

109TH CONGRESS
1ST SESSION

H. R. 3912

To amend the Internal Revenue Code of 1986 to encourage guaranteed lifetime income payments from annuities and similar payments of life insurance proceeds at dates later than death by excluding from income a portion of such payments.

IN THE HOUSE OF REPRESENTATIVES

SEPTEMBER 27, 2005

Mrs. JOHNSON of Connecticut (for herself, Mrs. JONES of Ohio, and Mr. ENGLISH of Pennsylvania) introduced the following bill; which was referred to the Committee on Ways and Means

A BILL

To amend the Internal Revenue Code of 1986 to encourage guaranteed lifetime income payments from annuities and similar payments of life insurance proceeds at dates later than death by excluding from income a portion of such payments.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the “Flexible Retirement
5 Security for Life Act of 2005”.

1 **SEC. 2. EXCLUSION FOR LIFETIME ANNUITY PAYMENTS.**

2 (a) LIFETIME ANNUITY PAYMENTS UNDER ANNUITY
 3 CONTRACTS.—Subsection (b) of section 72 of the Internal
 4 Revenue Code (relating to annuities) is amended by add-
 5 ing at the end thereof the following new paragraph:

6 “(5) EXCLUSION FOR LIFETIME ANNUITY PAY-
 7 MENTS.—

8 “(A) IN GENERAL.—In the case of lifetime
 9 annuity payments received under one or more
 10 annuity contracts in any taxable year, gross in-
 11 come shall not include 50 percent of the portion
 12 of lifetime annuity payments otherwise includ-
 13 ible (without regard to this paragraph) in gross
 14 income under this section. For purposes of the
 15 preceding sentence, the amount excludible from
 16 gross income in any taxable year shall not ex-
 17 ceed the applicable amount.

18 “(B) APPLICABLE AMOUNT.—For purposes
 19 of subparagraph (A), the applicable amount
 20 shall be determined in accordance with the fol-
 21 lowing table:

“Taxable Years Beginning in:	Applicable Amount is:
2006, 2007, 2008, 2009, 2010, or 2011	\$1,000
2012 or 2013	\$5,000
2014	\$10,000
2015 or thereafter	\$20,000.

1 “(C) COST-OF-LIVING ADJUSTMENT.—In
2 the case of taxable years beginning after De-
3 cember 31, 2015, the \$20,000 amount in sub-
4 paragraph (A) shall be increased by an amount
5 equal to—

6 “(i) such dollar amount, multiplied by

7 “(ii) the cost-of-living adjustment de-
8 termined under section 1(f)(3) for the cal-
9 endar year in which the taxable year be-
10 gins, determined by substituting ‘calendar
11 year 2005’ for ‘calendar year 1992’ in sub-
12 paragraph (B) thereof.

13 If any amount as increased under the preceding
14 sentence is not a multiple of \$500, such amount
15 shall be rounded to the next lower multiple of
16 \$500.

17 “(D) APPLICATION OF PARAGRAPH.—Sub-
18 paragraph (A) shall not apply to—

19 “(i) any amount received under an eli-
20 gible deferred compensation plan (as de-
21 fined in section 457(b)) or under a quali-
22 fied retirement plan (as defined in section
23 4974(c)),

1 “(ii) any amount paid under an annu-
2 ity contract that is received by the bene-
3 ficiary under the contract—

4 “(I) after the death of the annu-
5 itant in the case of payments de-
6 scribed in subsection (c)(5)(A)(ii)(III),
7 unless the beneficiary is the surviving
8 spouse of the annuitant, or

9 “(II) after the death of the annu-
10 itant and joint annuitant in the case
11 of payments described in subsection
12 (c)(5)(A)(ii)(IV), unless the bene-
13 ficiary is the surviving spouse of the
14 last to die of the annuitant and the
15 joint annuitant, or

16 “(iii) any annuity contract that is a
17 qualified funding asset (as defined in sec-
18 tion 130(d)), but without regard to wheth-
19 er there is a qualified assignment.

20 “(E) INVESTMENT IN THE CONTRACT.—

21 For purposes of this section, the investment in
22 the contract shall be determined without regard
23 to this paragraph.”.

