PENSION RIGHTS CENTER

NATIONAL WOMEN'S LAW CENTER
EXPANDING THE POSSIBILITIES

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Office of Regulations and Interpretations
Employee Benefits Security Administration
Room N-5655
U.S. Department of Labor
200 Constitution Avenue, NW
Washington, DC 20210

Attention: Pension Benefit Statements Project
RIN 1210-AB20

The Pension Rights Center and the National Women's Law Center commend the Department of Labor for considering proposed regulations that would require pension benefit statements for defined contribution plans to include lifetime income calculations.

BACKGROUND

The last several decades have seen a remarkable change in employer-sponsored plans. Today's workers are far less likely than yesterday's workers to participate in a defined benefit pension plan which pays a guaranteed monthly benefit throughout retirement. If they participate in a plan at all, it is likely to be a defined contribution plan—probably a self-directed 401(k) plan—where they must choose to participate, decide how much to contribute, manage their investments while they work' and manage their investments and the draw-down while they are retired.

Given these challenges for participants in defined contribution plans, tomorrow's retirees, on average, will have less retirement savings and run a greater risk of outliving those savings than retirees of the last generation.[1] In this new defined contribution environment a secure retirement requires advance planning based on solid information about retirement income options.

Participants in self-directed defined contribution plans receive quarterly statements giving the dollar value of their accounts and participants in other defined contribution plans receive annual statements. While participants can watch their account values change with time and investment returns, they also need information to assess whether their account balance will – or will not – be adequate to provide income through all of their years of retirement. Without that information

[1] See Alicia H. Munnell, Anthony Webb, and Francesca Golub-Sass, "The National Retirement Risk Index: An Update," Center for Retirement Research at Boston College, October 2012, Brief Number 12-20. http://crr.bc.edu/wp-content/uploads/2012/11/IB_12-20-508.pdf

participants have a greater chance of misinterpreting the value of their accounts for retirement, especially of overestimating the adequacy of their retirement savings. Translating lump sum numbers into monthly income provides numbers that are more understandable to the average participant. Lifetime income calculations, *with appropriate explanations*, would give participants a more realistic view of their account balances and better enable them to plan for their retirement years.

ISSUES AND DISCUSSION

The Labor Department's proposal includes lifetime income calculations for both current and projected account balances. We address these two sides of the proposal separately.

<u>Current Account Balances</u>

We urge the Labor Department to adopt a lifetime income calculation requirement, including joint and survivor calculations where appropriate, for defined contribution plan participant benefit statements. A lifetime income calculation for current account balances should be a requirement, not an option.

We agree with the methodology adopted in the ANPRM. The assumptions that payment begins immediately and the participant has reached normal retirement age are reasonable and would be readily understood by a typical participant. The ANPRM safe harbor interest rate and unisex mortality assumptions, when accompanied by appropriate explanations, also seem reasonable. It is our view that the Labor Department has chosen reasonable, well-publicized government figures for the safe harbor. This is important to participants who will be on the receiving end of the calculations. Direct, uncomplicated numbers are easier to explain and will be readily understood by participants. Many sponsors may choose to use the safe harbor formulas so that participants moving between employers, and spouses who may have different employers, would benefit from a consistent basis for the estimates.

We do not think that plans with annuity features should be required to use the plan's annuity calculations. Some plans, for example, may have more than one embedded annuity option. Although it is important for participants to see actual numbers if possible, especially participants nearing retirement, a requirement to use a plan's calculations could present complications for plan administrators who might have to match participants with their specific investment options. A better solution would be to permit, but not require, the use of a plan's annuity calculations as an alternative safe harbor, which would be available when the annuity purchase option is available to a participant. If an annuity calculation is related to a specific investment option, that information should be included in the explanation accompanying the lifetime income estimate. Similarly, if a plan administrator chooses not to use the plan's annuity calculations, the explanation accompanying the lifetime income calculation should clearly state that the plan's annuity option could differ.

We are pleased the ANPRM would *require* that lifetime income for a married participant be presented as a 50 percent joint and survivor benefit as well as a single life annuity. Since monthly income is lower when survivor benefits are chosen, married participants and their spouses need to know the joint and survivor estimate for informed retirement planning. Our experience in answering participant questions leads us to believe this information is essential. We recommend, however, that the sample Table 2 included in the ANPRM be revised slightly to separate the single life annuity estimate from the joint and survivor annuity estimate. The joint and survivor estimate could be presented below the single life estimate with an explanatory heading stating the joint and survivor estimates are for married participants. If presented in this fashion the plan administrator would not have to select out married participants. This separation would also make the numbers less confusing to the average participant.

We also are pleased that the conversion safe harbor uses a unisex mortality table. We support the suggestion that benefit statements include an explanation of the consequences of purchasing an annuity outside of an employer plan that may use gender-based mortality tables. For plans not using the safe harbor or in-plan annuity calculations, we recommend a requirement that the plan specify whether the mortality assumptions are gender-based and how that affects pricing for women, men, and couples.

