August 07, 2013

Office of Regulations and Interpretations,
Employee Benefits Security Administration, Room N–5655,
U.S. Department of Labor
200 Constitution Avenue N.W.
Washington, DC 20210
Attention: Pension Benefit Statements Project.

Re: Regulation Identifier Number RIN 1210–AB20

To Whom It May Concern:

The American Academy of Actuaries[1] Pension Committee is pleased to present the following comments to the Department of Labor, Employee Benefits Security Administration (DOL), regarding its development of proposed regulations for the pension benefit statement requirements under section 105 of the Employee Retirement Income Security Act of 1974, as amended (ERISA). The Pension Committee commends the DOL for developing these proposed regulations. Finding ways to help workers understand the value of lifetime income remains critical to ensuring they can plan for a secure retirement. We offer the following comments on several of the questions raised in the notice.

Assumed Rate of Investment Return

The committee understands the importance of keeping the statements as simple to prepare and understand as possible, and that DOL proposed the 7% safe harbor for the assumed rate of investment return with this goal in mind. However, the committee believes that it is not sufficient for the safe harbor assumption to consist of a single assumed rate of return that applies regardless of the portfolio allocations, investment time horizon, risk tolerance, or current economic conditions. While an assumed return of 7% may be appropriate for participants in certain contexts, in other circumstances this assumption will not be appropriate.

[1] The American Academy of Actuaries is a 17,000-member professional association whose mission is to serve the public and the U.S. actuarial profession. The Academy assists public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

For example, a portfolio that is currently invested 100% in fixed income securities is highly unlikely to generate 7% annual returns in the foreseeable future. For a participant with this asset allocation, a benefit projection based on a 7% rate of return may create an unrealistic retirement income expectation or encourage the participant to take inappropriate investment risks. At the same time, an assumed rate of return that is appropriate for a portfolio of fixed income investments in today's interest rate environment would be equally inappropriate for other allocations or in other economic climates.

The committee believes that to avoid providing participants with potentially misleading information, it is not feasible for the safe harbor to consist of a single assumed rate of return that applies in all instances. It is possible that the DOL could change the safe harbor to a dynamic approach that takes into account factors such as the current interest rate environment, investment horizon, and individual participant portfolio allocations. However, the substantial complexity and expense that this approach would add to the statements makes it potentially unfeasible for many plan sponsors. Instead, the committee recommends that DOL consider amending the safe harbor assumption to include the use of two rates of return. To qualify for the safe harbor, statements would need to show the projected results using both of these assumed rates of return. In addition to the 7% rate of return that the Advance Notice of Proposed Rulemaking (notice) identifies as a safe harbor assumption, the committee recommends that the safe harbor also call for the inclusion of results based on a 5% rate of return. The text of the statement should also note that neither 5% nor 7% is necessarily an appropriate expectation for a particular set of circumstance, and it should direct participants to their financial advisors for guidance. DOL should periodically review these assumed rates of return to ensure that they remain reasonable in future economic climates.

The primary advantage of this approach is that compared to a single 7% assumption, it provides relevant information to participants with a far wider range of portfolio allocations in a variety of economic climates. While it is inevitable that an assumption above 7% or below 5% will be appropriate in a particular situation, it is unlikely that any reasonable assumption will be sufficiently far from this range such that the statement will not provide the participant with useful information. This approach also avoids the implicit suggestion that there is a particular "correct" rate of return against which participants should measure their performance. Lastly, to the extent that participants share the information in these statements with their financial advisors, including projections with two separate rates of return will facilitate a discussion of the relationship between risk and reward that is crucial to long-term financial planning.

Inflation Adjusted Annuity Conversions

The notice calls for annuity conversions that include level payments for the life of the participant. Consistent with the notion of expressing projected information in today's dollars, DOL should extend the safe harbor to permit the use of inflation-protected annuities. One goal of these projections should be to ensure comparability to other information that the participants are receiving. With the continued migration away from private sector defined benefit (DB) plans, fewer and fewer participants will be including level DB annuities in their retirement planning. Meanwhile, nearly all participants will be considering their Social Security "annuities" as part of their retirement finances. Thus, not only is the use of inflation-protected annuities internally consistent with the concept of expressing projected information in today's dollars, it is also consistent with the majority of the other retirement financial planning information that participants will be reading. The illustration of a level dollar annuity payout overstates the inflation-adjusted value of the annuity payments. Providing a benefit estimate with an assumed 3% annual increase will provide a more realistic comparison.

