, and to manage your annuity investments over time. A variable annuity generally has two phases, an "accumulation" phase and a "payout" phase.

The "accumulation" phase is the period during which you are depositing money into your annuity via premium payments to the insurance company. You can purchase a variable annuity contract by making an up-front lump-sum payment or a series of purchase payments over time. Insurance companies that offer variable annuity products place investor funds in segregated accounts called "separate accounts," and the funds are then invested in "sub-accounts."

You manage your portfolio and can choose among a number of different investment options, depending on your risk tolerance. Most of the sub-account options in a variable annuity invest the underlying assets in stocks and bonds, and the investments are therefore subject to market risks, including the possible loss of principal. Many variable annuities will also allow you to allocate portions of your payments to a fixed account or money market that pays a fixed rate of interest to potentially safeguard against market fluctuations. You should consider a variety of factors before selecting investment options, such as the investment objectives of the underlying sub-accounts, management fees, and any other expenses. Information about investment options is contained in a prospectus relating to each sub-account, and you should read this information carefully before making investment decisions. You can move your money among various sub-accounts without paying tax on investment income or gains. However, the insurance company may limit the number of investment changes that can be made, or charge a fee for transfers.

The second phase of an annuity is the "payout" or "annuitization" phase, and represents the period during which you receive payments from the insurance company. Depending on the type of annuity you own, you may receive your purchase payments plus any gains (or minus losses) as a lump-sum payment, or as a stream of payments at regular intervals (e.g., monthly). Under many annuity contracts, you can opt for your annuity payments to last for a set time period (e.g., 25 years) or for the lifetime of you or a designee, such as your beneficiary. Annuity products can offer significantly different payout options, so you should make sure you understand the payout options before you invest.

In addition, some annuities can be structured as immediate annuities (versus deferred annuities), which means that the annuity is purchased with a lump sum payment and the payout begins immediately or shortly thereafter. Immediate annuities are often used to provide retirement income, but they can be used to serve other investment objectives as well.

It is important to remember that annuity contracts are highly individualized, especially when it concerns the payout phase. The choices you make concerning when and how to withdraw money from your annuity can significantly affect the benefits you receive under the contract, and can also have significant tax consequences. Therefore, you should be sure that you understand all of your options, and discuss your situation with your financial and tax advisors, before making any decisions.

## General Features of an Annuity

While variable annuities vary greatly in terms of the features they offer, and the costs associated with those features, many variable annuities have the following features in common:

### 1. Periodic Payments/Income

Once an annuity has reached the payout phase, most variable annuities allow you to receive a monthly income stream for the rest of your life (or the life of a spouse or beneficiary), as long as you have held the investment for the requisite time period. If you elect to “annuitize” (i.e., receive a guaranteed stream of payments), the amount you receive will depend on the performance of your investments and how long the designated recipients live. This feature offers potential protection against the possibility that, after you retire, you will outlive your assets. IRS rules generally provide that once you invest into an annuity contract you cannot withdraw the funds until you reach age 59½, or you will have to pay a 10% penalty to the IRS. Additionally, the insurance company will likely impose surrender charges if you withdraw more than the amount permitted by your contract before the designated holding period (see below for a discussion of “Surrender Charges”).

### 2. Death Benefit

Variable annuities offer a guaranteed death benefit. This feature generally provides that, if you die, your designated beneficiary is guaranteed to receive the higher of the value of your investments or the amount of your premium payments minus withdrawals. As an example, if you invested \$100,000 into an annuity and at the time of your death the value had grown to \$120,000, your beneficiaries would receive that higher amount. If the value had declined to \$80,000, your beneficiaries would still receive the \$100,000 you invested. Guaranteed death benefits often are not available if you have already elected to receive annuitized payments before you die, and can be significantly affected if you take withdrawals from the annuity. Death benefits vary greatly between products, and you should be sure that you understand the death benefit features of a particular annuity before investing.

