Get Ready for Lifetime Income Illustrations on Participant Statements

Every quarter, participants receive an email notification (or, in some cases, a paper mailing) indicating a new statement is available for review. For a participant-directed plan, the statement typically includes an account balance, investments held by the participant, and a few other features required by the regulations under section 404a-5. These statements are all about what the participant has accumulated in their account, but the statement typically lacks how the money will look in a stream of income in retirement.

The Setting Every Community Up for Retirement Enhancement Act of 2019 (SECURE Act) amended the Employee Retirement Security Act of 1974 (ERISA), requiring that statements now show a stream of income projection.

Here's What You Really Need to Know:

1. SECURE amended ERISA to add two lifetime income illustrations, furnished at least annually, to pension benefit statements for participant-directed plans.
2. It is the plan administrator's duty to furnish this statement (just like it is the plan administrator's duty to furnish existing participant statements), but in most cases, the recordkeeper prepares the statement on the plan administrator's behalf. Plan administrators should check their agreement with the recordkeeper to confirm whose responsibility it is to prepare and distribute the statements.
3. The Department of Labor (DOL) FAQ from July 2021, clarified that the first statements for participant-directed plans are due to be included on quarterly statements by the second calendar quarter of 2022 (ending June 30, 2022), meaning participants will see their statements change very soon.

Let's Dive In...

As you may recall, the SECURE Act in 2019 (the first one, not the pending second one) included many retirement plan provisions, three of which sought to address the issue of longevity – or rather, people outliving their savings: (1) safe harbor for selection of lifetime income provider, (2) portability for lifetime income options in plans, and (3) disclosures on participant statements. The provision for participant statements wasn't new. In 2013, the DOL started the rulemaking process to try to add this provision, received several comments, and never published a final rule.

So, why did this provision come back again? The goal is to help participants shift their mindset and get better prepared for retirement. According to a Bankrate survey, a combined 68 percent of American workers are either not sure or don't believe they are where they need to be for retirement. Further, many participants have only been taught to save for retirement but haven't been taught to think about how that translates into income and the "magic number" for which they are saving. The provision to add lifetime income disclosures to participant statements seeks to shift this participant mindset (though some are skeptical).

What's the Guidance: Plan fiduciaries should be aware of three key publications from the DOL since SECURE Act passed in 2019:

1. The DOL published a Fact Sheet in August 2020, which was the first publication from the DOL since the SECURE Act's passage. The Fact Sheet provides the quick highlights of the guidance and what's required to comply.

2. The DOL published the Interim Final Rule in the Federal Register in September 2020. This became effective on September 18, 2021, giving rise to the requirement that the first statement for participant-directed plans is due to be included on quarterly statements by the second calendar quarter of 2022 (ending June 30, 2022).

3. The DOL published FAQs on July 26, 2021 to help prepare for the effective date of the Interim Final Rule.

You may notice that one thing missing from this list is the Final Rule, which the DOL indicated would be forthcoming, but which was never published. Given that there is no final rule, the Interim Final Rule is the guidance to follow.

What's Required: This is just the snapshot, so check out the guidance above to get the full rundown, and we will spend our time here talking about the participant communication strategy. Here's the gist:

Using assumptions from the Interim Final Rule (IFR), plan administrators must calculate the monthly payment illustrations of participants' account balances as a single life annuity (SLA) and another as a qualified joint and survivor annuity (QJSA). This must be on a statement that the participant receives at least once a year. The IFR includes an assumed start date, age, interest rate, mortality, and survivor benefits. As you might imagine, these assumptions might conflict with some of the existing calculations that some plan administrators and recordkeepers already provide. However, here are a few things to keep in mind: first, the IFR provides a safe harbor for plan administrators that use the model language from the IFR, and second, the IFR makes some exceptions for those who are already providing lifetime income illustrations that comply with the 2013 proposal's illustrations (see DOL FAQ at Q3).

Considerations for Plan Fiduciaries: Participants have a lot of uncertainty right now. A recent New York Times article referred to it as "inflation anger" and "less confidence [than] at the start of the Covid pandemic, when the unemployment rate was four times as high as it is now. [Participants'] feelings toward the economy are almost as low as they were during the depths of the Great Recession in 2008." Given the uncertainty your participants might be experiencing, they may get a shock when they click to open their next statement.

How can plan sponsors and advisors help?

1. Let participants know that this change is coming and that there might be a new calculation on their next statement.

2. Help participants understand that the method of calculation on their statement might be different from the calculators they have seen in the past.

3. Start a discussion about what it means to think about income in retirement as opposed to only talking about savings. Consider how this discussion looks for participants of different ages, and consider that it applies to those beyond the pre-retiree population.

4. Help participants understand that there isn't a "magic number." As Jamie Hopkins said in a recent article: "If you knew you had just enough retirement savings to cover all your expenses through the end of your life but would have nothing left over, would you take that tradeoff? A lot of people likely would – you'd live very comfortably in retirement, though you'd have nothing to pass on to the next generations of your family. Despite this thought experiment, there's no "magic number" to save for that accomplishes this." While there is no magic number, there is a way to help participants think about what they need to live comfortably in retirement and shift their mindset.

Take a look at the guidance, but more importantly, think about how this can translate to a useful participant communication strategy to help the participants in the plans you work with to think about savings and income planning through a different lens.