

Are You Looking at Retirement Income Alternatives? The DOL and IRS Are!



ASPPA

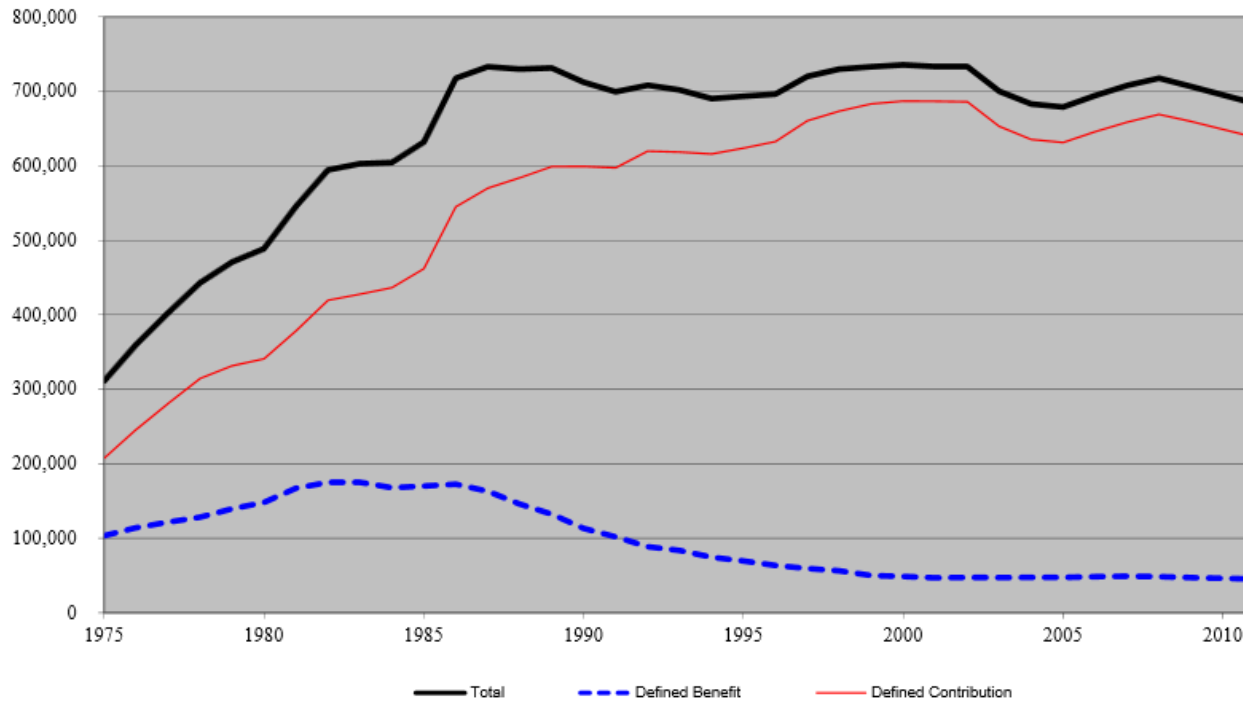
Making Retirement Plans Work

Part of the American Retirement Association

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DOL's Annuity Disclosure Proposal

Graph E1g. Number of Pension Plans
by type of plan, 1975-2011

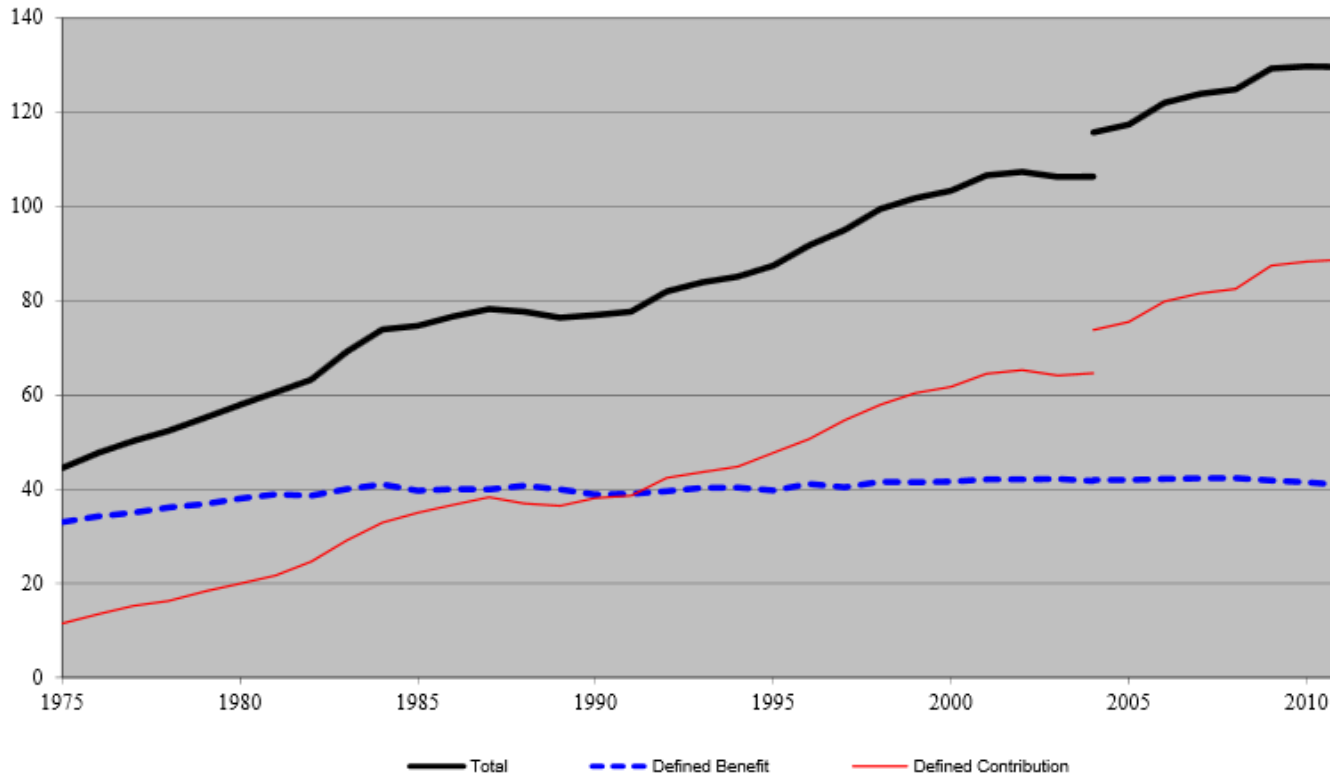


NOTE: Excludes plans covering only one participant.

