



Impacts of Tax Cuts and Jobs Act on Life and Annuity Administrative Processing

The largest Federal tax legislation in over thirty years was signed into law by President Trump the last week of 2017. The new legislation will impact corporations and individuals in many forms. The effective date for the legislation is January 1, 2018.

While primary public discussions surrounding the legislation focus on reducing corporate income tax rates to better align with global competition, there are also many subtle changes included that have not received much attention. These changes will impact some forms of life and annuity contract owner behaviors and increase reporting requirements of life insurers.

Original drafts of the House and Senate versions of the tax bill proposed many areas of change that impacted qualified plans, including changes to contribution thresholds for various types of plans and discussions concerning caps on pre-tax contributions, emphasizing Roth type contributions in full or in part. At the end of the long negotiation process, few of these proposed changes made it to the final stage. Three administrative topics, however, did survive and will impact individuals and insurers alike in administration of life and annuity contracts.

Roth Recharacterizations/Roth Reconversions

For IRA and Roth IRA annuities, administrative support will require a change to supported processes.

Old federal tax code allowed an individual to convert some or all of a pre-existing pre-tax traditional IRA into a Roth IRA and to pay income taxes on the amount converted in that tax year. The law also allowed the owner to recharacterize or 'undo' that action, going from the Roth conversion amount, back into pre-tax IRA classification, in full or in part, if the decision in hindsight turned out not to be a good one and the new goal is to 'undo' the taxable event. The new law disallows this 'undoing' action; once a decision is made to convert from traditional IRA to Roth IRA values, it is permanent. Current administrative support uses special IRS reporting codes to report the now-disallowed process. These special codes will no longer be available for use.

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Loan Treatments on 403b Plan Loans

If a participant in any 403b contracts, including 403b annuity contracts, has taken out a loan and then terminates employment, old law required that the unpaid loan balance must be paid off immediately or the unpaid loan became taxable immediately. This strict treatment has been relaxed to allow for loan repayment by as late as personal tax filing to avoid the taxable 'deemed distribution' under the old law.

Life Settlement Transactions Calculations and Reporting

If a life insurance contract is sold as a life settlement arrangement, calculation of the basis involved in determining taxability was confusing and difficult. In addition, reporting was lax and the Federal government had no consistent manner to track the sales events or the later death claim process. The new law now:

- Mandates new tax reporting rules when a life insurance contract is sold as part of a life settlement
- Outlines how parties to the transaction will calculate tax basis
- Reverses IRS Revenue Ruling 2009-13 on how to calculate tax-basis
- Mandates new reporting by insurer to IRS
 - (1) when a policy sale occurs to include policy basis and
 - (2) when a death benefit is later processed on a life settlement contract.

Expect more detail from Treasury on how to handle reporting requirements.

All of these changes are effective on January 1 of this year 2018, so it is important to make the administrative changes to your software as soon as possible to be in compliance.

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