Drawdown Illustrations

The notice discusses the need to help participants understand the "lifetime monthly income that can be generated from an account balance." Because most participants prefer lump sums over annuity or installment options, we believe the inclusion of a draw down illustration would be useful. To help participants understand the potential implications of a draw-down, it is important that the illustration show that it is possible for the participant and spouse to outlive their retirement income under this approach. The committee suggests that DOL consider expanding the notice to provide plan sponsors with the option of including drawdown illustrations in the lifetime income statements. These optional illustrations would be in addition to, not instead of, the mandatory annuitization illustrations.

Projected Retirement Ages

The notice specifies that the results must include projections to participants' normal retirement ages. While this requirement is reasonable for many plans, in many other plans this age is not indicative of when participants are likely to retire. In fact, in many DC plans, the sole purpose of a normal retirement age is to provide for 100% vesting at that age and does not reflect the actual pattern of retirement ages. For example, in some plans that cover workers in physically demanding jobs the normal retirement age may be 65 despite the fact that few participants remain employed until this age. In less physically demanding occupations, many participants are beginning to work until the Social Security full retirement age or later in order to receive larger Social Security benefits. Accordingly, it would be beneficial to plan participants if plan sponsors were allowed to project lifetime incomes commencing at older ages.[2]

The committee suggests that DOL consider allowing the use of the normal retirement age as a safe harbor, while permitting the use of other projection ages if the plan sponsor believes that a different age would be more relevant to the participants. In addition, the committee suggests that the safe harbor also include the use of participants' Social Security full retirement ages, since for many participants this age is more relevant than

[2] Source: NewsDash from PLANSPONSOR.com; June 18, 2013 "Results of Fidelity Investments' "Higher Education Faculty Study," which examined the behaviors and attitudes of Baby Boomer (ages 49 to 67) faculty members at higher education institutions, found 74% plan to delay retirement past the age of 65 or never retire at all. When asked the reasons for this delay, 81% cited professional reasons, while 69% cited economic concerns."

the normal retirement age in their DC plan. A plan sponsor would qualify for the safe harbor if it used either the plan's normal retirement age or Social Security full retirement age as the projected retirement age.

Insurance Loads for Annuity Conversions

According to the notice, the use of the 10-year constant treasury maturities is a result of the recommendation of a commenter whose members include a large majority of the U.S. annuity industry. Specifically, this commenter expressed the view that this rate, "best represents the interest rates that are reflected in actual annuity pricing."

The committee believes that including an explicit insurance load (defined in the notice as "the difference between the market price of lifetime income and the price of actuarially fair lifetime income") is unnecessary because the 10-year treasury basis already implicitly includes one. In other words, the actual discount rate that insurers will apply to the projected lifetime income cash flows when determining pricing will be higher than the 10-year treasury rates. There will be a "pricing spread" between what the insurers use in their internal pricing calculations and the annuity rates offered to consumers. This spread represents both the expenses and profits of the insurer. The 10-year treasury basis is a reasonable approximation for the rate offered to consumers, which already includes an estimate of the insurance load.

Mortality Assumptions for Annuity Conversions

The notice correctly states that the use of a unisex mortality assumption in the case of a participant buying an annuity will overstate the annuity benefit for the female participants and understate it for male participants in most states. The committee believes that the regulations should permit the use of sex-distinct mortality factors, and should include an appropriate sex-distinct table in the safe harbor assumptions. Further, to the extent that unisex factors are used, the proposed communications should properly warn participants of the potential understatement or overstatement of annuities.