SOURCE: Form 5500 filings with the U.S. Department of Labor.

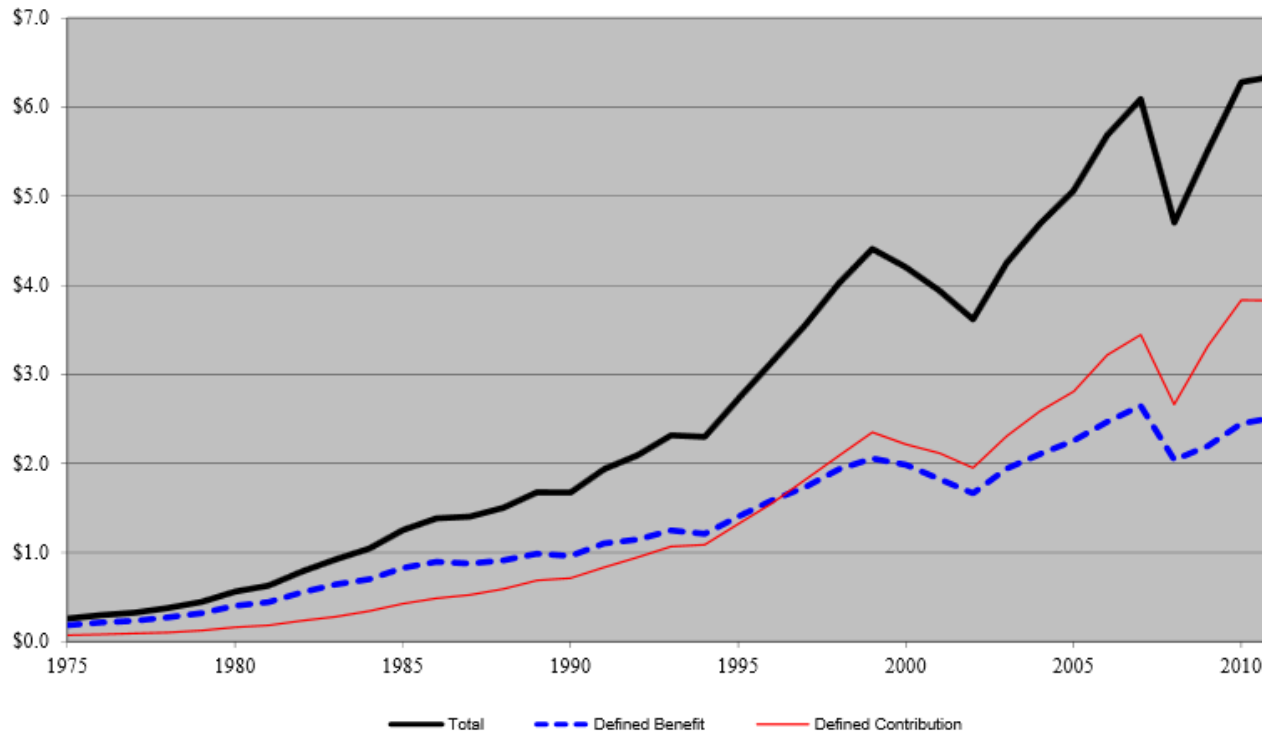
DOL's Annuity Disclosure Proposal

Graph E5g. Number of Participants in Pension Plans
by type of plan, 1975-2011
(numbers in millions)



