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January 14, 2015

Mr. J. Mark Iwry
Senior Advisor to the Secretary and Deputy Assistant Secretary
for Retirement and Health Policy
Department of the Treasury
1500 Pennsylvania Avenue, NW, Room 3044
Washington, DC 20220

RE: Qualified Longevity Annuity Contracts in Defined Benefit Plans

Dear Mr. Iwry:

The American Academy of Actuaries¹ Pension Practice Council commends the Treasury Department and the Internal Revenue Service for the recent publication of final regulations concerning Qualified Longevity Annuity Contracts (QLACs). Providing these benefits through qualified retirement plans and individual retirement accounts will enhance the retirement security of many Americans.

The Council believes that significantly more Americans could benefit from such longevity annuities if qualified defined benefit pension plans could provide these benefits directly, rather than by requiring the purchase of an insurance contract. In this letter, we point out the advantages provided by such direct provision and the form these benefits could take.

Advantages Offered by Defined Benefit Plan

Providing a QLAC through a qualified defined benefit pension plan offers several advantages:

- The employer is often a known and trusted source for the employee.
- Information regarding the QLAC would be a standard part of communication material provided to plan participants, thus making more individuals aware of QLACs and the potential benefits.
- Pricing of the QLAC, on a basis at least as favorable as 417(e), would likely be more attractive than in the insurance market.

¹ The American Academy of Actuaries is an 18,000+ member professional association whose mission is to serve the public and the U.S. actuarial profession. The Academy assists public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

- Pricing would not include the loads or commissions found in the insurance market.
- Providing a QLAC as an optional form of settlement greatly simplifies the process of obtaining a QLAC and could expand usage.

These advantages would likely provide greater utilization of QLACs at more favorable pricing. We next offer illustrations of ways in which a qualified defined benefit plan might offer a QLAC.

QLAC in Lieu of Total Lump Sum

Many defined benefit pension plans offer lump sums as a settlement option. Proposed regulations issued in 2012 allow defined benefit plans to provide partial lump sums, but do not provide for the residual defined benefit to be paid as a QLAC or provide any relief from the required minimum distribution rules. If defined benefit plans could directly provide QLACs, the lump sum option could be structured to provide a partial lump sum equal to the present value of all payments to be made before a certain age (to be selected by the participant, not to exceed 85). The difference between the total lump sum and the partial lump sum would be the consideration for the QLAC. To be consistent with the rules that apply to DC plans, the QLAC consideration could be limited to no more than 25 percent of the total lump sum or \$125,000, whichever is less.

Allowing such a partial lump sum and QLAC from the defined benefit plan could potentially decrease the total amount paid out as lump sums and increase the longevity protection of participants with very little administrative effort.

The ease and attractiveness of this alternative can be illustrated by a simple example.² A defined benefit plan that currently offers lump sums as an optional form could add a QLAC option. Assume a 65-year old is retiring with a benefit of \$1,000 per month payable as a life annuity. The lump sum alternative provides an immediate payment of \$160,900. The QLAC option would provide an immediate payment of \$147,800 and a monthly benefit of \$1,000 commencing at age 85. The consideration for the QLAC is \$13,100, an amount the retiree may be willing to pay for the longevity protection.

Future updates to the 417(e) mortality table will likely make the QLAC pricing more expensive relative to the total benefit; however, this option should still appear attractive to participants. Using the same assumptions as in the above example, but changing the mortality to a 50/50 blend of male and female mortality using the RP-2014 table and MP-2014 projection scale, with generational projection, the full lump sum would rise to \$168,000. The cost of the \$1,000 monthly QLAC would rise to \$17,900, leaving a \$150,100 residual lump sum.

QLAC Provided to Defined Contribution Plan of Same Employer

Many employers sponsor both a defined benefit plan and a defined contribution plan. Revenue Ruling 2012-4 allows such employers to accept rollovers from the defined contribution plan in

² Conversion to optional forms based on August 2014 IRC 417(e) interest rates and the 2015 applicable mortality table; amounts are rounded.

the defined benefit plan for the purpose of providing lifetime income, but does not currently provide that the lifetime income could be provided as a QLAC. Allowing the defined benefit plan to provide a QLAC in consideration of the rollover would enable more plan participants to have access to a QLAC. QLACs would be funded by a rollover of funds from the defined contribution plan to the defined benefit plan. Such rollovers could be limited to the same dollar limitation of the final regulation (25% of the DC plan balance or \$125,000, whichever is less). Benefits would be offered on a gender-neutral basis not less favorable than the 417(e) basis. The sponsor could routinely provide information concerning this option to all participants nearing retirement age, thus making more individuals aware of the option on a basis that would likely be more favorable than other potential markets. This could increase longevity protection for these individuals.

Revenue Ruling 2012-4 considers the amount of a rollover as a mandatory contribution. If the participant dies before the annuity start date, the mandatory contributions (plus interest) are payable as a death benefit, either as a lump sum or as an actuarially equivalent life annuity to the surviving spouse. We suggest a different treatment would be appropriate in the case of a rollover that is converted to a QLAC.

To be consistent with the way QLACs are provided through insurance contracts, the QLAC could be offered with and without a death benefit. A participant could elect a larger QLAC benefit and no death benefit, or a smaller QLAC benefit and a refund of premium (without interest) death benefit. To accomplish this, the rollover should immediately be converted to an annuity based on then-current 417(e) assumptions (or alternative plan basis if more favorable). The rollover date (and date of conversion to an annuity) should be treated as the annuity start date. If death then occurs before the first annuity payment, the death benefit elected by the participant (refund of premium or nothing) would then be payable. This is consistent with the annuity start date for mandatory contributions converted to regular lifetime benefits because the annuity start date is the date that the mandatory contributions are converted to an annuity using 417(e) assumptions.

The changes we are suggesting would potentially make many additional Americans aware of the QLAC alternative and enhance the retirement security of those who elect the option. We appreciate the Treasury Department and IRS consideration of these suggestions. Please contact Matthew Mulling, the Academy's pension policy analyst (202-785-7868; mulling@actuary.org) if you have any questions or would like to meet with us to discuss these items further.

Respectfully,

Eli Greenblum, MAAA, FSA, EA
Chairperson, Pension Practice Council
American Academy of Actuaries