U.S. Department of Labor **Employee Benefits Security Administration**
Washington, D.C. 20210

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2010-01A

Steven R. Kronheim
Vice President and Associate General Counsel
TIAA-CREF
730 Third Avenue
New York, New York 10017-3206

29 CFR § 2520.104-44

Dear Mr. Kronheim:

This is in response to your request on behalf of the Teachers Insurance and Annuity Association of America (TIAA) and College Retirement Equities Fund (CREF) (together "TIAA-CREF") for an advisory opinion concerning the reporting of the TIAA "Traditional Annuity" on the Form 5500 Annual Return/Report of Employee Benefit Plan. You ask whether the TIAA "Traditional Annuity" is a fully allocated contract for annual reporting purposes within the meaning of 29 C.F.R. § 2520.104-44(b)(2) and the Form 5500 Instructions. The answer determines whether the Traditional Annuity accumulations must be reported as plan assets on the Form 5500 and applicable schedules and attachments.

You represent that TIAA issues individual and group contracts as funding vehicles for retirement plans maintained by colleges, universities, independent schools, and other non-profit research and educational organizations.[1] The majority of these plans are tax-sheltered annuity programs under section 403(b) of the Internal Revenue Code (403(b) plans). TIAA also provides its contracts as funding vehicles for other defined contribution plans (including 401(k) plans). TIAA-CREF contracts generally provide three investment options for contributions: the Traditional Annuity, a CREF mutual fund account, or the TIAA real estate account. Participants receive quarterly statements detailing their account balances invested in the various TIAA-CREF options, including the Traditional Annuity accumulations.

You represent that during the accumulation phase, for each contribution or "premium," the Traditional Annuity provides a guarantee of principal, a guaranteed minimum interest rate (generally 3 percent but in some recent contracts between 1 percent and 3 percent), and the potential for additional interest when declared by TIAA. The additional interest, when declared, remains in effect for the "declaration year" which begins March 1 of each year, but additional interest is not guaranteed for future years. Although you describe the additional interest as a new contribution, you have

[1] TIAA contracts are also funding vehicles for state and local governmental employers throughout the United States. This letter addresses only those employee benefit plans that are covered under Title I of ERISA.

represented that the additional amounts are, in effect, a change in the interest rate on accumulations for the year.

The additional interest on the Traditional Annuity is added to the participant's current interest rate in "vintages." Vintages are periods typically composed of one or two contiguous months. A vintage identifies a portion of the participant's accumulation attributable to the contributions into the participant's Traditional Annuity account during that period. The amount of additional interest for each vintage is declared each year based on projections of a number of factors including the net investment earnings rate of TIAA's general assets supporting that vintage, minus a charge for administrative expenses and an amount set aside for contingency reserves. You have explained that TIAA uses the vintage system because the yields available on bonds, wholly owned real estate and other fixed income investments in the TIAA general account tend to change over time. You represent that the vintage system enables TIAA to declare and distribute excess earnings to participants on an equitable basis.

The TIAA contracts describe the Traditional Annuity as providing "guaranteed" benefits. Specifically, the TIAA Retirement Annuity contract provides that "[e]ach premium allocated to the Traditional Annuity buys a definite amount of lifetime income for you, based on the rate schedule in effect for your contract at the time the premium is paid." The TIAA Group Retirement Annuity contract provides that "[e]ach premium allocated to the TIAA Traditional under the contract buys a guaranteed minimum amount of benefit payments, based on the rate schedule in effect at the time the premium is credited." You have explained that the descriptions in both the Retirement Annuity and the Group Retirement Annuity refer to the guaranteed portions of each return, *i.e.*, the return of contributions and minimum interest rate.