DOL's Annuity Disclosure Proposal

**Graph E11g. Pension Plan Assets
by type of plan, 1975-2011**
(amounts in trillions)

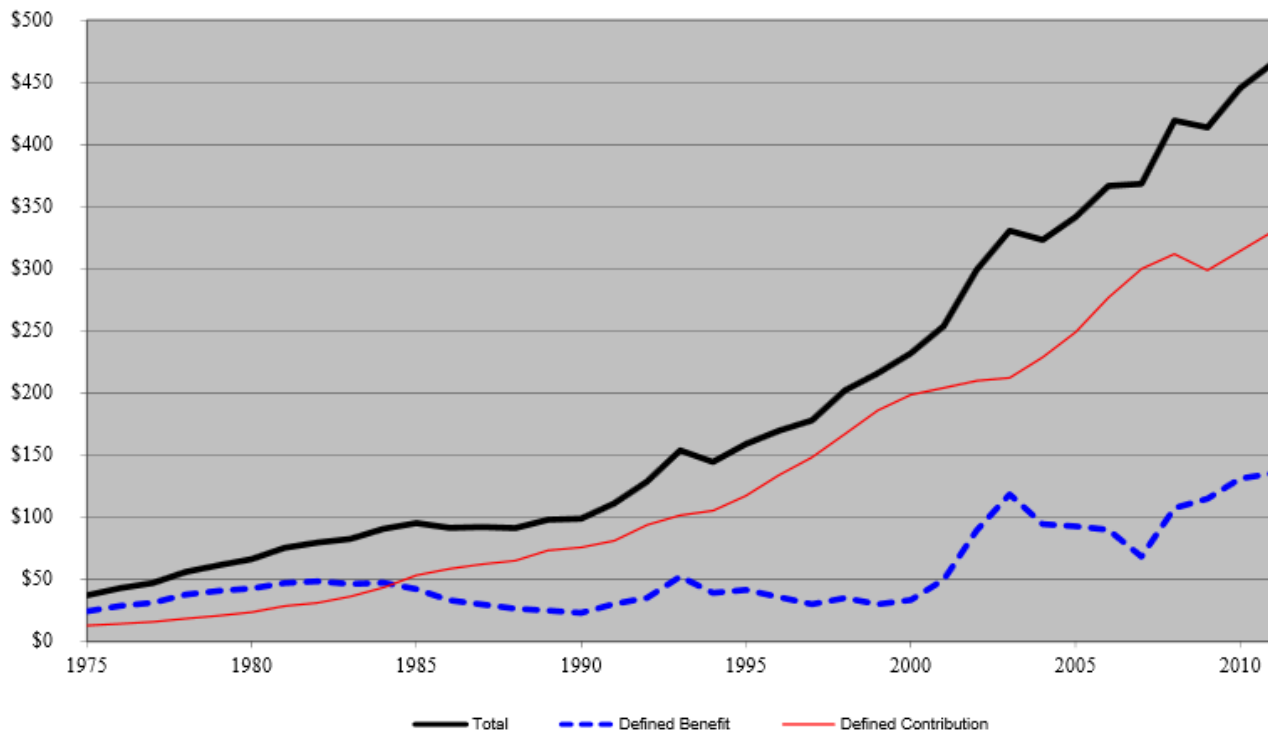


NOTE: Excludes plans covering only one participant.

SOURCE: Form 5500 filings with the U.S. Department of Labor.

DOL's Annuity Disclosure Proposal

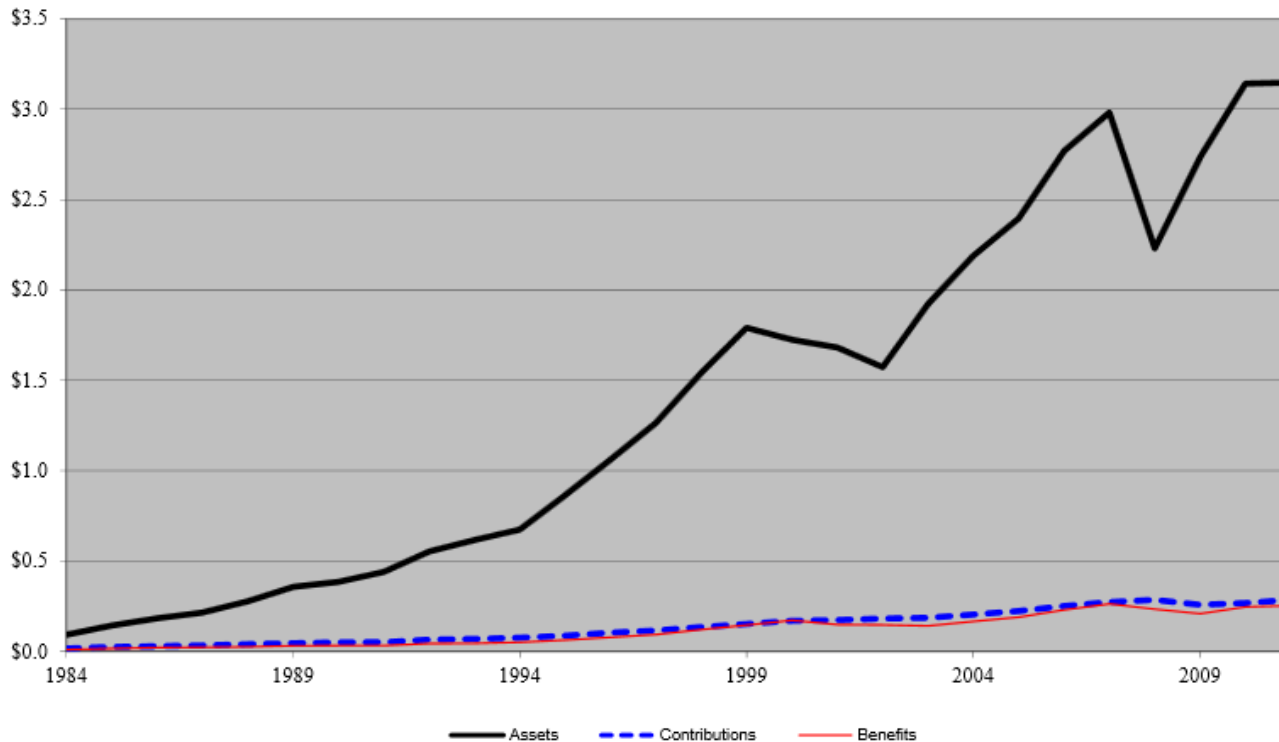
**Graph E14g. Pension Plan Contributions
by type of plan, 1975-2011**
(amounts in billions)



NOTE: Excludes plans covering only one participant.
SOURCE: Form 5500 filings with the U.S. Department of Labor.

DOL's Annuity Disclosure Proposal

**Graph E20g2. Assets, Contributions, and Benefit Payments of 401(k) Type Plans
1984-2011**
(amounts in trillions)



VOTE: Excludes plans covering only one participant.

SOURCE: Form 5500 filings with the U.S. Department of Labor.

DOL's Annuity Disclosure Proposal

- DOL - Advance Notice of Proposed Rulemaking – ANPRM
- Issued: May 8, 2013
- Comments through August 8, 2013 (extended)
- Proposed Guidance under Reg. §2520.105-1 adding new subsections (c), (d) and (e)

DOL's Annuity Disclosure Proposal

- Summary of ANPRM
 - (c) Benefit statement must include following info describing:
 - (2) “Total benefits accrued”
 - (v) Fair market value of account balance as of end of statement period
 - (vi) If participant not at NRA, current dollar value of projected account balance at NRA, using assumptions from (d)
 - (vii) FMV from (v) expressed as a lifetime income stream, using assumptions from (e)
 - (viii) Amount in (vi) expressed as a lifetime income stream, using assumptions from (e)

DOL's Annuity Disclosure Proposal

- Summary of ANPRM (continued)
 - (6) Assumptions for illustrations above must be explained
 - (i) Disclose assumptions from (d)
 - (ii) Disclose assumptions from (e)
 - (iii) Provide a statement that says: “illustrations only and that actual monthly payments that may be received at normal retirement age will depend on numerous factors and may vary from the illustrations in the benefit statement.”

