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IRS Okays Qualified Longevity Annuity Contracts for DC Plans and IRAs

By: Robert J. Toth, Jr.
Law Office of Robert J. Toth, Jr. LLC

On July 1, 2014, the IRS issued final regulations on Qualified Longevity Annuity Contracts (QLACs), which become effective immediately upon publication. This means that these annuity contracts can now be offered in defined contribution (DC) plans under §§401(a) and 403(b), as well as 457(b) governmental plans, and non-Roth IRAs. If an annuity contract meets the requirements of a QLAC, the premium paid for the contract is not used in the calculation of the required minimum distribution (RMD) amount under the plan or IRA.

A QLAC is a special type of deferred annuity contract that guarantees lifetime income to a participant starting no later than age 85. They are designed to operate in tandem with monthly benefits starting at normal retirement age and ensure that the participants do not outlive their account. For example, a participant could take payments from their 401(k) plan at a rate designed to exhaust the non-QLAC assets at age 85: then the QLAC would begin lifetime payouts.

To be a QLAC, the annuity must be purchased by a plan and the plan must have the ability to distribute the annuity from the plan to the participant. The Plan Administrator will have no responsibility for the QLAC once it is distributed from the plan.

The IRS first published proposed regulations on February 3, 2012, outlining the requirements of a QLAC. ASPPA commented on the proposed regulations, suggesting that the IRS increase the $100,000 limit on the amount that could be used in the purchase of the annuity. These final regulations made key changes, including incorporating ASPPA's request for an increase in the QLAC amount (though not as high as ASPPA requested).

An annuity contract is a QLAC (and its premium is excluded from RMD calculations) if the following requirements are met:

- The annuity is a simple straight life annuity payable beginning at an age not to exceed age 85;
- The annuity is not a variable annuity (or any annuity contract with an account balance), though the benefit can be adjusted for cost of living increases. The annuity may also pay experience dividends;
- The only death benefit payable by the QLAC is a joint and survivor annuity or a return of premium provision, which is newly allowed under the final regulation. There can be no surrender value. There are also special rules for determining the payouts to non-spousal beneficiaries;
- Only funded DC plans and non-Roth IRAs can purchase QLACs. DB plans, non-governmental §457(b) plans or Roth IRAs may not purchase one. The IRS has requested comments on whether or not QLACs should be available under defined benefit plans;

- The amount of premium paid for the contract does not exceed the lesser of $125,000 or 25% of the participant's or IRA holder's account balance;
- Special RMD rules apply to payments from QLACs, including a special rule for §403(b) plans; and
- The insurance company issuing the QLAC files annual reports on the QLAC to the IRS and copies the participant, similar to the annual IRS Form 5498 (IRA Contribution Information). The IRS will need to develop new forms for this reporting.

The final regulations also made other important changes to the proposed regulations:

- The proposed regulations required insurance companies to state that the annuity contract or certificate was a QLAC. In response to insurance industry concerns, the final regulations adopted a transitional rule. Insurance contracts issued before January 1, 2016 will not need to specifically state that they are QLACs, as long as the participant is notified at the time of purchase, in writing, that the contract is intended to be a QLAC, and that a rider that contains the QLAC language is issued by January 1, 2016;
- No special initial disclosure rules will be required upon the purchase of a QLAC; and
- The final regulations provide a one-year window to correct QLACs which exceed the dollar limitation.

As noted, QLACs can be provided from within a DC plan, or distributed from a DC plan. For guidance on how to distribute the QLAC from a plan as a "Qualified Plan Distributed Annuity", see the preamble to the proposed QLAC regulations at 75 FR 5253, February 2, 2010, and Revenue Ruling 2012-3.

WE NEED YOUR QUESTIONS FOR IRS FOR THE ASPPA ANNUAL CONFERENCE!

With another testing season in the rearview mirror and PPA restatements looming on the horizon, there are sure to be plenty of questions on everyone's mind…and ASPPA's IRS Q&A subcommittee wants to hear them! We are currently gathering questions to go on the list that will be submitted to our friends at the IRS and discussed at the Question & Answer general session at this October's Annual Conference.

The saying that there is no such thing as a dumb question applies here; however, we are especially interested in questions that include some nuance and might not have a clear-cut answer. Check with your co-workers, friends, family (ok, maybe not your friends and family unless they also happen to be co-workers) and send your questions to us at IRSquestion@asppa.org so that we can add them to the list.

Thanks,

--Adam C. Pozek, Chair

ASPPA GAC IRS Q&A Subcommittee