Under most TIAA contracts, a participant may transfer his or her funds between the Traditional Annuity, the CREF mutual fund account and the TIAA real estate account. Transfers from the Traditional Annuity are done with a TIAA "Transfer Payout Annuity," ten equal annual payments, after which the amounts transferred are reported as plan assets on the Form 5500. The 10-year payout schedule is designed so as not to deplete the liquid assets in TIAA's general account. The Transfer Payout Annuity is also used as a withdrawal method in the participant's "post-accumulation" phase, where the accumulation earns, in addition to the guaranteed minimum rate of between 1 percent and 3 percent, the same additional interest rate amounts declared by TIAA for the accumulation phase.

In addition to the Transfer Payout Annuity, there are other ways for the Traditional Annuity accumulations to be paid out to the participant. Several methods of withdrawal involve no lifetime guarantees. For example, if a participant dies while still in service, his or her Traditional Annuity accumulations are paid to the participant's spouse or other beneficiary. TIAA contracts under some plans also offer a lump sum option for distribution of the Traditional Annuity accumulations which carries a surrender charge of approximately 2.5 percent. Some contracts also offer an "interest only" option which leaves the participant's principal intact, but pays the participant a monthly payment equal to the guaranteed minimum interest and supplemental interest that TIAA would otherwise credit to the participant's Traditional Annuity account. This payout option continues until the earlier of the participant's death (at which time the balance in the account is paid to the participant's spouse or other beneficiary) or age 70 ½ at which time the participant may need to select another payment option to begin required minimum distributions.

TIAA also offers two "lifetime annuity" options: 1) the standard payment method, and 2) the graded payment method. Under the standard payment method, the participant receives monthly income for life based on the value of the Traditional Annuity accumulation, a 2.5 percent interest rate and an additional monthly amount that the TIAA Board may, at its sole discretion, declare in advance of the calendar year. No representation or guarantee is made concerning the payment of such amounts in subsequent years. In determining whether and to what extent additional amounts will be paid, TIAA has in the past considered the actual and projected earnings of TIAA, the anticipated mortality experience of participants, tax considerations, the overall economic outlook, the adequacy of TIAA's contingency reserves to enable TIAA to meet its contractual obligations under unanticipated adverse circumstances, and many other factors. You note that the level of additional amounts is sometimes varied depending upon when the original contributions were received by TIAA, when the payout annuity was issued, in addition to the participant's age and income option.

Under the graded payment method, a portion of the additional amounts is applied to the purchase of additional guaranteed income in the future. Under this method, any additional amount that is credited in a year is split. Part is paid in addition to the guaranteed income for a total monthly income based on a 4 percent interest rate. The amount above 4 percent, if any, is treated as if it were a contribution under the Traditional Annuity.

Under all of the distribution methods, the timing and terms of benefit payments are governed by the plan documents in addition to the TIAA contracts. For example, the Group Retirement Annuity provides: "Subject to your employer plan, the right to receive and exercise every benefit, option, right and privilege conferred by this certificate may not be immediately vested in you. In that case, your right to receive and exercise such benefits, options, rights and privileges will commence on your vesting date as determined in accordance with your employer plan."

You assert that the Traditional Annuity is an allocated contract because each contribution buys a guaranteed specific amount of benefits for participants based on the rate schedule in effect at the time paid. You take the position that the annual additional interest credited to a participant's Traditional Annuity account should not affect the Traditional Annuity's status as fully allocated because the additional interest is discretionary and only exists when declared and becomes allocated when credited to the participant's Traditional Annuity account. You also represent that the additional interest amounts are not subject to market fluctuation because they are declared in advance on an annual basis.

Section 29 C.F.R. § 2520.104-44(b)(2) provides that certain pension plans, the "fully guaranteed" benefits of which are provided "exclusively through allocated insurance contracts or policies," are provided a limited exemption from and alternative method of compliance with the requirement to report certain financial information on the annual report and to engage an independent qualified public accountant (IQPA) to examine the financial statements and schedules of the plan, and including with the annual report an IQPA's opinion concerning the plan's financial statements and schedules. Regulation section 2520.104-44(b)(2) provides, in pertinent part, that in order to qualify for this exemption the benefits of the pension benefit plan must be provided:

> [E]xclusively through *allocated* insurance contracts or policies which are issued by, and pursuant to the specific terms of such contracts or policies benefit payments are fully guaranteed by an insurance company or similar organization which is qualified to do business in any State, and the premiums for which are paid directly by the employer or employee organization from its general assets or partly from its general assets and partly from contributions by its employees or members (emphasis added). . . .

