

Lifetime income options

By Marcia S. Wagner, Esq.

One of the key retirement security goals of the Obama Administration is to “reduce barriers to annuitization of 401(k) plan assets” and promote “guaranteed lifetime income products, which transform at least a portion of retirees’ savings into guaranteed future income, reducing the risks that retirees will outlive their savings or that their living standards will be eroded by investment losses or inflation.”¹

DOL and IRS request for information. In connection with the Administration’s goals to promote DC plan annuitization, the DOL, Internal Revenue Service, and the Treasury Department issued a joint release on February 2, 2010, requesting information regarding lifetime income options for participants in retirement plans. In this release, these agencies announced that they were currently reviewing the rules under ERISA and the related rules under the Internal Revenue Code to determine whether and how they could enhance the retirement security of participants by facilitating access to lifetime income arrangements. The requests for information addressed a range of topics, including participant education, required disclosures, 401(k) plan and other tax-qualification rules, selection of annuity providers, ERISA Section 404(c), and QDIAs.

Unlike the Administration’s other initiatives to promote retirement security, the push towards lifetime income options is still in its infancy (as reflected by the RFI from the Labor and Treasury Departments).

The Retirement Security Project. The Retirement Security Project, a joint venture of the Brookings Institution and the Urban Institute, has released two white papers regarding DC plan annuitization. These papers were co-authored by Mark Iwry, who was appointed by the Treasury Secretary to serve as the Deputy Assistant Secretary for Retirement and Health Policy. The white papers include proposals to encourage DC plan annuitization by using deferred annuities as the default investment for participants for certain purposes.

Legislative proposals. A number of bills have been introduced in Congress that are designed to provide tax incentives to save for retirement through annuities (e.g., Lifetime Pension Annuity for You Act, Retirement Security for Life Act). These bills typically encourage annuitization by exempting a percentage of annuity income up to a

stated threshold (e.g., \$5,000 for individuals or \$10,000 for couples). Although they typically do not extend this exemption to annuity payments from defined benefit plans, they do exempt annuity payments made from DC plans.

In contrast to these tax-related measures, the Lifetime Income Disclosure Act puts a different spin on the subject of lifetime income and 401(k) plans.² Under this proposed legislation, 401(k) plan sponsors would be required to inform participants annually of how their account balances would translate into guaranteed monthly payments—a “retirement paycheck for life.” The goal of this legislation is to give participants an understanding of how much projected retirement income they can expect from their savings. The legislation directs the DOL to issue tables that employers may use in calculating an annuity equivalent and model disclosures. Employers and service providers that use the model disclosure and guideline assumptions would be insulated from liability under ERISA.

Tax requirements. The IRS addressed various tax-qualification requirements for DC plans with variable group annuity investment options for participants in PLR 200951039. This private letter ruling was helpful to the benefits community because it illustrated how these plans were viewed with respect to the age 70½ minimum distribution requirements and for purposes of the QJSA rules. In sum, DC plans with annuity investment options were not subject to any “surprise” interpretations with respect to these rules.

In conclusion, there will be much discussion and legislative and/or regulatory movement in the areas of DC annuitization in the coming months and years. ♦

Notes

1. Annual Report of the White House Task Force on the Middle Class, February 2010.
2. U.S. Senators Jeff Bingaman (D-NM), Johnny Isakson (R-GA), and Herb Kohl (D-WI) introduced this bill in December 2009.

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