1 (b) DEFINITIONS.—Subsection (c) of section 72 of
2 such Code is amended by adding at the end thereof the
3 following new paragraph:

4 “(5) LIFETIME ANNUITY PAYMENT.—

5 “(A) IN GENERAL.—For purposes of sub-
6 section (b)(5), the term ‘lifetime annuity pay-
7 ment’ means any amount received as an annu-
8 ity under any portion of an annuity contract,
9 but only if—

10 “(i) the only person (or persons in the
11 case of payments described in subclause
12 (II) or (IV) of clause (ii)) legally entitled
13 (by operation of the contract, a trust, or
14 other legally enforceable means) to receive
15 such amount during the life of the annu-
16 itant or joint annuitant is such annuitant
17 or joint annuitant, and

18 “(ii) such amount is part of a series
19 of substantially equal periodic payments
20 made not less frequently than annually
21 over—

22 “(I) the life of the annuitant,

23 “(II) the lives of the annuitant
24 and a joint annuitant, but only if the
25 annuitant is the spouse of the joint

1 annuitant as of the annuity starting
2 date or the difference in age between
3 the annuitant and joint annuitant is
4 15 years or less,

5 “(III) the life of the annuitant
6 with a minimum period of payments
7 or with a minimum amount that must
8 be paid in any event, or

9 “(IV) the lives of the annuitant
10 and a joint annuitant with a minimum
11 period of payments or with a min-
12 imum amount that must be paid in
13 any event, but only if the annuitant is
14 the spouse of the joint annuitant as of
15 the annuity starting date or the dif-
16 ference in age between the annuitant
17 and joint annuitant is 15 years or
18 less.

19 “(iii) EXCEPTIONS.—For purposes of
20 clause (ii), annuity payments shall not fail
21 to be treated as part of a series of substan-
22 tially equal periodic payments—

23 “(I) because the amount of the
24 periodic payments may vary in accord-
25 ance with investment experience, re-

1 allocations among investment options,
2 actuarial gains or losses, cost of living
3 indices, a constant percentage applied
4 not less frequently than annually, or
5 similar fluctuating criteria,

6 “(II) due to the existence of, or
7 modification of the duration of, a pro-
8 vision in the contract permitting a
9 lump sum withdrawal after the annu-
10 ity starting date, or

11 “(III) because the period between
12 each such payment is lengthened or
13 shortened, but only if at all times
14 such period is no longer than one cal-
15 endar year.

16 “(B) ANNUITY CONTRACT.—For purposes
17 of subparagraph (A) and subsections (b)(5) and
18 (x), the term ‘annuity contract’ means a com-
19 mercial annuity (as defined by section
20 3405(e)(6)), other than an endowment or life
21 insurance contract.

22 “(C) MINIMUM PERIOD OF PAYMENTS.—
23 For purposes of subparagraph (A), the term
24 ‘minimum period of payments’ means a guaran-

1 teed term of payments that does not exceed the
2 greater of 10 years or—

3 “(i) the life expectancy of the annu-
4 itant as of the annuity starting date, in the
5 case of lifetime annuity payments de-
6 scribed in subparagraph (A)(ii)(III), or

7 “(ii) the life expectancy of the annu-
8 itant and joint annuitant as of the annuity
9 starting date, in the case of lifetime annu-
10 ity payments described in subparagraph
11 (A)(ii)(IV).

12 For purposes of this subparagraph, life expect-
13 ancy shall be computed with reference to the ta-
14 bles prescribed by the Secretary under para-
15 graph (3). For purposes of subsection
16 (x)(1)(C)(ii), the permissible minimum period of
17 payments shall be determined as of the annuity
18 starting date and reduced by one for each sub-
19 sequent year.

20 “(D) MINIMUM AMOUNT THAT MUST BE
21 PAID IN ANY EVENT.—For purposes of subpara-
22 graph (A), the term ‘minimum amount that
23 must be paid in any event’ means an amount
24 payable to the designated beneficiary under an
25 annuity contract that is in the nature of a re-

1 fund and does not exceed the greater of the
2 amount applied to produce the lifetime annuity
3 payments under the contract or the amount, if
4 any, available for withdrawal under the contract
5 on the date of death.”.

