WRNewswire

An AALU Washington Report

Thursday, 3 July 2014 **WRN# 14.07.03**

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TOPIC: Treasury Issues Final Regulations to Facilitate Use of Longevity Annuity Contracts within Retirement Accounts

CITES: Final Regulations, Longevity Annuity Contracts, T.D. 9673 addressing 26 CFR Parts 1 and 602, 79 Federal Register 37633, July 2, 2014.

SUMMARY: In announcing the release of final regulations ("final regulations") which are intended to increase the attractiveness and practicality of utilizing a particular type of deferred annuity—called a QLAC ("qualifying longevity annuity contract")—within retirement accounts to avoid exhausting retirement savings, Mark Iwry, the Treasury's deputy assistant secretary for retirement and health policy stressed:

> As boomers approach retirement and life expectancies increase, longevity income annuities can be an important option to help Americans plan for retirement and ensure they have a regular stream of income for as long as they can live.

Under a qualified defined contribution plan, a 403(b) plan, a governmental 457(b) plan, or an IRA, a participant must generally begin making withdrawals—called minimum required distributions—at the age of 70 ½. The final regulations modify the required minimum distribution rules to facilitate the purchase of QLACs—deferred annuities that begin at an advanced age and that meet certain requirements, including the requirement that distributions not begin later than age 85. Under the final regulations, a participant's investment in a QLAC of the lesser of 25 percent of his or her account balance, or $125,000, generally is excluded from the account balance used to determine the participant's required minimum distributions. The maximum amount will be adjusted periodically for inflation. This *WRNewswire* provides an initial summary of the major provisions of the regulations.

MAJOR PROVISIONS:

The following is intended to describe the major features of the final regulations. We note that it does not include more detailed aspects, specific circumstances or departures from the major provisions, which may be analyzed in a forthcoming AALU report.

Limitation on premiums.

- In order to constitute a QLAC, the amount of the premiums paid for the contract under the plan on a given date cannot exceed the lesser of $125,000 or 25 percent of the employee's account balance on the date of payment. The regulations provide for a periodic inflation adjustment of the dollar limitation. An increase that is not a multiple of $10,000 will be rounded to the next lowest multiple of $10,000. Adjustments will be prescribed by the Commissioner in revenue rulings, notices, or other guidance published in the Internal Revenue Bulletin.

- To simplify the application of the percentage limit, the limit is applied with respect to an employee's account balance under a qualified plan as of the last valuation date preceding the date of a premium payment, increased for contributions allocated to the account (and decreased for distributions made from the account) after the valuation date but before the date the premium is paid.

- Although the value of a QLAC is excluded from the account balance used to determine required minimum distributions, the value of a QLAC is included in the account balance for purposes of applying the 25-percent limit.

- If an annuity contract fails to be a QLAC solely because premiums for the contract exceed the premium limits, then the contract will not fail to be a QLAC if the excess premium is returned to the non-QLAC portion of the employee's account by the end of the calendar year following the calendar year in which the excess premium was paid.

Maximum age at commencement.

- In order to constitute a QLAC, the contract must provide that distributions under the contract commence not later than a specified annuity starting date set forth in the contract. The specified annuity starting date must be no later than the first day of the month next following the employee's attainment of age 85. A QLAC could allow an employee to elect an earlier annuity starting date than the specified annuity starting date, but is not required to provide an option to commence distributions before the specified annuity starting date.

- In the future, the maximum age may be adjusted to reflect changes in mortality. The adjusted age (if any) will be prescribed by the Commissioner in revenue rulings, notices, or other guidance published in the Internal Revenue Bulletin.

Benefits payable after death of the employee.

- A QLAC generally may offer a return of premium ("ROP") feature that is payable before and after the employee's annuity starting date. Accordingly, a QLAC may provide for a single-sum death benefit paid to a beneficiary in an amount equal to the excess of the premium payments made with respect to the QLAC over the payments made to the employee under the QLAC. If a QLAC is providing a life annuity to a surviving spouse (or will provide a life annuity to a surviving spouse), it may also provide a similar ROP benefit after the death of both the employee and the spouse.

Other QLAC requirements.

- A QLAC does not include a variable contract under section 817, an indexed contract, or a similar contract. However, the Commissioner may provide an exception to this rule in revenue rulings, notices, or other guidance published in the Internal Revenue Bulletin.