DOL's Annuity Disclosure Proposal

- Summary of ANPRM (continued)
 - (D) Assumptions for projecting account balance to NRA
 - (1) Projections must be reasonable. Not reasonable unless
 - Expressed in current dollars
 - Take into account future contributions and investment returns

DOL's Annuity Disclosure Proposal

- Summary of ANPRM (continued)
 - (2) Following assumptions, if used together, deemed safe harbor reasonable
 - (i) Contributions continue to NRA and increase by three percent each year
 - (ii) Investment returns are seven percent per year
 - (iii) Discount rate of three percent is used to determine current dollars

DOL's Annuity Disclosure Proposal

- Summary of ANPRM (continued)
 - (E) Assumptions for converting account balance to lifetime income stream
 - (1) Lifetime income stream must be
 - (i) Level monthly payment for life of participant, assuming participant has attained NRA and immediate commencement
 - (ii) If participant is married, 50 percent J&S calculation, assuming participant has attained NRA, immediate commencement and spouse same age
 - (iii) Based on assumptions in (2) or (3) as applicable

DOL's Annuity Disclosure Proposal

- Summary of ANPRM (continued)
 - (2) Assumptions
 - (i) Interest and mortality must be reasonable under “generally accepted actuarial principles”
 - (ii) Following assumptions deemed safe harbor reasonable:
 - (A) Interest equal to ten-year constant maturity Treasury securities rate, as of first business day of the last month of statement period
 - (B) Mortality per IRS table under Code §417(e)(3)(B) as in effect for month that includes last day of statement period

DOL's Annuity Disclosure Proposal

- Summary of ANPRM (continued)
 - (3) If plan offers annuity form of distribution under a contract with a state-licensed insurer, plan shall substitute “actual plan terms” for the above assumptions
 - (4) Assumed annuity commencement date is first day following statement period and participant is assumed to have attained NRA (or actual age if older)

DOL's Annuity Disclosure Proposal

- Summary of ANPRM (continued)
- Appendix A shows tables to explain how proposed rules work
- **WARNING: TABLES MAY NOT BE USED AS ILLUSTRATIONS FOR PARTICIPANTS OR TO SATISFY DISCLOSURE REQUIREMENTS!**

DOL's Annuity Disclosure Proposal

Table 1

Normal Retirement Date.....	June 30, 2032.
Number of years in projection.....	19.5 (January 1, 2013 through June 30, 2032)
Number of contributions.....	19 (\$10,000 per year adjusted by contribution increase rate) + 1 (final contribution of \$5,000 in 2032, adjusted by contribution increase rate).
Paragraph (d)(2)(i) safe harbor – contribution increase rate.	3% compounded annually.
Paragraph (d)(2)(ii) safe harbor – rate of return applied to current account balance of \$125,000 and post 2012 projected contributions.	7% compounded annually.
Paragraph (d)(2)(iii) safe harbor – discount rate used to determine present value of the projected account balance.	3% compounded annually

DOL's Annuity Disclosure Proposal

Table 2

Paragraph (e)(2)(ii)(A) safe harbor – 10 year constant maturity Treasury rate on December 3, 2012:	1.63%, compounded annually.
Paragraph (e)(2)(ii)(B) safe harbor – Code section 417(e)(3)(B) applicable mortality table:	Unisex mortality table published in IRS Notice 2008-85
Assumed commencement date.....	January 1, 2013.
Assumed Age of P on the assumed commencement date.	65.
Assumed Age of P's spouse on the assumed commencement date.	65 (i.e., same as P).

DOL's Annuity Disclosure Proposal

The pension benefit statement would show the following lifetime income streams:

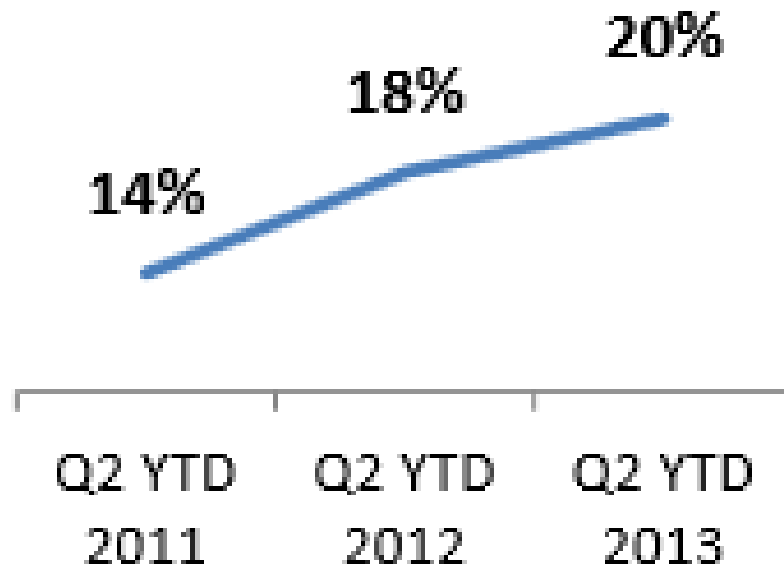
Account Balance on Last Day of Statement Period (12/31/2012)	Single Life Form (monthly payment for P's life with no survivor benefit)	Joint and 50% survivor form	
		Monthly payment during P's life	Monthly payment after P's death to surviving spouse
Current – \$125,000	\$625	\$564	\$282
Projected – \$557,534	\$2,788	\$2,514	\$1,257

DOL's Annuity Disclosure Proposal

- ANPRM - issues for consideration
 - Are these disclosures really necessary?
 - What evidence exists that they will be beneficial?