#### *A Word About Guarantees*

Guarantees such as income and death benefits, like all payment obligations of the issuing insurance company, are backed only by the financial strength of the issuing insurance company.

### 3. Step-up Features

Many annuities provide guarantees concerning the income benefits or death benefits available under the annuity contract. Some annuities also allow you to lock in a “stepped up” guarantee based on the value of the annuity on a designated date (for example, the anniversary date of your investment). This feature allows you to lock in positive investment performance to protect against future declines in the value of your sub-accounts. You should be aware that withdrawals from your annuity may adversely affect your step-up guarantee. Step-up features vary widely in terms of their characteristics, availability, and cost; please ask your H.D. Vest Advisor about available “step up” features and consult the annuity prospectus.

#### 4. Tax-Deferred Growth and Tax-Free Transfers

Variable annuities allow your investments to grow on a tax-deferred basis, meaning you will not have to pay tax on any gains or income until they are withdrawn. When you receive payments from your annuity, you will be taxed on any gains at ordinary income tax rates rather than capital gains rates, which currently are generally lower. Tax penalties may apply to withdrawals before age 59½. Many qualified retirement accounts (including Individual Retirement Accounts (IRAs) and 401(k) plans) already provide tax deferred treatment, so you should purchase an annuity in a qualified retirement account only if you decide that you need an annuity based on the other features the annuity provides, such as guaranteed income or death benefits. The IRS also allows you to transfer your money from one annuity sub-account to another sub-account without incurring tax at the time of the transfer, subject to any limitations on such transfers imposed by the insurance company in the applicable prospectus. You should consult your tax and financial representatives to help you understand the differences regarding how investments in (and withdrawals from) annuities and mutual funds are taxed, and whether an annuity is right for you given your particular situation.

#### 5. Free Look Period

After your annuity contract is delivered, you have a period of time, referred to as the “free look” period, during which you can cancel the contract without paying surrender charges or penalties. The “free look” period varies from state-to-state, but is generally between ten and thirty days. During the “free look” period, you should again carefully review your annuity contract, the prospectuses and any other information provided to make sure that the annuity is consistent with your needs, and that you are satisfied with the investment. Once the “free look” period ends, you will be bound to the annuity contract, and may incur substantial tax penalties and other charges if you change your mind.

### **Variable Annuity Charges**

As with any investment, there are costs associated with owning a variable annuity. These costs will vary among annuities and even within the annuity itself depending on the investment options and other features you elect to purchase. Make sure you review the annuity prospectus and ask your H.D. Vest Advisor to explain any charges you do not understand before you invest. The charges can significantly affect the value of your account and the return on your investment. Charges specific to annuities will often include the following:

*Surrender Charges* – Most insurance companies will charge a surrender fee if you withdraw money from the variable annuity before a specified holding period expires. Surrender charges often decline each year and typically disappear over time if you hold the annuity long enough. For example, the surrender charge may start at 7% in the first year of the contract, and decline by 1% per year thereafter until the surrender charge no longer applies. Often, annuity contracts will permit you to withdraw a portion of your investment each year (e.g., 10% of the account value) without incurring a surrender charge (tax penalties may still apply for withdrawals prior to age 59½).

*Mortality and Expense (M&E) Charge* – This fee pays for the insurance risks that the insurance company assumes for the annuity contract. Profit from M&E charges

may be used to pay insurance company costs of selling the variable annuity, such as a commission paid to your investment professional for selling the variable annuity to you. In general, these fees will be a percentage of your average account value each year. For example, if the variable annuity has an M&E charge of 1.25%, you would pay an annual fee of \$125 for each \$10,000 invested in the annuity.

*Administrative Fees and Contract Maintenance Fees* – The insurance company may also charge a separate record-keeping or administrative fee, which is typically a flat fee (e.g., \$30 per year) or a percentage of the account value (e.g., 0.15% per year). For example, if the annual administrative fee is assessed at 0.15% of the account value, you would pay an annual fee of \$15 for each \$10,000 invested in the annuity. The contract maintenance fee is an annual flat fee, approximately \$25 or \$30 a year, to keep the contract active. This fee may be waived on variable annuity contracts with account values over a certain dollar amount (e.g., \$50,000).