The 2008 Form 5500 Instructions further provide that plans that have "fully insured" contracts as described in 2520.104-44, as well as other assets, need not report the value of the allocated contracts on Part I of the Schedule H or I. According to these Instructions, a contract is considered to be allocated:

> …only if the insurance company or organization that issued the contract unconditionally guarantees, upon receipt of the required premium or consideration, to provide a retirement benefit of a specified amount. This amount must be provided to each participant without adjustment for fluctuations in the market value of the underlying assets of the company or organization, and each participant must have a legal right to such benefits, which is legally enforceable directly against the insurance company or organization. For example, deposit administration, immediate participation guarantee, and guaranteed investment contracts are NOT allocated contracts for Form 5500 purposes.[2]

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[2] Part I of Schedules H and I also states "Do not enter the value of that portion of an insurance contract which guarantees during this plan year, to pay a specific dollar benefit at a future date."

These 5500 Instructions reiterate the Department's longstanding view that "allocated" contracts include only those contracts under which an insurance company immediately assumes "fixed dollar obligations" and that the reporting exemption "'is premised on the fact that under such contracts the plan has effectively transferred the risk for the payment of benefits accrued to that date … to the insurer and, accordingly, limited reporting is appropriate.'" See Preamble to Revision of Annual Information Return/Report, 65 Fed. Reg. 5026-31 (February 2, 2000) (quoting Notice of Adoption of Revised Forms, 54 Fed. Reg. 8631, 8635 (March 1, 1989)).

The Department has rejected expanding the definition to include insurance products whose premiums are not immediately applied to purchase annuities but that purport to generally "guarantee benefits," or that "guarantee a fixed rate of return," or where group annuity contracts held by defined contribution plans credit or allocate each participant's interest in the contract to the participant's individual account in the plan, but the value of each participant's interest in the contract is adjusted for market value fluctuations. 65 Fed. Reg. 5030.

It is the Department's view that the Traditional Annuity is not a fully allocated contract within the meaning of 29 C.F.R. § 2520.104-44(b)(2). Upon receipt of each contribution or "premium," TIAA does not unconditionally guarantee to provide a retirement benefit of a certain amount or a "specific dollar benefit" without adjustment for fluctuations in the market value of TIAA's underlying assets.

The Traditional Annuity guarantees only a return of contributions and a minimum rate of interest during the accumulation phase. The Department has specifically rejected the view that a guaranteed rate of return is the same as a guarantee of a specific dollar benefit payable as retirement income. In light of the fact that the Traditional Annuity only carries a guaranteed minimum rate of return, and the value attributable to each of the Traditional Annuity contributions can increase when additional interest is declared, the Traditional Annuity does not provide a retirement benefit of a specified amount upon receipt of each contribution. Further, the actual rate of return for each contribution will vary from year to year at TIAA's discretion, because the additional interest is calculated in vintages based on the date and amount of the participant's original contribution, and is based, at least in part, on market value fluctuations on the assets held in TIAA's general account that support each vintage.[3] In this regard, you note that under the vintage structure, declared additional interest is based on projections of a number of factors, including investment performance, expenses, and the need to maintain adequate contingency reserves. While the Department appreciates that the value of each participant's additional interest is not adjusted for market value

[3] Whether TIAA has any discretion is irrelevant because § 2520.104-44(b)(2) requires that in order for a policy to be an "allocated" policy, all of the benefits provided must be guaranteed at the time of the original contribution–a standard which has not been met with respect to the contracts at issue.

fluctuations once such additional interest has been declared for a particular year, the arrangement nevertheless permits TIAA to reset the rate of additional interest each year based on myriad and variable factors, including past and projected investment performance. Therefore, the structure of the Traditional Annuity goes beyond the scope of what the Department intended to be a fully allocated contract within the meaning of 29 C.F.R. § 2520.104-44(b)(2).