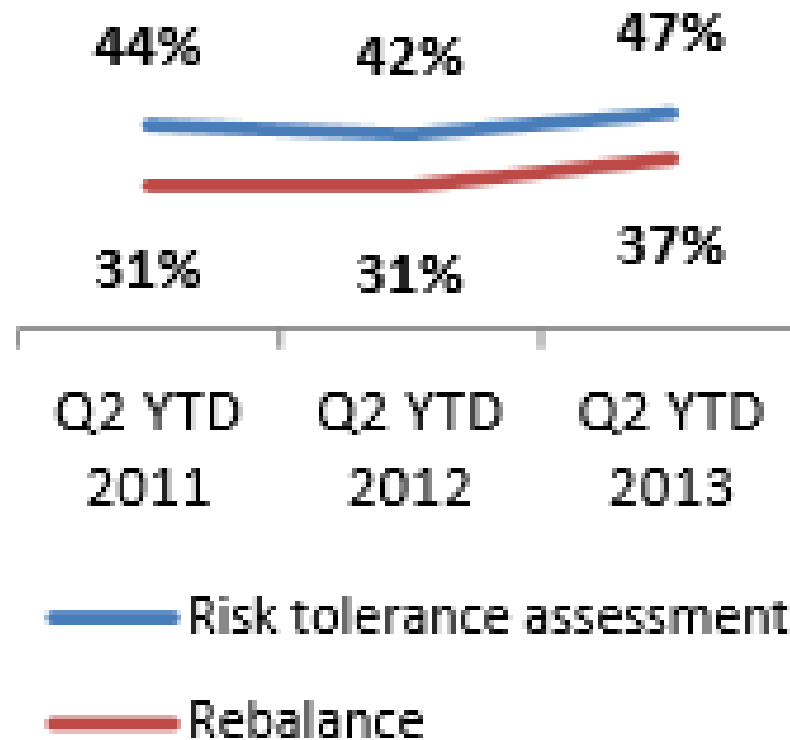
DOL's Annuity Disclosure Proposal

**% on track to reach
income goal**

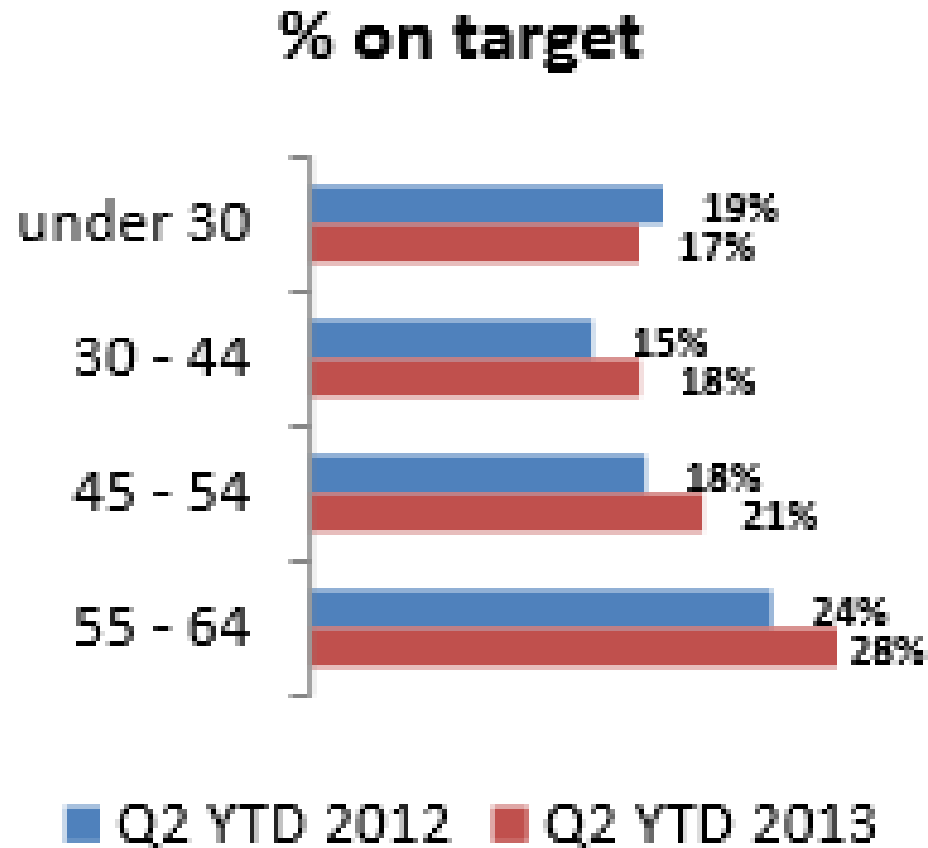


DOL's Annuity Disclosure Proposal

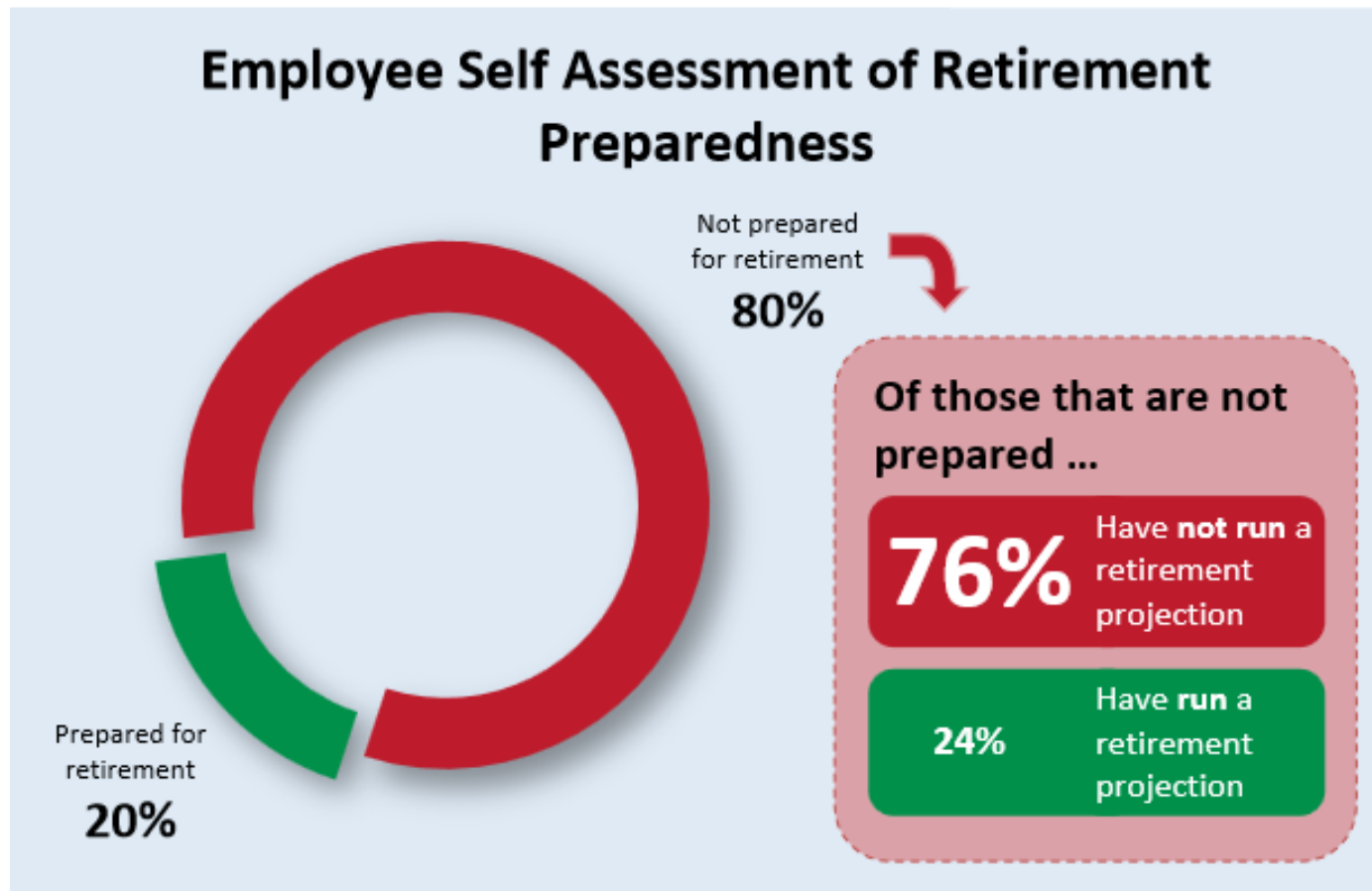
Investing Behavior



DOL's Annuity Disclosure Proposal



DOL's Annuity Disclosure Proposal



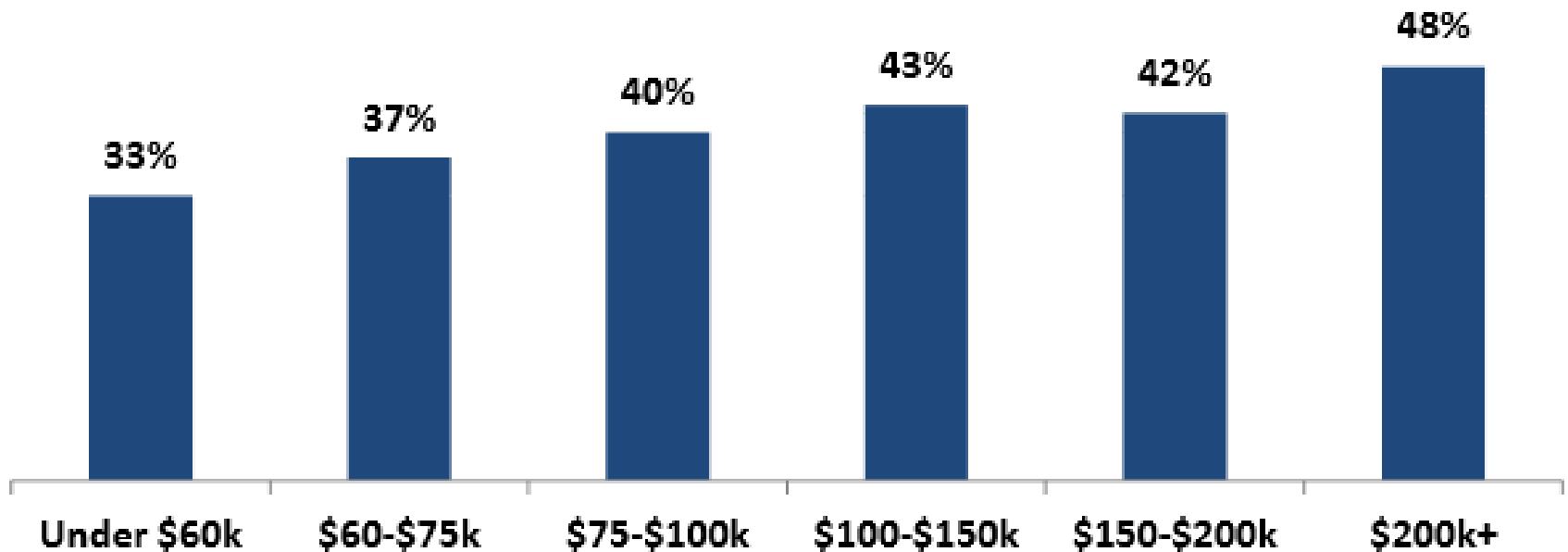
DOL's Annuity Disclosure Proposal

The percentage of respondents that are on track to reach their income-replacement goal in retirement

	2012	2013
Early Boomers (55 – 64)	24%	28%
Late Boomers (45 – 54)	18%	21%
Generation X (30 – 44)	15%	18%
Millennial (Under 30)	19%	17%

DOL's Annuity Disclosure Proposal

Percentage that have run a retirement projection



DOL's Annuity Disclosure Proposal

- ANPRM - issues for consideration

Does DOL have authority to mandate these kinds of disclosures?