*Sub-account Management Fees and Other Charges* – The underlying investment sub-accounts in which your annuity is invested also charge fees and expenses. These fees will vary depending on the various sub-account options you choose. The management fees and other fund-specific charges and expenses are disclosed in the fund prospectus.

*Premium Taxes* – Certain state and local governments impose premium taxes which currently range from 0% to 5%. The insurance company is responsible for paying these taxes and will determine the method used to recover premium tax expenses incurred. The insurance company may deduct any applicable premium taxes from the contract value, either upon death, surrender or annuitization, or at the time purchase payments are made, but no earlier than when the insurance company has a tax liability under state law.

*Other Possible Fees* – Insurance companies may offer special features as part of the annuity contract, such as long-term care insurance, living benefits, enhanced death benefits, guaranteed minimum income benefits, and others. These features, typically called “riders,” carry additional fees and charges. You should consider whether you need the benefit, and if you do whether you can purchase it for less outside of an annuity. Be sure you read the prospectus carefully and understand all the charges and fees of a variable annuity before you invest. The variable annuity prospectus will also contain a description of the associated fees and expenses for the particular rider you are considering. It is important to note that by product prospectus, this fee may increase during the life of the contract up to a stated maximum fee. For example, the initial rider fee may be .75% per year, but could increase to 1.2% during the life of the contract.

## **Annuity Share Classes**

Many insurance companies offer different share classes for a given annuity. The most common share classes for annuities are: B, C, and L share class annuities, and bonus class annuities. In general, the main difference in the share classes is the varying surrender periods and charges, and ongoing fees associated with each share class.

*“Class B” Shares* – If you purchase class B share annuities, you will not pay a front-end sales charge in most cases. However, you will be required to pay what is known as a contingent-deferred sales charge (also known as a “surrender charge”) if you make a partial or full surrender of the annuity within the surrender period. The product prospectus will identify the terms of the surrender schedule, but generally the surrender period averages 6-8 years, with the surrender charge initially ranging from 5%-7% of the annuity’s value. The surrender charge typically decreases each contract year until it reaches zero at the end of the surrender period.

*“Class C” Shares* - Class C share annuities generally do not carry surrender charges; however, because of their added liquidity these annuities will typically carry higher M&E charges and associated fees. Class C share annuities are best suited for investors who are willing to pay higher fees in exchange for greater flexibility in their annuity investment.

*“Class L” Shares* - Class L share annuities are similar to B share annuities in that they carry a surrender charge for early withdrawals. However, L share annuities have a much shorter surrender charge period than B share annuities (i.e., generally 3 to 4 years). Because of the enhanced liquidity, L share annuities typically carry higher charges and fees.

*“Bonus Class”* – Bonus Class annuities generally provide investors with a credit to their account, typically equal to a percentage of the amount invested. Many Bonus Class annuities are offered without any sales charges on the initial investment. However, Bonus Class annuities usually carry higher ongoing fees and expenses and longer surrender periods. If the annuity is held for a long time, at some point over the life of the annuity the higher expenses will likely outweigh the bonus credit. If you are considering this type of annuity, you should carefully review the benefit from the bonus against the possibly higher fees and expenses, and longer surrender period.

*John Hancock Annuity Note* – The John Hancock Annuity Note carries an up-front 3% sales charge and an annual product expense, which includes the fund fee and the lifetime income guarantee fee. There is no surrender schedule associated with this product. On the fifth contract anniversary the guaranteed retirement income value will be calculated and the income stream will start automatically. The Death Benefit is the contract value on date of death. Withdrawals prior to the fifth anniversary lock in will reduce the contract value dollar for dollar. After the fifth anniversary lock in, if withdrawals in excess of 5% are taken, the withdrawal benefit base will be reduced to the current contract value. The product’s prospectus will detail all fees associated with the annuity.

