QLAC

Simplified

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What is a QLAC?

A QLAC (Qualified Longevity Annuity Contract) is a unique type of longevity annuity that can be used in Traditional IRA's and qualified participating plans like 401k's, 403(b)s, and governmental 457(b)s. It was designed by the government to remind people to plan for their future income needs in a pension-less world. Yes, the government did something positive for the consumer!

The bill passed Congress in July 2014. The fact that the first product was not available for purchase until October of 2014 validates how off guard the annuity companies were by the passage of the bill to make QLACs possible. If you would like access to the bill click here to read it as it was written.

Primary point of what QLAC was designed for:

1) Tax-Deferral of income until your later years to act as an income insurance policy. Some have taken this as a tax-benefit, but the true benefit is income insurance. Guaranteed income you cannot outlive. The ability to defer the taxes on the principle amount is an added benefit.

2) To be somewhat redundant: Guaranteed Income regardless of how long you live. Complement to Social Security and pension plans. Simple, easy to implement and easy to understand.

This is not an investment it is a guaranteed income insurance policy… If you attempt to look at a QLAC as an investment you will get what I call the 'annuity flu'. In other words attempting to measure this as an investment will make you sick to your stomach. That said, looking and measuring this in terms of a guaranteed insurance contract that will pay me regardless of how long I live, and if joint with your spouse will pay as long as you both shall live.

One way to view a QLAC is the purchase of your own pension. The benefit is clearly building a degree of certainty into your lifetime income payments or peace of mind.

Will I Outlive a QLAC?

With the QLAC strategy, you are transferring the risk to the carrier to provide a lifetime income stream that you will never outlive. Regardless of how long you live, the annuity carrier is on the hook to pay.

With that in mind you now understand the importance of dealing with a quality insurance company that will outlive you financially. The guarantee is only as good as the company standing behind the promise.

What Happens if I Die?

If you die before the income stream turns on, 100% of the initial premium will be returned to your listed beneficiaries in a lump sum. The annuity company does not keep your money. If you have started taking your income stream and die the return of premium feature applies as long as the death benefit is paid out under specific calendar guidelines.

While it is always good to plan for contingencies when investing your money, but the design of QLAC is for living longer than your money will support you. It is a form of income insurance.

Is There an Annual Fee?

The QLAC has no annual fee for the life of the policy. It is a net transaction to you.

It would be fair to note that while there is no annual fee for the life of the contract… if you die before the payments are made you beneficiary gets back the original amount invested. Thus, the insurance company gets the use of your money during that period. However, the upside is if you live and the insurance company has to pay you as long as you are alive. In life this is known as give and take.

Cash Value Rules for QLAC

One of the limitations of the QLAC strategy is that there is no cash value once the policy is purchased. You can only get to the principal in payment form. Why do we bring this up? First, you should know that prior to putting your money into a QLAC contract. Second, there are annuity agent who may try and use this as a reason to sell you something else (another type of annuity) with a higher commission. BUYERS BEWARE!

Adding Money to a QLAC and Overfunding

QLACs do allow you to add money, but the funding guidelines/rules still apply (25% or $125,000 is maximum contribution allowed).

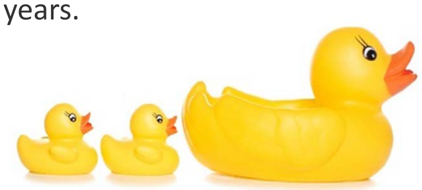
The primary reason that QLACs allow money to be added is for the person participating in an employer retirement plan that offers the QLAC option. The QLAC rules actually cover the possibility of mistakenly exceeding the funding limitations. This provision will take the excess amount out of the QLAC and back into your general account. Again, this possibly applies to QLACs within employer retirement plans. There is a one year window to correct QLACs that are overfunded.

This does raise the question… Is there an annuity that allows me to contribute more than $125,000 with the same income benefits as a QLAC?