Projected Account Balances

While we strongly support the lifetime income calculation requirement for current account balances, we suggest that *projected* account balances and the accompanying lifetime income calculations be made optional, and not a requirement for benefit statements. Plans that choose to provide projected account balances should be required to also provide the associated lifetime income calculation. And we recommend that the Labor Department continue to develop appropriate guidance and a safe harbor for those plans that choose to give projected account balances.

The safe harbor assumptions in the ANPRM for projecting account balances are overly optimistic and thus the average plan participant approaching retirement could find that the actual balance at retirement is much less than anticipated. We believe there is less risk for participants in anticipating and planning for lower benefits and later finding a greater benefit amount as they approach retirement, than in discovering too late that their retirement savings are inadequate.

We recommend two adjustments in the safe harbor assumptions for projecting account balances that would result in lower estimates. The safe harbor projection of participant contributions to normal retirement age includes a 3 percent annual increase in contributions. The ANPRM states the annual increase in contributions is based on anticipated increases in salary over the course of a career. While some participants may have rising wages on a regular basis, many others will not be so fortunate.[2] A projection based on current contribution levels without an annual increase will be more understandable to the average participant. Since benefit statements are provided on a regular basis, the effects of salary increases will be reflected in changes to the projections from one year to the next.

[2] The median weekly earnings of men in full-time employment expressed in constant 1982-1984 dollars have remained the same, with small variations, since 1980. See “Weekly and hourly earnings data from the Current Population Survey,” Department of Labor, Bureau of Labor Statistics, BLS Data Series LES1252881900.

The investment return assumption of 7 percent is overly optimistic. The combined assumptions in the ANPRM result in a 4 percent real rate of return. More realistic assumptions for the average participant, who tends to invest conservatively, would be in the neighborhood of a 2 to 3 percent real rate of return. Thus, we recommend that the 7 percent nominal return on investments be adjusted down to a more realistic level. It is preferable for participants to be pleasantly surprised with their investment gains rather than face financial problems at retirement due to overly optimistic assumptions.

In addition, the Labor Department should specify parameters for those sponsors who do not use the safe harbor to project account balances. Relying on "reasonable assumptions taking into account accepted investment theories" is too vague for guidance. The Department should consider specifying that projections be based on assumptions appropriate for the typical plan participant and that they be applied consistently. An example of an appropriate and consistent assumption would be the use of the same projection assumptions for all participants in the plan, rather than varying assumptions by the age of participants.

We agree that projected account balances should be discounted for inflation and presented in current dollars. The ANPRM asks whether the projected balance should be given on the benefit statement or just the projected lifetime income estimate. Without knowing the projected balance upon which it is based, participants will not be able to properly interpret a projected lifetime income estimate. The projected account balance should be included in the benefit statement.

Explanations of Calculations and Assumptions

Just as important as the lifetime income estimates for current account balances and projected account balances will be the explanations of the calculations and assumptions. Explanations must be written in a manner easily understood by participants. We recommend that the Labor Department write model explanations to accompany the ANPRM safe harbor lifetime income calculations.[3] Model language can be used with the safe harbor calculations and can serve as a guide for plan sponsors who do not use the safe harbors.

The ANPRM appropriately requires disclosure and explanations of all assumptions. Assumptions should include whether the mortality table is gender-neutral and an explanation of pricing differences for men and women (including clarification that sex-based tables will yield higher annuities for men than for women with the same account balance). Besides explanations of specific assumptions, helpful model language would include the statement that calculations are estimates only and that changes in the values of the variables will alter the estimate of lifetime income. Participants should be reminded that benefit statements should be kept for future reference and comparison. An explanation of how interest rates affect the conversion from account balance to lifetime income would help the average participant, including young participants making their initial savings decisions and especially for those near retirement. Additionally, plan participants nearing retirement should be advised to check annuity prices in the market which may differ from the lifetime income estimate on the benefit statement. We

[3] The Pension Protection Act of 2006 directed the Secretary of Labor to develop one or more model benefit statements to be used by plan administrators.

also suggest that benefit statements be required to include a reference to the Labor Department website for further information and for use of the calculator.

<u>Miscellaneous Issues</u>

The ANPRM asks whether providing lifetime income estimates once a year instead of quarterly would be sufficient for participants. We agree that an annual estimate should be enough provided that the estimate is given with the same quarterly statement each year, such as every first quarter. If estimates are provided annually they should alert participants that the lifetime income estimate is included.

Including joint and survivor lifetime income estimates on all statements, not just on those for married participants, would be acceptable. However, as stated previously, we recommend that the joint and survivor estimate be presented on a separate line from the single life annuity. The joint and survivor estimate should be accompanied by a clear heading that indicates the estimate is for married participants only.

We believe that both participants and employers would be helped by a published table of conversion factors, periodically updated and based on the safe harbor assumptions. We hope that the Labor Department will publish such a table as part of this regulatory initiative.

<u>Conclusion</u>

For the average participant the information provided on the benefit statement, along with Social Security statements, will form the basis of retirement planning. We commend the Labor Department for proposing to require that benefit statements for defined contribution plans include lifetime income estimates. Lifetime income estimates provide essential information for participants to understand their total accrued benefits when planning for retirement.

We appreciate the opportunity to comment on this important initiative.

Sincerely,

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