H.D. Vest and your Advisor will earn compensation irrespective of which share class you select; however, the amount of up-front and ongoing compensation will depend on the share class you select, and may be affected by the commission option that your Advisor selects. Please consult the prospectus, and see below for a discussion of “H.D. Vest’s Compensation and Conflicts of Interest.”

## **“Section 1035” Exchanges**

Section 1035 of the Internal Revenue Code allows individuals to directly transfer funds in an existing annuity policy to another annuity policy, without creating a taxable event. What this means is that, under the tax code, you can replace your existing annuity with a new annuity contract without being taxed on the accumulated income or gains. A 1035 exchange can be a useful if, for example, another annuity has additional features that better fit your needs, such different investment options, enhanced living or death benefits, or more favorable payout options.

If you are thinking about a 1035 exchange, you should compare both annuity products carefully. While a 1035 exchange may look like a great option, you may incur surrender charges on the original annuity if you are still in the surrender charge period. Additionally, you will likely have to begin a new surrender period with the new annuity. Also, while the new annuity may have better features, you also need to compare the fees associated with each annuity.

## **H.D. Vest’s Compensation and Conflicts of Interest**

H.D. Vest and your Advisor receive compensation for the sale of investment products, including variable annuities. This compensation may be based on a particular transaction, such as a commission for the purchase of an annuity, or may be based on fees if you have a fee-based investment advisory account. In addition, a portion of the total compensation received by H.D. Vest and your Advisor may take the form of a “trailer” or 12b-1 distribution fees; these fees are paid periodically during the period your account is open.

Insurance companies (and even different annuity products offered by the same company) pay different commissions and ongoing compensation, and thus the amount H.D. Vest earns depends on the investment you make. H.D. Vest’s up-front and ongoing compensation also varies depending on which annuity share class you invest in. For example, a class B share annuity typically pays a higher up-front commission but lower ongoing “trailers” than a class L share annuity. Most annuities also allow your Advisor some flexibility to choose between compensation options providing higher compensation up-front with lower continuing payments, and options providing lower up-front compensation with higher ongoing payments.

The annuity prospectus contains detailed disclosures about sales charges and ongoing fees. You should review this information carefully before investing, and ask your H.D. Vest Advisor any questions you have about how H.D. Vest is compensated in connection with your investment.

H.D. Vest has reviewed numerous insurance companies’ products, and has made them available for Advisors to offer their clients. Within this universe, a select group of companies have agreed to provide payments to help H.D. Vest with the educational, training, record-keeping, and other costs associated with bringing these products to H.D. Vest’s customers. These payments are calculated as a percentage of assets. The amount paid from insurance companies can range from 0.05% to 0.35% on sales, and 0.05% to 0.15% on assets each year. For example, for every \$10,000 in annuity value, H.D. Vest might receive up to \$35 at the time of initial purchase, and up to \$15 annually if these assets stay invested. H.D. Vest may also receive additional lump sum payments, which could be significant in amount.

In exchange for sharing costs, the insurance companies receive enhanced access to H.D. Vest's sales force, and may interact with H.D. Vest Advisors during training events, conference calls, and meetings. They also receive heightened visibility through the distribution of sales literature and newsletters, and by means of links, information, and lists posted on H.D. Vest's intranet pages.

All of these above-referenced payments are in addition to the sales charges and ongoing payments disclosed in the fee tables found in the product prospectus. Over the course of managing your relationship, your Advisor may recommend products from these insurance companies. Advisors do not, however, receive any portion of, or any additional compensation as a result of, these payments or compensation arrangements between H.D. Vest and the product sponsors. Advisors may, however, separately receive reimbursement for marketing expenses, client functions and attendance at due diligence, training and education meetings sponsored by H.D. Vest or the product sponsors.

