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August 8, 2013

Office of Regulations and Interpretations
Employee Benefits Security Administration
Room N-5655
U.S. Department of Labor
200 Constitution Avenue, NW
Washington, DC 20210

Submitted by e-mail to e-ORI@dol.gov

Attention: Pension Benefit Statements Project

Re: Advanced Notice of Proposed Rulemaking on Pension Benefit Statements
Docket ID: EBSA-2013-0007
RIN 1210-AB20

Dear Ladies and Gentlemen:

First, AFSCME would like to express our firm support for providing more complete information to workers who will rely upon defined contribution programs to provide for their retirement security. As we are now decades into defined contribution arrangements, it is long overdue that workers receive the vital information needed to plan their own retirement security in these self-managed plans.

We believe it is essential for plan participants to understand the approximate level of lifetime income that would be provided in retirement based on their current account balance. It is also important that this information be disclosed on a mandatory basis.

Projecting Future Contributions

AFSCME does not believe it is appropriate for benefit statements to anticipate future contributions to one's plan. Future earnings, employment, raises and contributions are not guaranteed. In fact, a 2009 GAO study showed that 3% of account balances were withdrawn from these accounts during working years (which is often referred to as leakage). Meanwhile, Vanguard has noted that leakage has increased in recent years. Thus, if we are to anticipate future contributions, should we not also

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anticipate future leakage? Otherwise, we risk painting an overly-optimistic view of the effectiveness of these plans in the real world, where these accounts are commonly seen as more than just retirement accounts (but a source of emergency cash and/or a source for loans).

http://www.pionline.com/article/20110307/PRINTSUB/303079974

Future Investment Returns

The ANPRM proposes to use a 7 percent investment return to project retirement accounts to a given retirement age. AFSCME believes this is too high, for a number of reasons. In addition, we will present alternative ideas below to address the issues presented by this assumption.

First, defined contribution plans have not historically generated strong returns for workers. As the notice indicated, defined contribution plans under-performed the market by 1.3 percent annually during 1990-2009. We also know that defined contribution plans underperformed defined benefit plans. As noted in *INVESTMENT RETURNS: DEFINED BENEFIT VS. 401(k) PLANS*:

> *"The bottom line is that over the period 1988-2004 defined benefit plans outperformed 401(k) plans by one percentage point. This outcome occurred despite the fact that 401(k) plans held a higher portion of their assets in equities during the bull market of the 1990s.*

http://crr.bc.edu/wp-content/uploads/2006/09/ib_52.pdf

What is often overlooked is the fact that defined contribution plans had much more favorable demographics than defined benefit plans during the time that this comparison was made (1998-2004). If the demographics were reversed (with relatively older participants in 401(k) plans), the spread would have been much wider. This is because defined contribution participants should adopt asset-preservation strategies near and during retirement. Thus, we should expect the investment return advantage in defined benefit (DB) plans to grow in the future as defined contribution (DC) plan participants mature.

Because 8 percent returns are reasonable for defined benefit plans, it is possible that 7 percent returns are feasible for defined contribution plans during one's younger years. However, it is certainly not appropriate to expect a DC plan participant to invest aggressively as one approaches retirement. This is particularly important because the time when one cannot afford an aggressive investment posture coincides with the time that account balances should be largest. Thus, the dollar-weighted impact of a capital preservation strategy of investing is great.

There are a number of potential means to address this issue. First, the investment return assumption could be based upon one's age. For instance, DC returns of 7 percent should be assumed up to age 55; 6 percent between ages 55-60; and 5 percent thereafter. (Attached is a worksheet highlighting the difference in value presented in traditional defined benefit plans versus defined contribution plans, with an illustration of how the investment timeframe affects the value received from the plan.)

If using select and ultimate return assumptions is deemed too burdensome, lowering the assumed return on investment 1 percent (to a return assumption of 6 percent) would roughly approximate the inefficiency presented by the shortened investment time horizon under DC plans (during working years).

Finally, it is also possible to show more than one scenario. For instance, projections based on both 5 percent and 7 percent returns could be required.

We also note that the large spread between wage growth and investment returns will distort the wage replacement projections that DC participants may make. A 4 percent spread is inappropriately large and will likely mislead participants into thinking they may replace far more of their income than may actually be the case. Most DB plans do not assume such a wide spread between investment returns and assumed wage growth. We welcome and expect a thorough discussion of this spread as the process moves forward.

Converting Account Balances into Lifetime Income Streams

AFSCME supports the use of the 10-year treasury security as the baseline discount rate to convert account balances at retirement into lifetime annuities. The use of a lower post-retirement discount rate appropriately recognizes the prudent choices available to retirees (either invest in safer, low-yield, investments or purchase an annuity based upon market prices.) Further, the issue of whether or not to include an insurance load should be studied further, by doing a careful comparison between market prices of annuities and the 10-year treasury yield. If the insurance load is inherently accounted for by utilizing a lower yield discount rate, it is appropriate to exclude the load. If this is not inherently accounted for, then it is appropriate to include an insurance load.