Absolutely. It is commonly referred to as a Deferred (Longevity) Income Annuity (DIA). We added the word longevity to make the comparison to the QLAC. The DIA allows for either qualified money or non-qualified money to fund the policy. With qualified money the only difference is the above the $125,000 required minimum distribution must still be made by age 70 ½. This allows for you to plan earlier income needs to be funded with a DIA contract and longer range income needs to use a QLAC.

Cost of Living Adjustment

With QLACs you have the ability to attach a COLA (Cost of Living Adjustment) annual increase at the time of application, and choose the percentage increase for the life of the policy. For example, you can attach a 3% COLA to a QLAC policy your income stream would then increase by 3% per year for the life of the policy. But, note that by adding a COLA to a QLAC the initial payment will be lower than if you don't attach the COLA. The good news with QLAC is that the $125,000 funding limit will be indexed to inflation and adjusted in $10,000 increments. If inflation is projected at 3%+ per year, then the contribution increase will probably happen every 3 to 4 years.



Laddering Strategies

With QLAC's you can have guaranteed income streams turning on at different ages within the funding rules of 25% or $125,000 (whichever is less). In other words you could have QLAC policies turning on at age 75, 80, and 85 as examples. The older you are the higher the payment will be. It also would account for inflation issues with five year increments. Using QLACs and DIAs in conjunction with social security is one simple way to apply income laddering to account for cost of living adjustments periodically.

Return on Investment and Internal Rate of Return (ROI)

With QLAC's you need to leave ROI calculations at the door. With lifetime income stream payments, there in no way to calculate ROI until you pass away. QLACs should be positioned in your mind and in your portfolio right beside Social Security payments and pension payments. QLACs are pure transfer of risk strategies that contractually guarantee that you will never outlive your money. They are not considered to be investments. Think of it more line with income insurance.

Again this is not a negative for the QLAC contract it is a part of what makes it a product that provides a guaranteed income stream. Like stated above, beware of agents attempting to sell you a different type of contract with fairy tale hypotheticals or returns that don't compare with a QLAC annuity.

Potentially Reduces Taxes

Required Minimum Distributions payments must begin by April 1st of the year that follows the year an IRA owner turns 70 ½ . Since taxes must be paid once these distributions begin owning a QLAC can potentially help reduce the taxes you pay. Since you are deferring $125,000 or 25% (whichever is less) of your IRA until later, up to age 85, your RMD calculations at 70 ½ will be based on a smaller dollar amount.

This is a side benefit of the QLAC… it is not the primary reason to buy a QLAC. FYI.

QLAC Ruling Summary:

- QLAC - Can be used in Traditional IRA's
- QLAC - Can be used in participating 401k,403(b), and governmental 457(b) plans
- QLAC - Can NOT be used in Roth IRAs, Inherited IRAs, and Pension Plans
- QLAC - Can defer up to age 85

QLAC Premium Limits:

- 25% of total amount of all qualified accounts, or $125,000, whichever is less
- One individual can add $125,000 as an aggregate amount of all IRAs
- The $125,000 limit will be indexed for inflation and adjusted in $10,000 increments
- The 25% limit on IRAs applies to as many IRAs you may have. The IRS is looking at the total dollar amount

Spousal/Beneficiary/Non-Spousal Benefits

Both you and your spouse can take advantage of the QLAC rules. Each household can potentially contribute as high as $250,000.

QLACs allow you to add your spouse as a joint annuitant to the contract. That means the income guarantee is for both lives, regardless of how long either of you live. Note that the contractually guaranteed payment will be lower because the carrier will be covering two lives.

QLACs allow you to list as many beneficiaries to the policy as needed. These beneficiary listings are revocable and can be changed.

You do have an option to guarantee payments to a non-spouse beneficiary, but the rules are a bit complicated and will depend on the specific QLAC product and carrier you choose.

Can I Contribute More?

Yes, kiss QLAC's cousin DIA (Deferred Income Annuity), also known as a Longevity Annuity where premiums must start by 70 1/2. Because QLACs have a premium limitation of 25% of your total IRA assets or $125,000 (whichever is less), people should use Longevity Annuities (DIAs) outside of their IRA if guaranteed future income is needed or the goal. With non-qualified (non-IRA) DIAs, there is no premium limitation. In combination with QLACs, DIAs can shore up any contractual income needs that you may have and can complement Social Security and pension payments.

