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Annuities

Practitioners Say QLAC Rules Widen Choices, But Plans May Be Reluctant to Offer Them

Recent final rules on qualifying longevity annuity contracts (QLACs)—which can help retirees ensure they have a stream of regular income through their advanced years—received praise from retirement insiders, but the new guidance doesn't guarantee that the products will be embraced, practitioners told Bloomberg BNA in a series of interviews.

Questions remain about whether employer-sponsored plans will be interested in offering them because of possible fiduciary liability, among other issues. In addition, consumers may be cautious to buy them because of the money involved.

''It's definitely a good step in terms of enabling defined contribution plans to provide a way for participants to protect against outliving their income. I'm not sure this one is going to be as popular in the plan market as in the IRA market. The question is whether employers are going to want to provide these annuities,'' Louis T. Mazawey, principal at Groom Law Group Chartered, told Bloomberg BNA on July 2.

On July 1, the Treasury Department and the Internal Revenue Service issued final regulations (T.D. 9673, RIN 1545-BK23) modifying the required minimum distribution rules to allow for the purchase of deferred annuities that start no later than age 85 (127 PBD, 7/2/14; 41 BPR 1393, 7/8/14).

The regulations make longevity annuities accessible to the 401(k) and individual retirement account markets and to employer-sponsored individual account plans. The rules expand the availability of retirement income options as more Americans reach retirement age, Treasury said in a July 1 news release.

Addressing Risk. Bryan W. Keene, a partner at Davis & Harman LLP told Bloomberg BNA July 3 that he is very happy with how the final rules turned out and ''that the government has taken the initiative to address this issue to really eliminate a road block that had been preventing this particular type of annuity from being used in the qualified plan and IRA markets.'' Keene's firm represents the Committee of Annuity Insurers, a coalition of 28 of the largest issuers of annuity contracts.

James Szostek, vice president of taxes and retirement security at the American Council of Life Insurers, agreed with Mazawey and Keene, telling Bloomberg BNA July 7 the final rules are ''another piece of the puzzle. A good piece of the puzzle we think to help people utilize a product that we think helps them address longevity risk. It's something that they couldn't do before in a qualified plan or an IRA.''

Jan Jacobson, senior counsel for retirement policy at the American Benefits Council, told Bloomberg BNA on July 3 that her group is very pleased the final rules have been issued, because it will allow people access to QLACs.

''Before this you really couldn't use qualified money, whether it was from a retirement plan or an IRA to buy a deeply deferred annuity to age 80 or 85 because of the minimum distribution rules that require you to start taking minimum distributions at age 70 ½. Without that you would still have to count whatever you spend on the premiums as part of your account balance and you would have to do minimum distributions based on that larger amount and in some cases those minimum distributions might exceed what you have left in your account. This is very helpful in that respect,'' she said.

Outstanding Issues. Karen Friedman, executive vice president and policy director of the Pension Rights Center, told Bloomberg BNA on July 2 that her group is pleased with the rule, but that there are some policy issues surrounding it that need to be addressed.

One issue involves the cost of buying a QLAC for women in an employer-sponsored plan versus an IRA, Friedman said.

''If somebody buys one of these longevity annuities and they buy it with their IRA money, women, older women who live longer and tend to have less money are going to have to buy a QLAC on the outside market where they use sex-based tables, which I will say are discriminatory against women,'' Friedman said.

Jacobson also said there are issues that need to be addressed, including the question of fiduciary liability.

''One issue that many employers have with just putting any kind of annuity in the plan is the potential for fiduciary liability for the choice of the company,'' she said.

In addition, there are questions surrounding what would happen if a participant purchases a QLAC through their retirement plan and then the plan changes service providers, Jacobson said. ''It's not clear what would happen in that situation. Hopefully the participant wouldn't have to give up their QLAC,'' she said.

Jacobson said plan sponsors might want to see a more extensive correction program than the one found in the final rules. The final rules provide that if excess premiums are made to a QLAC, it won't fail to be a QLAC if the excess premiums are returned to the non-QLAC portion of the employee's account by the end of the calendar year that the excess premiums were paid, according to the rules. However, she said there is concern about what happens if an error is discovered after the calendar year is over.

Double-Edged Sword. Just because the new final rules allow plans and IRAs to offer QLACs doesn't mean they will and it doesn't mean that participants will be lining up to buy them, practitioners said.

''These new QLACs are going to have to be sold to people. Because it's going to still be a big stretch for people to say, I'm going to put aside money today so that maybe if I live to age 85 I'm going to have money,'' Friedman said. The flip side of that is that if people don't buy annuities, they risk outliving their money, she said.

''These are good ideas in terms of a retirement planning tool, it's just going to be a question of whether there's take up rates and I think that that's going to take a lot of education from the government, from the industry and from the consumer groups,'' Friedman said.

There is also an emotional component to buying QLACs and similar products, Keene said.

''There's a behavioral response to annuitization where some people are perhaps reluctant to do so because they feel like if they pay that money over to the insurance company and then they die—worst case scenario they die the next day—then they feel like they'd be losing out or their beneficiary would lose out on something,'' he said.

That is where the new return of premium feature included in the final rules comes in, Keene said. The final rules allow longevity annuities or IRAs to provide a ''return of premium'' feature that would return to a retiree's account premiums paid but not received as annuity payments if a retiree purchasing an annuity dies before or after the age that an annuity begins.

While this is an assurance for some looking to buy annuities, it can still be an expensive proposition, William Bortz, a pension fellow with the Pension Rights Center and former associate benefits tax counsel, Office of Benefits Tax Counsel, Treasury, told Bloomberg BNA on July 2.

''The reason why the original proposed regs didn't have it is because it's expensive. And they were trying to keep the QLACs cheap. It costs in the neighborhood of 5 to 10 percent more,'' he said.

QLAC Education. Now that the final rules are out, there will be a need to educate both employers and consumers about the benefits and availability of QLACs, Keene said.

''One of the kind of unspoken benefits of these rules is that if employers start putting these types of products into their plans, it starts the education process and it starts people thinking about really the income side of retirement,'' he said.

Keene said even if people don't buy QLACs, seeing them offered in their plans may start the thought process of what to do about saving for retirement and how to live off of that money once retirement hits.

Still, the question remains about whether these types of annuities will catch on with employer plans, Mazawey said.

''Whether larger companies are going to want to take the step and do the homework and reviewing the different QLACs that are out there and comparing them remains to be seen. We hope they will and I think Treasury hopes they will, but we just don't know,'' Mazawey said.

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