JULY 10, 2015

IRS Puts a Halt to Lump Sum Windows for In-Pay Retirees

On July 9, 2015, the IRS announced its intention to propose rules prohibiting defined benefit pension plans from offering temporary lump sum windows to retirees receiving annuities. Although the proposed rules have not yet been issued, the IRS has announced the prohibition will be effective retroactive to July 9, 2015, with certain grandfathered exceptions noted below. As a result, plan sponsors will not have the opportunity to offer lump sum windows before the effective date unless planning for the lump sum windows was well underway. (See "Grandfathered Windows" below.)

Background. Lump sum windows have been a key pension de-risking strategy in recent years. Although they offer participants greater control over their retirement savings, lump sum windows have drawn criticism from regulators and participant rights groups who believe they transfer risk from the plan and plan sponsor to individual participants who in many cases lack the sophistication to manage investment and longevity risks.

Recent Guidance. The availability of lump sum windows to participants who are already receiving annuities was unclear under the required minimum distribution (RMD) regulations, which generally prohibit annuity payments from increasing over time. However, the IRS issued a series of private letter rulings (PLRs) beginning in 2012 holding that a temporary lump sum window does not violate the non-increasing annuity rule because it is part of an amendment to increase benefits.

Reversing Course. Notice 2015-49 rejects the interpretation of the RMD rules reflected in this series of PLRs by announcing that the IRS will modify these regulations to permit only amendments that increase the amount of *ongoing* annuity payments; amendments to accelerate payments will be prohibited under the RMD regulations.

Effective Date. The changes announced in Notice 2015-49 are expected to become effective as of July 9, 2015. Accordingly, lump sum windows offered to retirees receiving annuities are prohibited immediately unless they qualify for the grandfathering described below.

Grandfathered Windows. The changes will **not** apply to certain grandfathered lump-sum windows, including those, which as of July 9, 2015, have been:

- Adopted or authorized by a board of directors or other committee with authority to amend;
- Communicated in writing to participants; or
- Reflected in a binding collective bargaining agreement.

The IRS is not overturning its holdings applicable to the parties who have received PLRs on lump sum

windows. Further, the IRS announced that it will not challenge lump sum windows that qualify for the grandfathered treatment described above.

Impact on Other De-Risking Strategies. The effect of Notice 2015-49 is limited to lump sum windows offered to retirees already receiving annuity payments. It does not affect offer lump sums offered to participants at retirement or windows for deferred vested participants.

Further, this guidance does not prohibit pension risk transfers by way of terminating a plan or portion of a plan by purchasing a group annuity contract. However, in many cases plan sponsors offer lump sum windows before they proceed with the purchase of a group annuity contract to decrease the overall cost of an annuity purchase. As a result, Notice 2015-49 may impact the implementation of de-risking through purchasing an annuity contract.