- Section 105(a)(2)(A)(i)(I) requires a benefit statement to indicate the participant's or beneficiary's “total benefits accrued.”
- Section 505, in relevant part, provides that the Secretary may prescribe such regulations as the Secretary finds necessary or appropriate to carry out the provisions of Title I of ERISA

DOL's Annuity Disclosure Proposal

- ANPRM - issues for consideration (continued)
Does DOL have authority to mandate these kinds of disclosures?

Section 109(c) - The Secretary may prescribe the format and content of the summary plan description, the summary of the annual report described in section 104(b)(3) and any other report, statements or documents (other than the bargaining agreement, trust agreement, contract, or other instrument under which the plan is established or operated), which are required to be furnished or made available to plan participants and beneficiaries receiving benefits under the plan.

DOL's Annuity Disclosure Proposal

- ANPRM - issues for consideration (continued)
 - Does DOL have authority to mandate these kinds of disclosures?
 - But see: Section 3(23) - The term “accrued benefit” means
 - (B) In the case of a plan that is an individual account plan, the balance of the individual's account . . .

DOL's Annuity Disclosure Proposal

- ANPRM - issues for consideration (continued)
 - If DOL has authority, is this the best approach?
 - What about Interpretive Bulletin 96-1 approach?
 - How should disclosure occur? How often?

DOL's Annuity Disclosure Proposal

- ANPRM - issues for consideration (continued)
 - Are the mandated disclosures the right ones?
 - Are the assumptions the right ones? If not, why not?

DOL's Annuity Disclosure Proposal

- ANPRM - issues for consideration (continued)
 - Is a safe harbor a good idea?
 - Fiduciary liability?
 - Other issues to consider?
 - Guaranteed lifetime withdrawal benefits
 - How to explain QLACs
 - Multiple annuity plans – 403(b)s
 - FINRA/SEC coordination
 - State insurance laws

DOL's Annuity Disclosure Proposal

Alternative proposal

- Show basic amounts only:
 - “An account balance of \$100,000 will buy \$X per month if 65 or \$Y per month if 67”*
 - Can substitute other amounts: \$250,000, \$500,000, \$750,000, etc.
 - * Based on current annuity rate assumptions

DOL's Annuity Disclosure Proposal

Alternative proposal (continued)

- DOL online calculator structured as follows:
“If your account balance today is [\$10,000] and you are age [30], [40], [50], [60] –
Then your account must earn an average of [3%], [5%], [7%] and receive combined (employee/employer) annual contributions of \$_____ to reach [\$100,000], [\$250,000], [\$500,000] at age [65], [67]”

Longevity Insurance in Qualified Plans

- The problem:
 - Americans are living longer
 - Code §401(a)(9) forces distributions
 - Lump-sum payments are the norm
 - Retirees risk running out of pension funds

Longevity Insurance in Qualified Plans

- Treasury's solution
 - Allow partial lump sums and annuities from DB Plans
 - Allow “annuitization” of DC Plan accounts through rollover to DB Plans (Notice 2012-4)
 - Provide 401(a)(9) relief through QLACs
 - Clarify the operation of J&S rules for DC Plans (Notice 2012-3)

Longevity Insurance in Qualified Plans

- The private sector solution?
 - New “quasi-annuity” annuity products
 - “Flexible income” contracts as investments in DC plans – i.e., annuity-type contracts with a guaranteed lifetime withdrawal benefit (GLWB) or a guaranteed minimum withdrawal benefit (GMWB) feature

Longevity Insurance in Qualified Plans

- DOL Response?
 - Fiduciary issues – responsibility for selection of annuity or investment products
 - Participant education and disclosure – what to disclose and how to do it
 - Reporting – who is responsible and what needs to be said
 - Status? Some “safe harbor” guidance issued for annuity selection – DOL Reg §2550.404a-4

Longevity Insurance in Qualified Plans

– Focus of this outline

- Rev. Rul. 2012-4 - rollovers from DC to DB Plans
- Treas. Reg. §1.401(a)(9)-6 Q&A-17 – Qualified Longevity Annuity Contracts
- Private sector products offering “flexible income” or “guaranteed minimum withdrawal” rights - GLWB and GLMB contracts

Longevity Insurance in Qualified Plans

- Revenue Ruling 2012-4 (Effective January 1, 2013)
 - Main facts
 - Profit sharing plan account balance
 - No after-tax employee money in the account
 - Plan is exempt from J&S rules
 - DB Plan sponsored by the same employer
 - DB Plan will accept and annuitize a direct rollover from DC Plan

Longevity Insurance in Qualified Plans

- Revenue Ruling 2012-4 (Effective January 1, 2013)
 - Additional details
 - Participant at least age 55 with ten years of service
 - DB Plan does not disregard rollovers for distributions of small amounts

Longevity Insurance in Qualified Plans

- Revenue Ruling 2012-4
- Holdings
 - DB Plan does not violate 411 or 415 by providing an annuity from the rollover funds
 - DB Plan cannot use “less favorable” actuarial assumptions (411(a)(1) violation)
 - Plan can use more favorable assumptions, but that raises 415 and 401(a)(4) issues

Longevity Insurance in Qualified Plans

- Revenue Ruling 2012-4
- Additional comments in the ruling
 - If the DB Plan's AFTAP is below 60 percent, plan cannot accept rollover
 - Starting date for rollover annuity need not be the same as that payable under DB Plan

Longevity Insurance in Qualified Plans

- Revenue Ruling 2012-4
- Observations
 - Ruling holds that a former employee can roll over to a former employer's plan without plan disqualification
 - Compare PLR 2009-25049 (DB Plan to DC Plan)

Longevity Insurance in Qualified Plans

- Revenue Ruling 2012-4
- Observations (continued)
 - What about surviving spouse and alternate payee rollover rights? See 402(c)(9) and 402(e)(1)(B)
 - How far do rollover rights extend?
 - Conduit IRA
 - Former employee not a DB Plan participant
 - Former employee in DB but rollover from another plan or IRA

Longevity Insurance in Qualified Plans

- Revenue Ruling 2012-4
- Observations (continued)
 - What if rollover includes after-tax funds
 - Is the rollover a separate “right or feature?”
 - How does the “high 25” rule apply here?

