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DOL Presses Forward With Lifetime Income Disclosure in Defined Contribution Plans

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On August 18, 2020, the Department of Labor (the "DOL") issued an interim final rule (the "IFR") implementing Section 203 of the Setting Every Community Up for Retirement Enhancement Act of 2019 (the "SECURE Act"), which requires an annual lifetime income disclosure for 401(k) and other ERISA defined contribution plan participants. [See Groom Alert: Lifetime Income Provisions Under the SECURE Act].

Lifetime income disclosure has long been a focus of legislative and regulatory efforts. Section 203 of the SECURE Act was originally the bipartisan Lifetime Income Disclosure Act, which was first introduced in 2009. That bill was then incorporated into the USA Retirement Funds Act of 2014 – sponsored by the Chair of the Senate Committee on Health, Education, Labor and Pensions – and the 2016 Retirement Enhancement and Savings Act – sponsored by the Chair and Ranking Member of the Senate Finance Committee. It was then picked up by the House as part of the SECURE Act. The DOL also began work on a lifetime income disclosure rule almost a decade ago. The agency issued an advanced notice of proposed rulemaking ("ANPR") in 2013 and received public comments. However, the DOL did not finalize the rule.

I. Key Takeaways

- The IFR applies to all ERISA-covered defined contribution plans (*e.g.*, 401(k), 403(b) plans), regardless of whether annuities/lifetime income investment options are offered in the plan.
- The IFR requires plan administrators to provide at least yearly two lifetime income illustrations (the "LIIs"). The LIIs are estimated monthly payments based on a (1) single life annuity (the "SLA") and (2)

qualified joint and 100% survivor annuity (the "100% QJSA"). Notably, both LIIs are required regardless of whether the participant is single or married.

- The LIIs are based on the participant's account balance as of the last day of the relevant statement period rather than a projected balance that considers future contributions and investment returns.
- The IFR specifies several assumptions that must be used to calculate the LIIs.
- The SECURE Act provides a limitation of fiduciary liability for any plan sponsor, plan fiduciary, or "other person" that furnishes the LIIs in accordance with the DOL's rules. The IFR clarifies that this liability shield only applies if LIIs are provided using the assumptions and the model language provided in the IFR. The IFR further notes that the liability shield does not extend to existing or separate estimates that are not provided in accordance with the IFR.
- The IFR contains special rules for distribution annuities and deferred annuities.
- The DOL requested comments on every major aspect of the IFR and has indicated that it intends to release a final rule in advance of the IFR's effective date.
- Absent any additional action by the DOL, the rule will become effective 12 months after the issuance of the IFR.

II. Required Assumptions for LII Calculations

The LIIs must be calculated based on assumptions specified in the IFR. In this regard, the DOL notes that there are four factors that go into a lifetime income calculation. The following table identifies each of the four factors, and also summarizes the required assumption for each factor:

Factor	Required Assumption under IFR
Commencement Date & Age of Participant on That Date	The IFR assumes that the annuity commencement date will be the last day of the relevant benefit statement period. Unless the participant is over 67 (in which case, the participant's actual age will be used), the IFR assumes that the participant will be 67-years-old on the commencement date.
Marital Status	The IFR assumes a 100% QJSA (which is the most generous benefit for a surviving spouse), with an assumption that the spouse is the same age as the participant. The DOL notes that although it considered a 50% contingent annuity assumption, which was used in the DOL's 2013 ANPR, it chose 100% for the IFR given that it "believes there is a benefit to showing the participant these extremes because all other annuity options fall somewhere in between."

Interest Rate	The IFR requires using the 10-year Constant Maturity Treasury ("CMT") rate for the interest rate assumption. The DOL notes that comments received in response to its 2013 ANPR suggested that the CMT best represents the actual pricing of commercial annuities.
Mortality	The IFR incorporates the unisex mortality tables provided by the IRS in Code section 417.

The LII calculations also assume that participants will be 100% vested in their account balances and will repay any outstanding loan amounts. In addition, the LII calculations do not take into account "insurance loads," (i.e., an insurer's spread), the impact of inflation, or any projections for a participant's account balance to reflect future contributions and investment gains.

