No images? Click here

ATAXPLAN PUBLICATIONS

CHOATE'S NOTES: October 2023

Your QLAC is now a twofer.

The "qualifying longevity annuity contract" or QLAC was created by IRS regulation to allow IRA owners to use IRA funds to provide for guaranteed income later in life. The QLAC annuity payout begins at age 85 (or earlier) and lasts for the life of the IRA owner (and within limits the life of the owner's designated beneficiary).

The IRA owner purchases the contract inside an IRA (a separate IRA created for this contract, funded via IRA-to-IRA transfer from existing IRA) sometime before reaching the payout start date. The limit on the amount of IRA money that could be used to purchase a QLAC was originally $125,000 (or 25% of the IRA owner's combined IRA account balances if less).

Why was a special regulation needed to permit this?

Because the QLAC starting point is age 85, so it is an exception to the usual mandatory starting point for RMDs (age 70½ at the time).

But aside from the desire to have a guaranteed income stream later in life, purchasing a QLAC in the IRA had a secondary advantage, pertaining to required minimum distributions (RMDs): The amount invested in the QLAC (and, later, the value of the QLAC, including its growth) were excluded from the "year end account value" used to determine RMDs to the IRA owner. Thus, during the pre-age-85-years, RMDs would be somewhat smaller than they would have been if $125,000 had not been transferred out of the "IRA account balance" and into the "deferred immediate annuity." This was of special appeal

to IRA owners who became subject to RMDs while still working and earning in their 70's.

Of course, there was a tradeoff.
Once payouts under the QLAC began at age 85, the IRA owner would be receiving that taxable income—AND the RMDs as usual from the rest of the IRA assets (the "non-annuitized" part of the IRA). And just as the QLAC value had always been excluded from the "year end account value" for computing RMDs from the non-annuitized portion of the IRA, the QLAC payout did not count towards those RMDs either, once the annuity payout started.

Now along comes SECURE 2.0 and says: *You can have your cake and eat it too!*
Where an IRA owner has annuitized all or part of his IRA (such as by purchasing a QLAC), the IRA owner can elect at any time to have the fair market value of the annuity amalgamated with the rest of the IRA assets for RMD purposes—so the value of the contract will be included in the numerator (prior year-end account value) for purposes of computing the RMD, and distributions from the contract will count toward the RMD from the combined account and contract.

The only requirements are, the election must apply to all of the IRA owner's accounts and IRA-owned annuity contracts, and the applicable IRA providers must permit this.

So: Exclude the QLAC from RMD computation value while it's accumulating, but count the payout towards RMDs when it starts paying out. A twofer!

To put frosting on this cake, SECURE 2.0 increased the maximum QLAC investment to $200,000.

Example: Jerry, age 75, owns a $2 million IRA invested in a diversified portfolio of stocks and bonds. Since Jerry is still working, his $81,632.65 RMD is taxed at a hefty bracket.

Suppose $200,000 from that IRA had been invested into a QLAC which will start payouts to Jerry at age 85 (by which time Jerry will be retired). The $2 million account balance is reduced to $1,800,000 and the age-75 RMD would have been only $73,469. The QLAC purchase produces a small but helpful reduction of the RMD, saving a few thousand dollars of current income taxes. And Jerry may well feel more comfortable with stock market investments knowing that this annuity will provide some fixed income for life, perhaps considering this annuity part of the "bonds" allocation of the portfolio.

At age 85 the QLAC will start paying out the hopefully hefty annuity. But then, thanks to SECURE 2.0, Jerry can elect to treat the (annually declining) QLAC value as part of the "prior year end balance" of all his combined IRAs and the annuity payouts as part of the RMD. Since the QLAC is producing an income flow, this may allow Jerry to more easily maintain the stock/bond balance of the IRA's other investments in later years.

Needless to say, the QLAC is not a good move unless the annuity contract itself is a good investment with a favorable payout from a strong insurer. But assuming you find such a QLAC, you can thank SECURE 2.0 for this "twofer!" Thanks to my financial advisor Bryce Schintzius, Beverly Deveny and Mike Jones for their helpful comments on this issue.

I plan to cover this and other important SECURE 2.0 changes in my upcoming **Boston Tax Institute webinar** on November 3.

For details or to register, visit:

Estate Planning for Retirement Benefits after SECURE & SECURE 2.0
Live Video Conference – Boston Tax Institute, LTD.

Can’t make it to the BTI webinar?
For more upcoming webinars, and seminars, visit:

Natalie Choate’s Seminar Schedule at Ataxplan Publications

Happy Halloween,

Natalie Choate

“...thank you for all your books and lectures.
You make a crazy legal topic almost sane!”

—Susan, CPA

Natalie B. Choate, Esq.
Ataxplan Publications
Wellesley, Massachusetts

Choate's Notes October 2023

Unsubscribe