DOL Lifetime Income Disclosure Regulation

By Barry Salkin and Roberta Casper Watson

In 2019, the SECURE Act amended Section 105 of ERISA. That section requires participant benefit statements to be distributed to participants and beneficiaries, and prescribes the contents of the benefit statements. The SECURE Act amendments require that participant account balances in defined contribution plans be expressed as both a life annuity and a qualified joint and survivor annuity ("QJSA"), in addition to the other mandated disclosures. In August of 2020, the DOL released an interim final regulation detailing the new lifetime income disclosures required to comply with the SECURE Act.

The new regulation applies to defined contribution plans whether or not they in fact provide annuities as a form of distribution. The regulation is not effective until September 18, 2021, one year after it is published in the Federal Register, at which time the next benefit statement that is issued after that date must contain the required disclosures. Although issued as an interim final regulation, the DOL is allowing a 60-day comment period, and it hopes to improve the regulation, before its effective date, based on the responses it receives to those comments.

The new disclosures must be made once every 12 months. So long as they are made fully in accordance with the new regulation, plan sponsors, fiduciaries and others are shielded from liability arising out of such disclosures.

The new regulation defines "participant" to include a beneficiary with an account under the plan, and gives the example of an alternate payee under a qualified domestic relations order.

The regulation prescribes specific assumptions to be used by a plan administrator in quantifying the lifetime income streams. First, the annuity commencement date should be the last day of the statement period. Second, a participant who is age 67 or less should be assumed to be age 67 on that commencement date. If a participant is over age 67, the participant's actual age should be used. After considering several other ages, the Department chose age 67 because it is the full normal retirement age under Social Security for most workers. The Department requests comments on whether age 67 is the most appropriate age, and also on whether disclosure should be required assuming multiple ages at commencement.

Third, the plan administrator should assume that the participant is married, regardless of the participant's actual marital status, and should assume that the participant's spouse is the same age as the participant. For the QJSA illustration, the plan administrator should assume that 100% of the monthly payment continues to the spouse following the death of the participant.

Fourth, a plan administrator should assume an interest rate equal to the 10-year constant maturity Treasury ("CMT") securities yield for the first business day of the last month of the period to which the benefit statement relates. The Department requests comments on whether this is the best interest rate, and on whether it would be better to base the calculation on that rate as of the last business day of the last month of the benefit statement period instead of the first business day of that month.

Fifth, the plan administrator should convert a participant's account balance assuming mortality based on the applicable mortality table under Section 417(e)(3)(B) of the Internal Revenue Code (the "Code"). The Department notes that this is a unisex mortality table. The Department requests comments on whether this is the best table, and on whether use of a unisex table is the best approach.

The Department chose not to add a specific insurance load factor, to cover the profit an insurance company would make in issuing an annuity, believing that a sufficient load factor is inherent in the 10-year CMT interest rate, but it requests comments on whether it would be better for an additional load factor to be used.

The Department chose not to require an inflation-adjusted income stream, but the regulation does require an explanation that the purchasing power of the stated amount will decline over time due to inflation. The Department requests comments on whether an inflation-adjusted stream would be preferable. The Department also chose not to require disclosures based a term certain or any other features common to annuities, but requests comments on whether it would be better to do so. The Department also chose not to factor future contributions and earnings into the disclosures.

Certain informational disclosures are required, and model language is provided to meet each disclosure. The regulation requires that each disclosure be included, but makes the model language optional. However, plan fiduciaries must use the model language to benefit from the liability relief provided by the regulation. The model language is provided in two formats – one as a separate statement accompanying each required disclosure, and the other as a consolidated Model Benefit Statement Supplement. The following informational disclosures are required:

1. The assumed date on which the payments start and the assumed age of the participant on that date, and a statement explaining the impact of payments beginning at a younger or an older age.
2. An explanation of what a single life annuity is.
3. An explanation of what a 100% QJSA is, and a statement that a lesser survivor percentage may be available and what the impact would be of having a lesser survivor percentage.
4. The assumption that the participant is married to a spouse of the same age as the participant, and an explanation of the impact of having a spouse who is younger or older than that age.
5. An identification of the interest rate being used, an explanation of how it was determined, a statement that it fluctuates with market conditions, and an explanation of the impact on the benefit of a higher or lower interest rate.
6. An explanation of the mortality assumptions used.
7. A statement that the payments described are for illustrative purposes only and are not guaranteed.
8. An identification of various factors that could cause the participant's actual monthly income, based on the current account balance, to differ from the illustration, including the participant's actual age at retirement, the actual account balance, and the market conditions at the time. Also required is a statement that an annuity purchased outside of an employer's plan may provide larger payments for males than females.
9. An explanation that the amounts illustrated will not be adjusted for inflation, and the impact of that fact on purchasing power over time.
10. An explanation that 100% vesting is assumed, regardless of the participant's actual vested percentage.
11. An explanation that, for a participant who has taken a plan loan and is not in default, the loan is assumed to be repaid. This explanation is not required for a plan that does not have a participant loan program.

The Department requests comments on both the substance of the disclosures and the model language, and on the model language in both the separate statement format and the Model Benefit Statement Supplement.

If a plan has in-plan distribution annuities, deferred annuities, or both, special rules apply. If distributions may be taken in the form of actual annuities purchased under contract from an insurance company under the plan, an optional special rule allows the plan administrator to base its disclosures on the actual annuities that the participant may receive instead of the hypothetical annuities described in the regulation. Illustrations using the special rule still must assume that the first payment is made on the last day of the statement period, that the participant is 67 (unless actually older on such date), and that the participant has a spouse of the same age on such date. The interest assumption would be based on the contract rate and mortality assumptions as specified in the contract, rather than on the DOL's regular prescribed assumptions. Illustrations may use the percentage survivor's benefit specified in the contract if less than 100%. The additional required explanations must be made. A separate Model Benefit Statement Supplement is provided for plans distributing annuities, and the Department requests comments on all aspects of the special rule and the modifications related to it.

If a plan allows participants to purchase deferred income annuities ("DIAs") during the accumulation phase of their participation in the plan, the regulation provides adaptations to the regular rules for the portion of a participant's account balance that is actually invested in a DIA. For that portion of the benefit, the assumptions of the participant's DIA are to be substituted for the hypothetical assumptions otherwise provided. The regular disclosure rules apply, however, to any portion of the participant's accrued benefit not used to purchase a DIA.

Because participants select the age at which payments under a DIA will commence, the plan administrator must also disclose the frequency and amount of deferred income stream payments under the contract as of the commencement date in current dollars, as well as any survivor benefit, period certain commitment, or similar feature. Also required is a statement as to whether the deferred income stream payments are fixed or will adjust with inflation or in some other way during retirement, and a general explanation of how any such adjustment is determined. Inaccurate statements, such as that the illustrations are only hypothetical, are to be omitted. To avoid double counting of the DIA, the value of the DIA is excluded from the account balance subject to the other disclosures required by the regulation. The Department requests comments on the special rule for DIAs. No model disclosure language is provided for DIAs because the model language is for hypothetical illustrations and the DIA information is factual based on specific contracts.

There is no relief from liability for the DIA disclosures or for additional hypothetical disclosures that many plan administrators already provide for their participants. However, the Department requests comments on whether there should be a safe harbor for this type of additional information provided to participants, to help them in planning for their retirement.

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