QLAC Benefits and QLAC Limitations

Benefits:

- Principal protection via a fixed annuity structure
- Lifetime income guarantee regardless of how long you live
- No annual fees
- Simple and easy to understand… fewer moving parts
- Transparent contractually guaranteed proposal from the carrier (request a quote here)
  You can structure the policy to provide a legacy to your beneficiaries
- Younger workers in a participating 401k can plan for future income needs
- You can defer up to 15 years, or age 85, with a Traditional IRA
- COLAs(Cost of Living Adjustments) can be added to the QLAC Policy to contractually and incrementally increase the income stream
- You can ladder QLAC contracts to have income starting at different dates
- Money can be added to the QLAC contract (specific rules apply)
- Traditional IRAs, 401ks, 403(b)s and eligible governmental deferred compensation plans can offer QLACs

Limitations:

- Lack of liquidity relative to the principle amount
- No growth component during deferral years
- Rigid contract structure
- No cash surrender value
- Premium limits of 25% of your total IRA or $125,000, whichever is less
- QLACs are optional for 401k type plan sponsors
- Roth IRAs, Defined Benefit Plans, and non-governmental 457 plans cannot house QLACs(but you can buy a traditional Longevity Annuity – DIA in non-qualified accounts

IF I HAVE MORE QUESTIONS ABOUT QLACs

Questions to answer before you request a QLAC quote:

How you structure the contract will determine the amount of monthly income you receive. Thus, it is important to know which questions to ask to properly structure the policy to meet your desired income goals. The following questions will fill in the blanks, literally, for the type of contract that best fits your needs. It is important that you focus on the phrase "you choose" when determining what benefits work best for you relative to a QLAC.

Do you want the payout to be single-life or joint-life?

Lifetime income payments from annuities are primarily based on your life expectancy at the time you take the payment. In the annuity world of make believe definitions this payment is referred to as mortality credits or mortality yield.

Even though a single person owns an IRA account, you can choose to structure the lifetime income to pay for the lives of both the IRA owner and the owner's spouse. Common sense dictates that the guaranteed payments for two lives will be less than one life, but many like the option of taking care of their spouse with a QLAC guaranteed income stream.

Choosing who will receive the income is a decision you will make when the contract is established. Do you want the surviving spouse to receive income should they outlive you? Or, would you like more income now and the payment to stop upon the owner's death? You choose.

Should I add a return-of-premium guarantee?

A common fallacy about annuities is that the annuity company always keeps the money if the owner passes away early in the contract. That is only one of many ways to structure the payout, and it's referred to as "life only." Some QLACs allow you to choose life only, which does provide the highest guaranteed payout.

However, you can also add a return of premium, or ROP, guarantee to your QLAC contract as well. For example, if you pass away during the income-stream phase, your listed beneficiaries would receive any unused amount and the annuity company wouldn't keep a penny.

Choosing this benefit comes down to the objective at the time of setting up the contract structure. You as the contract owner have total control of how the money is distributed during your lifetime and, should you die early, you can control the distribution after your death. You choose.

Does a COLA rider make sense?

Cost of living adjustment (COLA) riders are attachments to a policy that will annually increase your income by the percentage you choose at the time of application. This feature might sound too good to be true, but annuity companies have the big buildings for a reason — they don't give anything away and they know how to calculate everything.

If you add a COLA rider to your QLAC policy, the initial income payment will be lower than if you didn't add the COLA. That doesn't mean you should not consider a COLA, but you should ask your agent to show you both quotes (with and without) to compare the payout differential.

Choosing the COLA rider is a matter of deciding to have less now and the income to increase each year by the rate you chose at the time of starting the QLAC contract. It boils down to life expectancy and longevity. Unfortunately, those are areas insurance companies are the masters of the universe in performing calculations. Despite all that, you choose.

What are my total IRA assets?

QLACs allow you to use the lessor of 25% of your total IRA assets (non-Roth) or $125,000, whichever is less. For example, if you have $500,000 in total IRA assets, then you can place $125,000 in a QLAC.