Longevity Insurance in Qualified Plans

- Creation of the “QLAC” - Treas. Reg. §1.401(a)(9)-6 Q&A-17 (effective for contracts purchased after July 2, 2014)
- The problem to be addressed:
 - Under Reg. §1.401(a)(9)-6 Q&A-12, the value of a deferred annuity contract in a DC Plan must be included in the account balance to determine the MRD
 - This requirement applies to plans under 401(a), 403(b), IRAs and 457(b) (government).

Longevity Insurance in Qualified Plans

- The solution
- Create a new rule for a deferred annuity contract that can be excluded from the MRD calculation – a Qualified Longevity Annuity Contract – “QLAC”

Longevity Insurance in Qualified Plans

- Treas. Reg. §1.401(a)(9)-6 Q&A-17 (continued)
- QLAC rules
 - Cannot be a variable annuity or equity-indexed
 - Total premiums cannot exceed lesser of 25 percent of account balance or \$125,000
 - Payments must start no later than age 85
 - No commutation or cash surrender value

Longevity Insurance in Qualified Plans

- Treas. Reg. §1.401(a)(9)-6 Q&A-17 (continued)
- QLAC rules (continued)
 - No death benefit except:
 - Straight life annuity to the surviving spouse or designated beneficiary OR
 - Return of premium feature – with restrictions
 - Annuity must state it is a QLAC
 - COLAs and participation dividends are permitted

Longevity Insurance in Qualified Plans

- Treas. Reg. §1.6047-2
- QLAC Reporting
 - Initial – at time of purchase (not filed with IRS)
 - Description of dollar and percentage limits
 - Annuity start date and early start right if any
 - Estimated payment amount – and notice of no cash out right
 - Calculation of any death benefit
 - Administrative procedures – forms, elections, etc.

Longevity Insurance in Qualified Plans

- Treas. Reg. §1.6047-2 (continued)
- Reporting
 - Annual reporting (filed with IRS)
 - Filing to be made by contract issuer – not plan
 - Issuer ID information
 - Purchaser ID information
 - Plan ID information
 - Annuity start date
 - Amount paid for annuity
 - Must file until age 85 or death – even if annuity starts sooner

Longevity Insurance in Qualified Plans

- Treasury's QDIA Proposal – Notice 2014-46 (October 24, 2014)
 - Plan may create target date funds (TDFs) with embedded deferred annuities – QLACs
 - TDFs must be a series of integrated funds with the same investment manager
 - TDFs cannot include GLWBs or GMWBs

Longevity Insurance in Qualified Plans

- Treasury's QDIA Proposal – Notice 2014-46 (October 24, 2014) (continued)
 - No employer securities in the TDF unless publicly traded
 - Age banding for TDFs limited to three years? See Part IV example.
 - Each TDF must have similar fees and expenses

Longevity Insurance in Qualified Plans

- Treasury's QDIA Proposal – DOL response
 - Advisory Letter from DOL to Mark Iwry at Treasury (October 23, 2014)
 - TDFs that hold unallocated QLACs and meet Notice 2014-46 requirements “will not fail” to satisfy QDIA rules
 - Response limited to facts in letter

Longevity Insurance in Qualified Plans

- Treasury's QDIA proposal – DOL response (continued)
 - Fiduciary issues – both for TDF and embedded annuities
 - TDFs must be managed by ERISA §3(38) manager and QLACs must be issued by an insurance company “independent” from the investment manager

Longevity Insurance in Qualified Plans

- Questions and issues
 - Is the QLAC dollar/percentage limitation reasonable?
 - What if after-tax money is involved?
 - Is the “safe harbor” fiduciary standard for selecting an issuer workable? How does that apply to a TDF?
 - Annual reporting must be done by issuer – what is his/her fiduciary status?

Longevity Insurance in Qualified Plans

- Questions and issues (continued)
 - M&A issues – maintaining issuer contracts
 - The QLAC return of premium feature – trap for the unwary? Disclosure liability?
 - The MRD alternative – the statutory annuity

Guaranteed Lifetime Withdrawal Benefits

- What is a GLWB?
 - Annuity type contract
 - Allows flexible withdrawal/payment rates
 - Guarantees a lifetime minimum benefit, IF withdrawal rates not exceeded
 - Offers upside potential

Guaranteed Lifetime Withdrawal Benefits

- GLWB mechanics
 - Minimum income stream assured if set withdrawal rate not exceeded
 - “One-way ratchet” – revised “benefit base” can increase income stream
 - Unlimited access to contract funds – but over withdraw and GLWB value goes to zero
 - Death benefit available for unused funds

Guaranteed Lifetime Withdrawal Benefits

- GLWB fiduciary issues
 - Offering a GLWB – a settlor function
 - Selecting a GLWB provider – a fiduciary function
 - GLWB fees usually higher than standard annuity products
 - Portability

Guaranteed Lifetime Withdrawal Benefits

- GLWB fiduciary issues (continued)
 - Evaluating fees - cost only one factor
 - Volatility of GLWB investments
 - Available withdrawal rates
 - Benefit base step up frequency
 - How are fees assessed? Comparisons?
 - Fee increases permitted?

Guaranteed Lifetime Withdrawal Benefits

- GLWB fiduciary issues (continued)
- DOL annuity selection safe harbor
 - Objective, analytical search
 - Sufficient information to assess financial status of issuer
 - Cost of contract versus benefits offered
 - Issuer able to meet contractual obligations
 - Expert advice, as necessary

Questions?