The Traditional Annuity is not an allocated contract regardless of the method of benefit distribution because the contract does not guarantee a benefit of a specified amount on receipt of each contribution. A participant's amount of retirement benefit cannot be ascertained even if the participant chooses one of TIAA's "lifetime annuity" options and commences monthly payments. The participant is notified as to what the minimum monthly amount will be, based on his or her accumulation, but the actual amount of each monthly payment will vary because, as in the accumulation phase, TIAA retains the discretion to award additional supplements, basing the amount on factors similar to the factors used during the accumulation phase, including TIAA's investment experience and the time and amount of the original contributions into the participant's account.

Lastly, in addition to the benefits not being ascertainable from the TIAA contracts, the amount of the benefit may be affected by terms in the plan such as a vesting schedule. Both the TIAA Retirement Annuity Contract and the TIAA Group Retirement Annuity certificate provide that "the right to receive and exercise every benefit, option, right and privilege conferred by this contract [certificate] may not be immediately vested in you. In that case, your right to receive and exercise such benefits, options, rights and privileges will commence on your vesting date as determined in accordance with your employer plan." Any vesting requirement under the terms of a plan would be inconsistent with the definition of allocated contract. The contract would not guarantee a specified benefit from an insurance company because the amount of the benefit is subject to limitations in the plan. The vesting provision further demonstrates that a participant's Traditional Annuity account is not a definite amount at such time that a contribution is made.

For the reasons set forth above, the Department is unable to conclude that the Traditional Annuity, as described in your submission, constitutes an allocated insurance contract for purposes of the annual reporting requirements. We acknowledge that the issue of whether the TIAA Traditional Annuity could be treated as an allocated contract for annual reporting purposes under Title I of ERISA was not entirely free from doubt and that, in reliance on its legal interpretation of the annual reporting requirements, TIAA-CREF issued guidance to its client plan administrators that "TIAA Traditional Annuities are fully allocated contracts and as a result any accumulations to these annuities are not required to be reported as plan assets on Form 5500."[4] Under these circumstances, the Department does not believe that it would be appropriate to require the plan administrators of those plans that relied in good faith on TIAA-CREF's guidance to file amended and corrected annual returns/reports. Thus, the Department will not, as a matter of annual reporting enforcement policy, reject a plan's Form 5500 Annual Return/Report or require an amended Form 5500 Annual Return/Report for 2008 and prior plan years solely for failure to report the TIAA Traditional Annuity on Schedules H or I as an unallocated insurance contract, or for failure to treat the Traditional Annuity as an unallocated insurance contract for purposes of the Schedule A or an IQPA's audit of the plan. In addition, the Department also will not reject a Form 5500 for 2008 and prior plan years on the basis of a "qualified," "adverse," or "disclaimed" IQPA opinion if the reason for such a qualified or adverse opinion or disclaimer of opinion was because the Traditional Annuity was treated as an allocated insurance contract for purposes of the IQPA audit and the plan's financial statements. For plan years beginning on or after January 1, 2009, however, the Traditional Annuity cannot be treated as an allocated contract within the meaning of 29 C.F.R. § 2520.104-44(b)(2) and the Form 5500 Instructions. Further, this relief is limited to Form 5500 annual reporting requirements, and does not address any other provisions of Title I of ERISA or any other applicable state or federal law.

This letter constitutes an advisory opinion under ERISA Procedure 76-1. Accordingly, it is issued subject to the provisions of that procedure, including section 10 thereof relating to the effect of advisory opinions.

Sincerely,

Lisa M. Alexander
Chief, Division of Coverage, Reporting and Disclosure
Office of Regulations and Interpretations

[4] *See* chapter 4.3.1 of the TIAA-CREF Plan Sponsor Reporting and Audit Guide—2008 Plan Year Reporting for Qualified Plans, http://www.tiaa-cref.org/administrators/pdf/C43271.pdf