The notice discusses the use of the current 417 table as the safe harbor mortality assumption for annuity conversion calculations. There is some merit to the notion that this table should be projected forward to each participant's projected retirement age in order to reflect anticipated mortality improvements. However, the committee believes the use of a projected table overly complicates the calculation and is not necessary, particularly considering the variability of the interest rate used to determine the price of the annuity.

Administrative Concerns

The example in the Appendix to the notice is complicated, which places a burden on the plan sponsor in the production of the statements, and a burden on the participants who will need to read and understand the information. See the committee's sample lifetime income illustrations at the end of this letter. The committee has the following additional recommendations that are intended to minimize the cost of preparing the statements, while making the information more understandable to participants.

- Only require these statements on an annual basis. In most circumstances, it is not necessary or helpful for participants to review their long-term financial planning every three months, and limiting the statements to annual preparation will help mitigate the preparation costs.

- Publish tables of conversion factors. Some plan sponsors and third-party administrators, particularly those involved with smaller plans, lack easy access to the resources necessary to convert participants' account balances into annuities. DOL publication of standard tables would be helpful to plan sponsors in applying the regulation.

- Permit the rounding of results. The results should be rounded, which will reinforce the concept that the benefits shown are estimates and will change. The committee suggests permitting rounding to the nearest $50 or $100 for monthly benefits and to the nearest $1,000 for balances.

- Include a statement about the impact of interest rates on annuitization results. Since interest rate movements are critical to this calculation, and are also likely to be the factor that participants are least likely to consider in their retirement planning, it is appropriate for the illustrations to highlight their impact. The statement, "the actual monthly payments that may be received at normal retirement age will depend on numerous factors" should include the following additional language: "including the interest rate at the time of retirement."

The Pension Committee appreciates the opportunity to comment on these proposed regulations and would be happy to discuss any of these items with you at your convenience. Please contact David Goldfarb, the Academy's pension policy analyst (202-785-7868, goldfarb@actuary.org) if you have any questions or would like to discuss these items further.

Sincerely,

Michael F. Pollack, FSA, MAAA, EA, FCA
Chairperson, Pension Committee
American Academy of Actuaries

Sample Lifetime Income Stream Illustrations

Data

As of 12/31/2013, the balance in your accounts was $125,000. During 2012, you and your employer contributed a total of $10,000 into your accounts. Your current age is 44.

Assumptions

The lifetime income stream illustrations are based on estimated annuity purchase rate is assumed to be $5.00 per $1,000 of account balance for the life only annuity and $4.51 per $1,000 for the joint and 50% survivor annuity. Your beneficiary's age is assumed to equal your age. The purchase rate when you retire will be different than illustrated depending on many factors including your gender and the interest rates at the time you begin drawing your benefits. In the second illustration, your current balance and expected future contributions are accumulated with two rates of return (5% and 7%) from 12/31/2013 to your assumed retirement age (66). The resulting balance is then discounted back to the present time at an annual rate of 3% to show the results in terms of today's dollars. Your future contributions are equal to your and your employer's 2012 contributions with an assumption they will increase by 3% per year.

Annuity Illustrations

The first illustration shows the approximate income you could realize from your current account balance as if you were now at your retirement age.

		Joint and 50% Survivor Form	
Balance	**Your Monthly Annuity Income (life annuity payable to you only)**	**Your Monthly Annuity Income**	**Monthly Annuity Income Payable to Beneficiary after death of Retiree**
$125,000	**630**	**560**	**280**

This second illustration assumes a range of rates of return and assumes you and your employer continue to contribute to the plan at the same dollar amount as in 2013 increased each year by 3%. Your accounts are assumed to earn a rate of return of 5.00% or alternately 7.00%. **The actual result can be more or less than what is illustrated**. The values shown in this chart represent the purchasing power of your future benefits, expressed in terms of today's dollars.

			Joint and 50% Survivor Form	
Rate of Return earned by your account	**Projected Balance**	**Your Monthly Annuity Income (life annuity payable to you only)**	**Your Monthly Annuity Income**	**Monthly Annuity Income Payable to Beneficiary after death of Retiree**
5.00%	415,000	$2,300	$2,100	$1,050
7.00%	627,000	$3,100	$2,800	$1,400