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LEGAL ALERT

May 8, 2013

DOL Issues Advance Notice of Proposed Rulemaking on Lifetime Income Estimates in Plan Participant Statements

On May 7, 2013, the Department of Labor released an advance notice of proposed rulemaking (ANPRM) that seeks commentary on requiring a projection of estimated lifetime income to be included in participant statements from defined contribution plans subject to the reporting and disclosure provisions of the Employee Retirement Income Security Act of 1974, as amended (ERISA).

- The ANPRM follows on from the Request for Information Regarding Lifetime Income Options for Participants and Beneficiaries in Retirement Plans jointly published by DOL and the Treasury Department in February 2010 (RFI). It takes up the important policy question of how best to educate participants about the adequacy of their defined contribution plan savings for retirement income security.

- Although the ANPRM includes the preliminary text of a potential regulation (and an illustration of its potential application), an ANPRM is not itself a proposed rulemaking. Rather, it is a request for comments on policy, concepts and specific regulatory language in advance of a proposed regulation.

The ANPRM posits and asks for commentary on a potential regulation that would require participant statements to include the following, on a quarterly basis:

- The participant's current account balance at the end of the statement period.

- The participant's projected account balance at normal retirement age (NRA) under the plan, for participants who have not yet reached that age. The projection would be based on "reasonable assumptions taking into account generally accepted investment theories," but must be expressed in current dollars and take into account future contributions and investment returns. The intent is to allow best practices to continue to evolve and for statements to be consistent with online or other tools provided to participants, subject to a reasonableness standard.

  The regulation would, however, provide an optional safe harbor if the following assumptions were used, along with each participant's current account balance and years to NRA:

  - Contributions continuing at the current rate to NRA, increasing by 3% annually (as a proxy for the effect of wage increases);
  - A nominal investment rate of return of 7%; and
  - A discount rate of 3% to account for inflation in converting the projected account balance into current dollars.

- The participant's projected lifetime income at NRA based on the current account balance. The projection would be derived from the following assumptions:

  - For the income starting date, the later of NRA or the participant's current age;

  - For the form of projected income, level monthly payments under a single life annuity and, for married participants, also under a joint and 50% survivor annuity (assuming the participant and spouse are the same age); and
  - For mortality and interest assumptions, "reasonable assumptions taking into account accepted actuarial principles." For plans offering an in-plan commercial annuity, the mortality and interest assumptions in that product would be used. The regulation would also provide another optional safe harbor for using (i) interest equal to the 10-year constant maturity Treasury securities rate for the first business day of the last month in the statement period and (ii) mortality assumptions from the IRC § 417(e)(3)(b) table published from time to time by the Treasury Department (for converting annuity payments to lump sums under the survivor annuity rules for qualified plans). These safe harbor assumptions would not take into account the commercial costs of purchasing a lifetime annuity from an insurance company.

- A similar projection of lifetime income at NRA based on the projected account balance at that age.

- An "understandable" explanation of the assumptions and a disclaimer that the projections are estimates and not guarantees.

DOL has also posted on its website an online lifetime income calculator that follows the principles outlined in the ANPRM.

The ANPRM effectively requests comments on all aspects of the proposed regulation it posits, including the following:

- Are income estimates based on both current and projected account balances the best approach?
- Are the mechanics of making the estimates of future account balances and income payments appropriate? For example, should Social Security retirement age be used instead of NRA? Are the various assumptions optimal? Should the commercial costs of an annuity contract be included in the income estimates?
- When plans include, as an investment option, annuity products that accumulate units of guaranteed lifetime income over the participant's working life, how should that income be reflected in the estimates?
- Would this approach adequately address the liability concerns expressed in response to the RFI?
- Are there ways to make the regulation more cost effective? For example, what would be the cost/benefit effect of requiring the estimates only annually, rather than quarterly? Would it be helpful for DOL to publish tables for making the estimates based on the safe harbor assumptions?
- What, if any, guidance would be required to coordinate any such regulation with the Financial Industry Regulatory Authority (FINRA) rule prohibiting projections of performance?

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If you have any questions about this Legal Alert, please feel free to contact any of the attorneys listed below or the Sutherland attorney with whom you regularly work.

Adam B. Cohen	202.383.0167	adam.cohen@sutherland.com
Mikka Gee Conway	202.383.0827	mikka.conway@sutherland.com
Carol T. McClarnon	202.383.0946	carol.mcclarnon@sutherland.com
Alice Murtos	404.853.8410	alice.murtos@sutherland.com
Joanna G. Myers	202.383.0237	joanna.myers@sutherland.com
Vanessa A. Scott	202.383.0215	vanessa.scott@sutherland.com
W. Mark Smith	202.383.0221	mark.smith@sutherland.com
Rich Sun	202.383.0833	rich.sun@sutherland.com
William J. Walderman	202.383.0243	william.walderman@sutherland.com
Carol A. Weiser	202.383.0728	carol.weiser@sutherland.com