6 (c) RECAPTURE TAX FOR LIFETIME ANNUITY PAY-
7 MENTS.—Section 72 of such Code is amended by redesi-
8 gnating subsection (x) as subsection (y) and inserting after
9 subsection (w) the following new subsection:

10 “(x) RECAPTURE TAX FOR MODIFICATIONS TO OR
11 REDUCTIONS IN LIFETIME ANNUITY PAYMENTS.—

12 “(1) IN GENERAL.—If any amount received
13 under an annuity contract is excluded from income
14 by reason of subsection (b)(5) (relating to lifetime
15 annuity payments), and—

16 “(A) the series of payments under such
17 contract is subsequently modified so any future
18 payments are not lifetime annuity payments,

19 “(B) after the date of receipt of the first
20 lifetime annuity payment under the contract an
21 annuitant receives a lump sum and thereafter is
22 to receive annuity payments in a reduced
23 amount under the contract, or

24 “(C) after the date of receipt of the first
25 lifetime annuity payment under the contract the

1 dollar amount of any subsequent annuity pay-
2 ment is reduced and a lump sum is not paid in
3 connection with the reduction, unless such re-
4 duction is—

5 “(i) due to an event described in sub-
6 section (c)(5)(A)(iii), or

7 “(ii) due to the addition of, or in-
8 crease in, a minimum period of payments
9 within the meaning of subsection (c)(5)(C)
10 or a minimum amount that must be paid
11 in any event (within the meaning of sub-
12 section (c)(5)(D)),

13 then gross income for the first taxable year in
14 which such modification or reduction occurs
15 shall be increased by the recapture amount.

16 “(2) RECAPTURE AMOUNT.—

17 “(A) IN GENERAL.—For purposes of this
18 subsection, the recapture amount shall be the
19 amount, determined under rules prescribed by
20 the Secretary, equal to the amount that (but for
21 subsection (b)(5)) would have been includible in
22 the taxpayer’s gross income if the modification
23 or reduction described in paragraph (1) had
24 been in effect at all times, plus interest for the

1 deferral period at the underpayment rate estab-
2 lished by section 6621.

3 “(B) DEFERRAL PERIOD.—For purposes
4 of this subsection, the term ‘deferral period’
5 means the period beginning with the taxable
6 year in which (without regard to subsection
7 (b)(5)) the payment would have been includible
8 in gross income and ending with the taxable
9 year in which the modification described in
10 paragraph (1) occurs.

11 “(3) EXCEPTIONS TO RECAPTURE TAX.—Para-
12 graph (1) shall not apply in the case of any modi-
13 fication or reduction that occurs because an annu-
14 itant—

15 “(A) dies or becomes disabled (within the
16 meaning of subsection (m)(7)),

17 “(B) becomes a chronically ill individual
18 within the meaning of section 7702B(e)(2), or

19 “(C) encounters hardship.”.

20 (d) LIFETIME DISTRIBUTIONS OF LIFE INSURANCE
21 DEATH BENEFITS.—

22 (1) IN GENERAL.—Subsection (d) of section
23 101 of such Code (relating to life insurance pro-
24 ceeds) is amended by adding at the end thereof the
25 following new paragraph:

1 “(4) EXCLUSION FOR LIFETIME ANNUITY PAY-
2 MENTS.—

3 “(A) IN GENERAL.—In the case of
4 amounts to which this subsection applies, gross
5 income shall not include the lesser of—

6 “(i) 50 percent of the portion of life-
7 time annuity payments otherwise includible
8 in gross income under this section (deter-
9 mined without regard to this paragraph),
10 or

11 “(ii) the amount in effect under sec-
12 tion 72(b)(5).

13 “(B) RULES OF SECTION 72(B)(5) TO
14 APPLY.—For purposes of this paragraph, rules
15 similar to the rules of section 72(b)(5) and sec-
16 tion 72(x) shall apply, substituting the term
17 ‘beneficiary of the life insurance contract’ for
18 the term ‘annuitant’ wherever it appears, and
19 substituting the term ‘life insurance contract’
20 for the term ‘annuity contract’ wherever it ap-
21 pears.”.

22 (2) CONFORMING AMENDMENT.—Paragraph (1)
23 of subsection (d) of section 101 of such Code is
24 amended by adding “or paragraph (4)” after “to the
25 extent not excluded by the preceding sentence”.