III. Overview of Participant Disclosure

The participant disclosure must list the participant's account balance as of the last day of the statement period and identify the two LIIs (i.e., the hypothetical monthly payments based on an SLA and 100% QJSA). To accompany these figures, the disclosure must also include the following explanations "written in a manner calculated to be understood by the average plan participant":

- The commencement date and age assumptions (including how commencing benefits earlier/later could reduce/increase monthly benefit payments).
- What a single life annuity is and how it works.
- What a 100% QJSA is and how it works, and the availability and impact of other survivor percentage options.
- The marital status and age of spouse assumptions (including the impact on payments if the spouse is older or younger than the participant).
- Interest rate assumptions and use of the CMT rate.
- Mortality assumptions and use of IRS tables.
- The fact that the illustrations are estimates only and do not constitute guarantees.
- The fact that actual monthly payments may "vary substantially" from the illustrations, and will depend on numerous factors.
- The fact that the illustrations are fixed amounts that will not increase to reflect inflation (i.e., unlike Social Security payments, the illustrations will not be revised based on a cost-of-living adjustment).
- The assumption that the participant is 100% vested in his/her account balance.
- The assumption that the participant will repay any outstanding plan loans.

The DOL notes that while the explanations will help assist participants understand the LIIs, the primary reason for including them is "to clarify to participants that the projected monthly payments are not guarantees."

The IFR includes model language—both on a section-by-section basis and as part of a complete model disclosure—for each of the required explanations. While the model language can be modified to a very limited extent, the DOL cautioned that the language must remain "substantially similar in all material respect" to the model language.

IV. Special Rules for Distribution Annuities and Deferred Income Annuities

The IFR has special rules for distribution annuities and deferred income annuities offered to defined contribution plan participants. For distribution annuities, there is an optional rule to use the interest rate, survivor benefit percentage, and mortality assumptions under the annuity contract's actual terms rather than the assumptions for those factors provided in the IFR.

If the plan offers participants the ability to purchase a deferred income annuity (a "DIA"), the IFR provides that the portion of a participant's account balance that is used to purchase a DIA will be excluded for purposes of calculating the LIIs. Notwithstanding that exclusion, the plan administrator must separately disclose the portion of a participant's account balance that has been used to purchase a DIA, including:

- The frequency and amounts payable under the DIA;
- The date payments are scheduled to commence;
- A description of any survivor benefits, period certain commitments or similar features of the DIA; and,
- Whether and how the payments may be adjusted.

Notably, the IFR does not include model language for the required disclosure for DIAs.

V. Limitation of Fiduciary Liability

The IFR provides a limitation of fiduciary liability for plan sponsors, plan fiduciaries, and "other persons" who furnish LIIs, if the IFR's assumptions and model language are used. Either the section-by-section model language or the complete model disclosure may be used for the limitation of fiduciary liability.

Despite the DOL's stated intention to avoid disruption of current practices, the limitation of fiduciary liability does not extend to preexisting or separate retirement income disclosures that are commonly provided by recordkeepers (i.e., those that are not based on the IFR's assumptions and accompanied by the IFR's model language). Additionally, the DOL explicitly excluded the additional DIA disclosures from the limitation of fiduciary liability. In this regard, the DOL noted that those disclosures are statements of fact rather than projections like the LII. However, many DIA providers currently make the types of disclosures about their product that the IFR requires to avoid requiring the plan administrator to do so.

VI. Observations, Comment Period, and Effective Date

Implementing the IFR may require many recordkeepers and other service providers to develop new systems capable of making the required disclosures. Additionally, recordkeepers that currently provide lifetime income estimates will need to determine if they want to change their estimates in order to conform to the IFR or, alternatively, provide both sets of estimates.

Notably, the DOL has requested comments on nearly every aspect of the IFR. Specifically, the DOL is seeking comments on the assumptions and methodology used to derive the LIIs, the required participant explanations/model language, as well as the overall benefits of the LIIs. The comment period will last for 60 days from the date the IFR is published in the Federal Register. The DOL will then have to decide whether to make any changes before the statutory effective date (*i.e.*, 12 months after the issuance of the IFR).