Another key aspect to consider, with regard to converting an account balance into a lifetime income stream, is whether or not to take inflation into account. AFSCME believes it is appropriate to do so, for two key reasons. First, we should recognize that inflation has been persistent over time and will likely continue to be a reality. Thus, for an income stream to maintain a certain standard of living, withdrawals would have to increase during one's retirement (which could be decades). Second, workers approaching retirement may use this information from their benefit statement as a guidepost to determine the level of withdrawals that are appropriate to ensure their account balances endure for their projected lifetime.

We appreciate your consideration of the foregoing and we look forward to reviewing the proposed regulations.

Sincerely,

Steven Kreisberg
Director of Collective Bargaining and
Health Care Policy

SK/dd

Effect of Returns on Value Provided in DB and DC Plans

Basic Information				#1 - DB plan value		#2 - The DC Promise		#3 - The DC Reality	
age	pay (incr 5%)	Contrib's %	Contrib's $'s	Inv. Return	Balance	Inv. Return	Balance	Inv. Return	Balance
25	25,000	10%	2,500	8.0%	2,598	7.0%	2,586	7.0%	2,586
26	26,000	10%	2,600	8.0%	5,508	7.0%	5,457	7.0%	5,457
27	27,040	10%	2,704	8.0%	8,759	7.0%	8,635	7.0%	8,635
28	28,122	10%	2,812	8.0%	12,382	7.0%	12,149	7.0%	12,149
29	29,246	10%	2,925	8.0%	16,412	7.0%	16,025	7.0%	16,025
30	30,416	10%	3,042	8.0%	20,886	7.0%	20,293	7.0%	20,293
31	31,633	10%	3,163	8.0%	25,844	7.0%	24,985	7.0%	24,985
32	32,898	10%	3,290	8.0%	31,330	7.0%	30,137	7.0%	30,137
33	34,214	10%	3,421	8.0%	37,392	7.0%	35,786	7.0%	35,786
34	35,583	10%	3,558	8.0%	44,082	7.0%	41,972	7.0%	41,972
35	37,006	10%	3,701	8.0%	51,454	7.0%	48,738	7.0%	48,738
36	38,486	10%	3,849	8.0%	59,570	7.0%	56,130	7.0%	56,130
37	40,026	10%	4,003	8.0%	68,495	7.0%	64,200	7.0%	64,200
38	41,627	10%	4,163	8.0%	78,301	7.0%	73,000	7.0%	73,000
39	43,292	10%	4,329	8.0%	89,064	7.0%	82,588	7.0%	82,588
40	45,024	10%	4,502	8.0%	100,868	7.0%	93,026	7.0%	93,026
41	46,825	10%	4,682	8.0%	113,803	7.0%	104,382	7.0%	104,382
42	48,698	10%	4,870	8.0%	127,968	7.0%	116,726	7.0%	116,726
43	50,645	10%	5,065	8.0%	143,469	7.0%	130,135	7.0%	130,135
44	52,671	10%	5,267	8.0%	160,420	7.0%	144,693	7.0%	144,693
45	54,778	10%	5,478	8.0%	178,947	7.0%	160,488	7.0%	160,488
46	56,969	10%	5,697	8.0%	199,183	7.0%	177,615	7.0%	177,615
47	59,248	10%	5,925	8.0%	221,275	7.0%	196,177	**6.0%**	194,372
48	61,618	10%	6,162	8.0%	245,380	7.0%	216,283	6.0%	212,378
49	64,083	10%	6,408	8.0%	271,670	7.0%	238,051	6.0%	231,719
50	66,646	10%	6,665	8.0%	300,330	7.0%	261,609	6.0%	252,483
51	69,312	10%	6,931	8.0%	331,560	7.0%	287,091	6.0%	274,768
52	72,084	10%	7,208	8.0%	365,576	7.0%	314,644	6.0%	298,676
53	74,968	10%	7,497	8.0%	402,612	7.0%	344,424	6.0%	324,315
54	77,966	10%	7,797	8.0%	442,924	7.0%	376,598	6.0%	351,801
55	81,085	10%	8,108	8.0%	486,784	7.0%	411,348	**5.0%**	377,700
56	84,328	10%	8,433	8.0%	534,491	7.0%	448,865	5.0%	405,226
57	87,701	10%	8,770	8.0%	586,364	7.0%	489,358	5.0%	434,474
58	91,210	10%	9,121	8.0%	642,752	7.0%	533,047	5.0%	465,544
59	94,858	10%	9,486	8.0%	704,030	7.0%	580,173	5.0%	498,541
60	98,652	10%	9,865	8.0%	**760,353**	7.0%	**620,785**	5.0%	**523,468**
Age 65 balance as multiple of pay					**771%**		**629%**		**531%**
Loss Due to *Return Inefficiencies* while working					**N/A**		**-18.4%**		**-31.2%**
Annual amount available for retirement					57,515		42,695		29,146
Annual amount as % of final pay					58.3%		43.3%		29.5%
Loss Due to Return Inefficiencies Overall					**N/A**		**-25.8%**		**-49.3%**

Conclusions:

- Achieving higher investment returns is the key to efficient retirement system
- Getting lower investment returns is very costly (while working and after retirement), but a 401k participant also needs to get conservative at all times when account balance is large, creating a lost opportunity cost and loss of efficiency.
- A participant has to be conservative during all the years where his balance is substantial -- driving down dollar weighted investment returns greatly.