1 (e) EFFECTIVE DATE.—

2 (1) IN GENERAL.—The amendments made by
3 this section shall apply to amounts received in cal-
4 endar years beginning after the date of the enact-
5 ment of this Act.

6 (2) SPECIAL RULE FOR EXISTING CON-
7 TRACTS.—In the case of a contract in force on the
8 date of the enactment of this Act that does not sat-
9 isfy the requirements of section 72(c)(5)(A) of the
10 Internal Revenue Code of 1986 (as added by this
11 section), or requirements similar to such section
12 72(c)(5)(A) in the case of a life insurance contract),
13 any modification to such contract (including a
14 change in ownership) or to the payments thereunder
15 that is made to satisfy the requirements of such sec-
16 tion (or similar requirements) shall not result in the
17 recognition of any gain or loss, any amount being in-
18 cluded in gross income, or any addition to tax that
19 otherwise might result from such modification, but
20 only if the modification is completed prior to the
21 date that is 2 years after the date of the enactment
22 of this Act.

1 **SEC. 3. ANNUITY AND LIFE INSURANCE CONTRACTS WITH**
2 **LONG-TERM CARE INSURANCE RIDERS.**

3 (a) EXCLUSION FROM GROSS INCOME.—Subsection
4 (e) of section 72 of the Internal Revenue Code of 1986
5 (relating to amounts not received as annuities) is amended
6 by redesignating paragraph (11) as paragraph (12) and
7 by inserting after paragraph (10) the following new para-
8 graph:

9 “(11) SPECIAL RULES FOR CERTAIN COMBINA-
10 TION CONTRACTS PROVIDING LONG-TERM CARE IN-
11 SURANCE.—Notwithstanding paragraphs (2), (5)(C),
12 and (10), in the case of any amount applied against
13 the cash value of an annuity contract or the cash
14 surrender value of a life insurance contract as pay-
15 ment for coverage under a qualified long-term care
16 insurance contract which is part of or a rider on
17 such annuity or life insurance contract—

18 “(A) the investment in the contract shall
19 be reduced (but not below zero) by such
20 amount, and

21 “(B) such amount shall not be includible
22 in gross income.”.

23 (b) TREATMENT OF COVERAGE PROVIDED AS PART
24 OF A LIFE INSURANCE OR ANNUITY CONTRACT.—Sub-
25 section (e) of section 7702B of such Code (relating to

1 treatment of qualified long-term care insurance) is amend-
2 ed to read as follows:

3 “(e) TREATMENT OF COVERAGE PROVIDED AS PART
4 OF A LIFE INSURANCE OR ANNUITY CONTRACT.—

5 “(1) COVERAGE TREATED AS CONTRACT.—Ex-
6 cept as otherwise provided in regulations prescribed
7 by the Secretary, in the case of any long-term care
8 insurance coverage (whether or not qualified) pro-
9 vided by a rider on or as part of a life insurance
10 contract or an annuity contract, this title shall apply
11 as if the portion of the contract providing such cov-
12 erage is a separate contract.

13 “(2) APPLICATION OF SECTION 7702.—Section
14 7702(e)(2) (relating to the guideline premium limi-
15 tation) shall be applied by increasing the guideline
16 premium limitation with respect to the life insurance
17 contract, as of any date—

18 “(A) by the sum of any amount (other
19 than premium payments) applied against the
20 life insurance contract’s cash surrender value
21 (within the meaning of section 7702(f)(2)(A))
22 for coverage made to that date under the life
23 insurance contract, less

24 “(B) any such amounts the application of
25 which reduces the premiums paid for the life in-

1 surance contract (within the meaning of section
2 7702(f)(1)).

3 “(3) PORTION DEFINED.—

4 “(A) IN GENERAL.—For purposes of this
5 subsection, the term ‘portion’ means only the
6 terms and benefits under a life insurance con-
7 tract or annuity contract that are in addition to
8 the terms and benefits under the contract with-
9 out regard to long-term care insurance cov-
10 erage.

11 “(B) TREATMENT OF DISTRIBUTION FOR
12 PURPOSES OF TITLE.—For purposes of this
13 title, any distribution made pursuant to the
14 terms of the long-term care portion of the con-
15 tract shall be treated as made solely under such
16 portion, irrespective of the effect of the dis-
17 tribution on the cash value of the annuity con-
18 tract portion or the cash surrender value of the
19 life insurance contract portion.