If you are married QLACs are available for both spouses assuming each has an IRA or qualified plan. Taking advantage of this for both IRA accounts adds to the planning opportunities. You choose.

When do I want the lifetime income to start?

QLAC rules allow you to defer the income start date to as far out as age 85. You can start the payments any time before age 85, and you might choose to stagger income start dates at 75, 80, and 85 using multiple contracts.

If you don't want to defer payments until age 72 or longer using a QLAC doesn't offer you much benefit. The guaranteed income is still available, but the key feature is to defer beyond the required minimum distribution rules. If you want to have income earlier you may want to consider a Deferred Income Annuity which doesn't limit the contract amount deposited from a qualified plan. In the example above of having an IRA of $500,000 you could convert as much of that amount as needed to create the income desired guaranteed. You choose.

How many QLAC carriers fit my parameters?

It's important to know that QLAC issuers won't always offer every benefit. For example, some might offer "Life Only" as a payout choice, and some may not. Even with the handful of companies currently offering QLACs, not every option is available with every carrier. Make sure you shop all the carriers that fit your specific contractual goals. Don't look at only one QLAC company. Carriers will offer different payout options and rates… all the more reason to get quotes from all the ones that fit your needs. You choose.

What will be my potential RMD *(Required Minimum Distribution)* tax savings?

One of the unique benefits of the QLAC product is that the premium amount isn't part of your required minimum distribution (RMD) calculation. For example, a $500,000 IRA asset total would allow you to place $125,000 into a QLAC. When you calculate your RMDs using this scenario, the amount used would be $375,000 instead of $500,000. Thus, the distribution amount normally required from the $125,000 avoids the income tax levied on the distribution amount. The savings will vary based on your age, taxable income and state of residence. That said, it is worth the time to investigate the benefits. You choose.

5 RULES for Deciding if a QLAC is Right for You

RULE ONE – Not everyone qualifies to own a QLAC. You must own a qualified plan and it must qualify according to the regulation. An IRA, TSA, SEP-IRA, 457b, or 401k all qualify for a QLAC. Thus, if you don't have one of these, you don't qualify.

RULE TWO – You want to defer up to 25% or a maximum of $125,000 into a QLAC for future income.

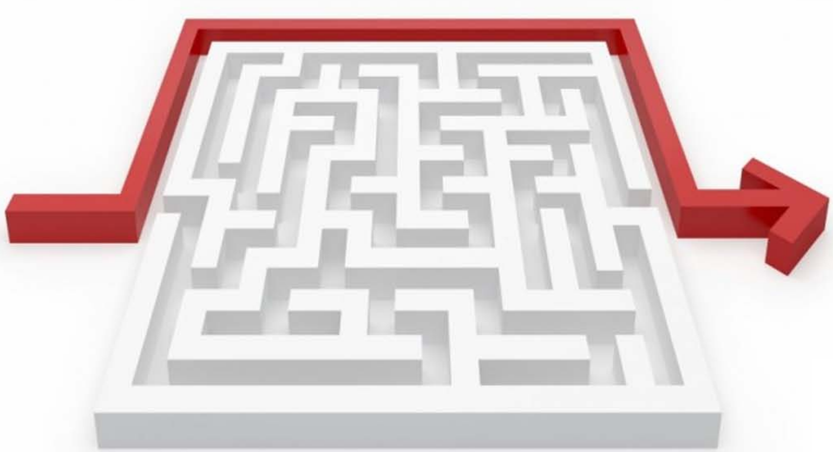
RULE THREE – You want to take advantage of the deferral benefits beyond age 72. Less than that can be done in the qualified plan you already have.

RULE FOUR – Your primary focus is future income guaranteed. (Income Insurance)

RULE FIVE – Your objective is to defer taxes on your qualified plan as long as possible. Up to age 85. (Legacy planning for your heirs)

WANT MORE INFORMATION? GET A LIVE QUOTE

QLAC



Simplified

Guaranteed Income You Can't Outlive
&
Tax Advantaged Treatment of RMDs