- In order to be a QLAC, a contract is not permitted to make available any commutation benefit, cash surrender value, or other similar feature.

- When the contract is issued, an employee must be notified that the contract is intended to be a QLAC. However, this requirement will be satisfied if this language is included in the contract, or in a rider or endorsement with respect to the contract.

IRAs.

- In order to constitute a QLAC, the amount of the premiums paid for the contract under an IRA on a given date may not exceed $125,000. If, on or before the date of a premium payment, an IRA owner has paid premiums for the same contract or for any other contract that is intended to be a QLAC under the IRA or under any other IRA, plan, or annuity, the $125,000 limit is reduced by the amount of those other premium payments. In addition, in order to constitute a QLAC the amount of the premiums paid for the contract under an IRA on a given date generally may not exceed 25 percent of the individual's IRA account balance.

- For purposes of both the dollar and percentage limitations, unless the trustee, custodian, or issuer of an IRA has actual knowledge to the contrary, the trustee, custodian, or issuer may rely on the IRA owner's representations of the amount of the premiums (other than the premiums paid under the IRA) and, for purposes of applying the percentage limitation, the amount of the individual's IRA account balances (other than the account balance under the IRA).

Section 403(b) plans.

- The final regulations apply the tax-qualified plan rules, instead of the IRA rules, to the purchase of a QLAC under a section 403(b) plan. For example, the 25-percent limitation on premiums is separately determined for each section 403(b) plan in which an employee participates. In addition, the tax-qualified plan rules relating to reliance on representations, rather than the IRA rules, apply to the purchase of a QLAC under a section 403(b) plan.

Section 457(b) plans.

- The rule relating to QLACs is limited to eligible governmental plans under section 457(b). This is because section 457(b)(6) requires that an eligible section 457(b) plan that is not an eligible governmental plan be unfunded, and the purchase of an annuity contract under such a plan would be inconsistent with the requirement that such a plan be unfunded.

Defined benefit plans.

- Defined benefit plans generally are required to offer annuities, which provide longevity protection. Because longevity protection is already available in these plans, the final regulations do not apply to defined benefit plans. However, the Treasury Department and the IRS request comments regarding the desirability of making a form of benefit that replicates the QLAC structure available in defined benefit plans.

Initial disclosure and annual reporting requirements.

- The final regulations do not require an initial disclosure to be issued to the employee in light of the existing disclosure practices that take into account disclosure requirements under state law and under Title I of ERISA. If the Treasury Department and the IRS determine that employees are not receiving sufficient information before a QLAC is purchased, this issue may be reexamined.

- The final regulations prescribe annual reporting requirements under section 6047(d) which require any person issuing any contract that is intended to be a QLAC to file annual calendar-year reports with the IRS and to provide a statement to the employee regarding the status of the contract. The report will be required to identify that the contract is intended to be a QLAC and to include, at a minimum, the following items of information:

    - The name, address, and identifying number of the issuer of the contract, along with information on how to contact the issuer for more information about the contract;

- The name, address, and identifying number of the individual in whose name the contract has been purchased;

- If the contract was purchased under a plan, the name of the plan, the plan number, and the Employer Identification Number (EIN) of the plan sponsor;

- If payments have not yet commenced, the annuity starting date on which the annuity is scheduled to commence, the amount of the periodic annuity payable on that date, and whether that date may be accelerated;

- For the calendar year, the amount of each premium paid for the contract and the date of the premium payment;

- The total amount of all premiums paid for the contract through the end of the calendar year; and

- The fair market value of the QLAC as of the close of the calendar year.

Effective/Applicability Dates.

- The final regulations apply to contracts purchased on or after July 2, 2014. If on or after July 2, 2014, an existing contract is exchanged for a contract that satisfies the requirements to be a QLAC, the new contract will be treated as purchased on the date of the exchange and therefore may qualify as a QLAC. In such a case, the fair market value of the contract that is exchanged for a QLAC is treated as a premium that counts toward the QLAC limit.

RELEVANCE: The final regulations represent additional recognition of the important role played by life insurance products and the life insurance industry in meeting Americans' increasing need for savings and financial and retirement security. The final regulations should increase the attractiveness and practicality of utilizing QLACs in retirement accounts to avoid exhausting retirement savings. Advisors will want to explore with clients and plan sponsors how QLACs may enhance current practices to ensure adequate retirement savings.

***WRNewswire* #14.07.01 was written by Tom Korb on the AALU staff.**

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