20 “(4) ANNUITY CONTRACTS TO WHICH PARA-
21 GRAPH (1) DOES NOT APPLY.—For purposes of this
22 subsection, none of the following shall be treated as
23 an annuity contract:

24 “(A) A trust described in section 401(a)
25 which is exempt from tax under section 501(a).

1 “(B) A contract—
2 “(i) purchased by a trust described in
3 subparagraph (A),
4 “(ii) purchased as part of a plan de-
5 scribed in section 403(a),
6 “(iii) described in section 403(b),
7 “(iv) provided for employees of a life
8 insurance company under a plan described
9 in section 818(a)(3), or
10 “(v) from an individual retirement ac-
11 count or an individual retirement annuity.

12 Any dividend described in section 404(k) which is
13 received by a participant or beneficiary shall, for
14 purposes of this paragraph, be treated as paid under
15 a separate contract to which subparagraph (B)(i)
16 applies.”.

17 (c) TAX-FREE EXCHANGES AMONG CERTAIN INSUR-
18 ANCE POLICIES.—

19 (1) EXCHANGE OF LIFE INSURANCE, ENDOW-
20 MENT, AND ANNUITY CONTRACTS FOR LONG-TERM
21 CARE CONTRACTS.—Subsection (a) of section 1035
22 of such Code (relating to general rules) is amended
23 by striking the period at the end of paragraph (3)
24 and inserting “; or” and by adding after paragraph
25 (3) the following new paragraph:

1 “(4) a contract of life insurance, contract of en-
2 dowment insurance, or annuity contract for a quali-
3 fied long-term care insurance contract.”.

4 (2) ANNUITY CONTRACTS CAN INCLUDE QUALI-
5 FIED LONG-TERM CARE INSURANCE.—Paragraph (2)
6 of section 1035(b) of such Code is amended by add-
7 ing at the end the following new sentence: “For pur-
8 poses of the preceding sentence, a contract shall not
9 fail to be treated as an annuity contract solely be-
10 cause a qualified long-term care insurance contract
11 is a part of or a rider on such contract.”.

12 (3) LIFE INSURANCE CONTRACTS CAN INCLUDE
13 QUALIFIED LONG-TERM CARE INSURANCE.—Para-
14 graph (3) of section 1035(b) of such Code is amend-
15 ed by adding at the end the following new sentence:
16 “For purposes of the preceding sentence, a contract
17 shall not fail to be treated as a life insurance con-
18 tract solely because a qualified long-term care insur-
19 ance contract is a part of or a rider on such con-
20 tract.”.

21 (4) TAX-FREE EXCHANGES OF QUALIFIED
22 LONG-TERM CARE INSURANCE CONTRACT.—Sub-
23 section (a) of section 1035 of such Code (relating to
24 certain exchanges of insurance policies), as amended
25 by paragraph (1), is amended by striking “or” at

1 the end of paragraph (3), by striking the period at
2 the end of paragraph (4) and inserting “; or”, and
3 by inserting after paragraph (4) the following new
4 paragraph:

5 “(5) a qualified long-term care insurance con-
6 tract for a qualified long-term care insurance con-
7 tract which only covers the same insured.”.

8 (d) QUALIFIED LONG-TERM CARE COVERAGE
9 TREATED AS QUALIFIED ADDITIONAL BENEFITS UNDER
10 LIFE INSURANCE CONTRACT.—Subparagraph (A) of sec-
11 tion 7702(f)(5) of such Code (defining qualified additional
12 benefits) is amended by striking “or” at the end of clause
13 (iv), by redesignating clause (v) as clause (vi) and insert-
14 ing after clause (iv) the following new clause:

15 “(v) coverage under a qualified long-
16 term care insurance (as defined under sec-
17 tion 7702(B)(e)).”.

18 (e) EFFECTIVE DATES.—

19 (1) IN GENERAL.—Except as provided by para-
20 graph (2), the amendments made by this section
21 shall apply to contracts issued after the date of the
22 enactment of this Act.

23 (2) SUBSECTION (c).—The amendments made
24 by subsection (c) shall apply with respect to ex-

1 changes occurring after the date of the enactment of
2 this Act.

○