Sub-account policies can be found in the prospectus and Statement of Additional Information for the particular investment option you choose. If you have any questions about these practices, please contact your H.D. Vest Advisor.

The following insurance companies (or their affiliates) paid H.D. Vest for training and support, account administration or record-keeping services during the past year: The Hartford Insurance Group, Sun Life of Canada (US), Lincoln Benefit Life, Lincoln Financial Distributors, John Hancock Distributors, Met Life Investors USA Insurance Company, MetLife Investors Insurance Company, The Hartford/PLANCO, Allianz Life, and AXA Distributors.

*For more complete information about variable annuity products or to obtain a variable annuity prospectus, please ask your H.D. Vest Advisor. Investors should consider the contract and the underlying portfolios' investment objectives, risks, and charges and expenses carefully before investing. This and other important information is contained in the prospectuses. You should read and consider the information in the prospectuses carefully before investing.*

## **Things to Consider**

A variable annuity can be an important component of your financial, retirement and estate plan, but it is important to make sure it is an appropriate investment choice for you. Don't be afraid to ask your H.D. Vest Advisor any and all questions you have about the product. Your H.D. Vest Advisor is there to answer your questions in order to help you make appropriate investment decisions.

The Securities and Exchange Commission ("SEC") has compiled a non-exclusive list of questions that you should consider before investing in a variable annuity, which includes:

- Will you use the variable annuity primarily to save for retirement or a similar long-term goal?
- Are you investing in the variable annuity through a retirement plan or IRA (which would mean that you are not receiving any additional tax-deferral benefit from the variable annuity)?
- Are you willing to take the risk that your account value may decrease if the underlying investment options perform badly?

- Do you understand the features of the variable annuity, including all features, riders and conditions?
- Do you understand all of the fees and expenses that the variable annuity charges?
- Do you intend to remain in the variable annuity long enough to avoid paying any surrender charges if you have to withdraw money?
- If a variable annuity offers a bonus credit, will the bonus outweigh any higher fees and charges that the product may charge?
- Are there features of the variable annuity, such as long-term care insurance, that you could purchase more cheaply separately?
- Have you consulted with a tax advisor and considered all the tax consequences of purchasing an annuity, including the effect of annuity payments on your tax status in retirement?
- If you are exchanging one annuity for another one, do the benefits of the exchange outweigh the costs, such as any surrender charges you will have to pay if you withdraw your money before the end of the surrender charge period for the new annuity?

## Final Thoughts

Variable annuities can help you address your financial goals, but they are not right for everyone. Before purchasing a variable annuity, you should learn as much as possible about how variable annuities work, the benefits they provide, and the charges you will pay. Read the prospectus carefully before investing. For more information, you can also consult the following online publications available from the SEC and FINRA:

SEC Publication, Variable Annuities: What You Should Know  
[\(<http://www.sec.gov/investor/pubs/varannty.htm>\)](http://www.sec.gov/investor/pubs/varannty.htm)

SEC Publication, Variable Annuities and Variable Life Products: Questions to Ask  
[\(<http://www.sec.gov/investor/pubs/varaquestions.htm>\)](http://www.sec.gov/investor/pubs/varaquestions.htm)

FINRA Publication, Variable Annuities: Beyond the Hard Sell  
[\(<http://www.finra.org/InvestorInformation/InvestorAlerts/AnnuitiesandInsurance/VariableAnnuitiesBeyondtheHardSell/index.htm>\)](http://www.finra.org/InvestorInformation/InvestorAlerts/AnnuitiesandInsurance/VariableAnnuitiesBeyondtheHardSell/index.htm)

FINRA Publication, Should You Exchange Your Variable Annuity?  
[\(<http://www.finra.org/InvestorInformation/InvestorAlerts/AnnuitiesandInsurance/ShouldYouExchangeYourVariableAnnuity/index.htm>\)](http://www.finra.org/InvestorInformation/InvestorAlerts/AnnuitiesandInsurance/ShouldYouExchangeYourVariableAnnuity/index.htm)

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