Retirement Income
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Will the 'BIC' Affect QLAC Sales?

By Kerry Pechter *Thu, Sep 24, 2015*

We're talking about the DOL's proposed Best Interest Contract exemption and sales of Qualified Longevity Annuity Contracts. "Most firms will just pass on this uncertainty and risk," said Caleb Callahan, chief operating officer of ValMark Securities.

Is an element of the DOL fiduciary proposal at odds with the Treasury Department's QLAC provision? During the House Finance Committee hearing on the DOL proposal earlier this month and in written testimony, a financial services industry executive suggested that it is.

Caleb Callahan, chief operating officer (below right) at ValMark Securities in Akron, Ohio, argued that the DOL's proposed amendment to "PTE [Prohibited Transaction Exemption] 84-24" contains language that would discourage his firm and other firms from selling Qualifying Longevity Annuity Contracts to IRA owners because it raises questions of fiduciary liability. He says that the amendment leaves open the possible interpretation that sellers of QLACs might have to meet the new "BIC" (Best Interest Contract) exemption, which involves pledging to act purely in a client's best interest.

"The DOL proposed rule would make it difficult, if not impossible, for our business to offer these critical retirement savings products to our clients, contradicting this Treasury Department initiative and sending a conflicting message to Americans," Callahan wrote in testimony submitted to the DOL. He testified as chairman of the Association of Advanced Life Underwriters' Retirement Planning Committee.

Reish: QLACs fall under 84-24

QLACs are deferred income annuity contracts (DIAs), sold to IRA owners, whose income payments don't begin until after the owner reaches age 70½. Before action by the Treasury Department in July 2014, sales of DIAs were problematic because their terms conflicted with rules requiring that distributions from tax-favored accounts begin at age 70½.

The Treasury Department capped QLAC premiums at the lesser of $125,000 or 25% of tax-favored savings, and required that income from a QLAC start by age 85.

But prominent pension law attorney Fred Reish told RIJ that the amendment won’t affect advisors who want to recommend QLACs to their clients. “As I look at it from a purely legal perspective, I don’t think it will be that big a change for QLACs. That’s because QLACs, as far as I know, are fixed annuities (from the general accounts of insurance companies) and therefore fall under 84-24,” Reish told *RIJ* in an email.

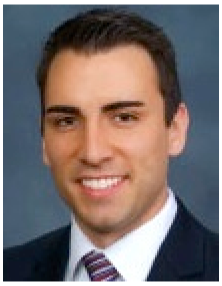
The language of the proposed amendment seems clear on this point. It says that the DOL wants to deprive only sellers of variable annuities and certain sellers of mutual funds of the existing exemption from fiduciary liability when earning a commission on such sales to IRA owners. According to the DOL/Employee Benefits Security Administration website:

“The amendment would revoke relief for insurance agents, insurance brokers and pension consultants to receive a commission in connection with the purchase by IRAs of variable annuity contracts and other annuity contracts that are securities under federal securities laws and for mutual fund principal underwriters to receive a commission in connection with the purchase by IRAs of mutual fund shares.”

Instead, sellers of variable annuities to IRA owners and mutual fund underwriters would need to sign a contract pledging that their sales were in the client’s “best interest.” “A new exemption for the receipt of compensation by fiduciaries that provide investment advice to IRA owners is proposed elsewhere in this issue of the Federal Register in the ‘Best Interest Contract Exemption,’” the proposal reads.

A cloud remains over QLACs

Whichever prohibited transaction exemption DOL offers to commission-earning sellers of QLACs, Callahan says, the DOL still considers a QLAC sale to be prohibited transaction by fiduciary, and therefore puts it under a legal cloud. And, regardless of what the DOL intends, if its amendment makes broker-dealers hesitant to sell QLACs for fear violating the regulations, it will effectively frustrate Treasury’s QLAC initiative.



“Each business will need to make a decision on its own basis,” Callahan told *RIJ* in an email. “But it is pretty clear these are prohibited and you would need to choose an exemption to avoid the prohibition. (That’s why you need an exemption…because it’s prohibited). I'm suggesting for many businesses, including ours—we would choose not to take this risk."

Callahan added that, even if selling QLACs is safe, recommending the sale of IRA assets to fund a QLAC might not be. "In addition, while the actual sale of the QLAC… could be exempted under 84-24—although it is unclear—the act of advising on how much and when to take [money] out of other plan funds and put [it] into the QLAC is not able to be exempted. In practice, most firms will just pass on this uncertainty and risk when you look at the typical account size and risk/reward. The fact is, it is unclear. And all that matters is what businesses actually do."

Impact on VA sales

If any annuity appears to be in the DOL's cross-hairs, it would be variable annuities, not QLACs. Advisors sells tens of billions of dollars worth of VAs each year, and the market for QLACs is undeveloped. The DOL proposal to amend 84-24 is clearly aimed at making sure that the sale of a variable annuity is in the IRA owner's best interest.

"[PTE] 84-24 was first issued in 1979 and then updated in 1984 (hence the 84 in the name)," Reish wrote in an email. "A number of broker-dealers and insurance companies have successfully used that exemption for many years. … It has some proposed changes–mainly the fiduciary standard (the "best interest" requirement) and the prohibition on misleading statements. But I think that, for quality agents and advisors, that will be manageable.

"For other types of annuities—meaning variable annuities—sold to IRA owners, the changes will be much more material," he added. "That's because those sales, or recommendations, will be under BICE, which will be better than largely anticipated, but more burdensome than 84-24."