PENSION RIGHTS CENTER

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STATEMENT OF THE PENSION RIGHTS CENTER
BEFORE THE ERISA ADVISORY COUNCIL
ON MODEL NOTICES AND DISCLOSURES FOR PENSION RISK TRANSFERS

AUGUST 18, 2015

Good morning. I am Jane Smith, Policy Analyst for the Pension Rights Center. The Pension Rights Center is a nonprofit consumer organization that has been working since 1976 to protect and promote the retirement security of American workers, retirees, and their families. Thank you for inviting us to testify about disclosure needs of participants when faced with a risk transfer. We commend the Council for studying this issue of crucial importance to participants and their families. We particularly applaud the Issue Committee for drafting helpful sample risk-transfer notices for participants.

The Council is studying disclosure needs in two risk-transfer transactions. The first, and clearly the most difficult for participants, is the offer of a lump-sum payment instead of a guaranteed lifetime pension.[1] Recently the Internal Revenue Service issued a notice of intent to amend required minimum distribution regulations to prohibit employers from offering lump sums to retirees in pay status.[2] These amendments were effective July 9, 2015. As a result of the IRS amendments, some retirees will still receive lump-sum offers, but the bulk of such offers in the future will be made to deferred vested participants.[3]

The second risk-transfer transaction the Council is studying is the transfer of annuities from a pension plan to an insurance company.[4] Although this transaction does not involve a participant decision, any change in retirement income providers is a matter of great concern, especially the loss of protection by the Pension Benefit Guaranty Corporation.

My comments will focus mainly on the lump-sum offer. Comments about the draft notices are at the end of this statement.

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[1] See “Should you take your pension as a lump sum?” Pension Rights Center, July 16, 2012 (Updated March 2015). http://www.pensionrights.org/publications/fact-sheet/should-you-take-your-pension-lump-sum

[2] IRS Notice 2015-49.

[3] The amendments will not apply if an employer, prior to July 9, 2015, has adopted a lump sum risk-transfer program, received an IRS determination letter or private letter ruling, has informed selected participants of a lump sum offer, or entered an agreement with an employee representative authorizing a lump sum offer.

[4] See “What happens when a pension is transferred to an insurance company?” Pension Rights Center, August 15, 2012. http://www.pensionrights.org/publications/fact-sheet/what-happens-when-pension-transferred-insurance-company

LUMP SUM OFFERS

Participant concerns
The Pension Rights Center and the regional pension counseling projects we advise have been contacted by many participants who are confused and upset over lump-sum offers. Callers often ask what they should do. They don't know where to go for information and help. While the decision itself is "stressful, time-consuming, and worrisome," in the words of one caller to the Center, the materials participants receive often make matters worse. The materials do not clearly state or explain choices and may even imply that no type of pension benefit is safe. Another caller received materials that said the employer could terminate the plan, but the materials did not say that the benefits would not change. This person was left with the feeling that her pension could be eliminated after the lump-sum window had closed.

Information for an informed decision
The Council asks what useful information participants need to make an informed decision in a risk-transfer transaction. *Participants first need clear, accurate, and specific information about their benefit options.* At the Center we have seen lump-sum offers that do not include a specific mortality table or interest rate. Participants need to know how many years they and their spouses are expected to live under the plan's calculations so they can properly evaluate their options.

Specific information about benefit options should begin with a description in plain English of a lump sum equivalent and how it is calculated, including an example of a lump-sum conversion using a specific annuity amount, participant age, mortality assumption, and interest rates. Participants need to know the specific mortality table and interest rates to be used by the plan and the specific sources of each, not just references to the Internal Revenue Code. Deferred vested participants need a complete and accurate list of their benefit options at retirement, or early retirement. Deferred vested participants also need to know whether taking a lump sum before normal retirement age will reduce the amount of the lump sum offered, and if so, the interest rate that will be used to discount the value of their benefit. Information on benefit options should include the effects of each option on spousal benefits and rights. Participants should be informed of spousal consent requirements and advised how taking a lump sum can affect spousal rights if the lump sum is not rolled over into another employer-sponsored plan.

Participants need assurance that the pension benefits they have earned and are entitled to are guaranteed lifetime benefits. Some materials provided with lump sum offers imply that participants' benefits under the pension plan are at risk. This encourages participants to take a lump sum while the money is there. Participants need to know that their earned benefits cannot be reduced by an employer or plan amendment. Accurate information about the benefit guarantees provided by the Pension Benefit Guaranty Corporation (in the event the pension plan should become underfunded and terminate) is essential.

The notice accompanying a lump sum offer needs to include the precise risks of accepting a lump sum offer as well as a description of the circumstances that would make a lump sum offer *beneficial.* Participants facing a window period for a decision may not be able to afford to hire a financial advisor or have enough time to locate an expert before the deadline. Those participants able to afford and locate experts should be encouraged to seek out advisors who will put their interests first.

A lump-sum offer notice should inform participants and their spouses that in accepting a lump sum they also are accepting the investment and mortality risks associated with the lump sum. Their investment returns can be less than expected, they can lose principal in a severe market downturn, and they run the risk of outliving their income. There will be no survivor's benefits. In addition, they should be informed that a lump sum could be subject to creditors' claims and affect their eligibility for certain public benefits such as Medicaid. Participants should be informed about costs if they later decide to purchase a an annuity from a life insurance company, including fees, and the higher costs for women without the gender-neutral protections provided in employer-sponsored plans.

The tax implications of accepting a lump sum offer should be clearly explained, including the IRS required minimum distribution rules and the tax consequences of taking a lump-sum that is not rolled over into another tax qualified plan or IRA. Similarly, participants need to be informed that a pension paid out as a lump sum can be subject to claims of creditors.

A disclosure notice should remind participants and their spouses to check all personal information provided by the employer for accuracy, such as age, dates of employment, salary, and elected spousal benefit.

ANNUITY TRANSFERS

Participants facing the sale of their future pensions to an insurance company are concerned that their monthly benefit amounts or benefit options may not remain the same. They need assurance that these will not change. At the same time, they should be alerted to the fact that, depending on their state's laws, their annuities could be subject to the claims of creditors if they file for bankruptcy.[5] Participants should be given specific contact information for the employer and for the purchasing insurer, including specific names, titles, phone numbers, and department of the insurer, plus any identifying information for the group of annuities transferred.

[5] Last month, Connecticut enacted a law to protect annuities resulting from risk transfers from creditors. The law goes into effect October 1, 2015. A similar proposal has been introduced in New York State but has not been enacted. See "In Connecticut, Creditors Can't Touch De-Risked Pensions," Nick Thornton, *BenefitsPro*, July 14, 2015. http://www.benefitspro.com/2015/07/14/in-connecticut-creditors-cant-touch-de-risked-pens; "New Connecticut Law Protects Retirees' Annuities from Creditors," Jerry Geisel, *Business Insurance*, July 21, 2015. http://www.businessinsurance.com/article/20150721/NEWS03/150729958

Since participants will no longer have the protections of the Pension Benefit Guaranty Corporation, they need information on the state guaranty associations that will guarantee their benefits in the unlikely event that an insurer cannot pay the benefits. This information should include an explanation of how to determine which state guarantee limits will apply to their situation.

DELIVERY OF THE NOTICES

The Pension Rights Center has long supported the Department of Labor's rules on delivering disclosures to participants.[6] These rules basically require delivery by mail unless the participant has affirmatively consented to receive information electronically, or unless the participant is actively employed and using the employer's computer network as part of his or her daily duties. Mail delivery is particularly important where participants are being asked to make risk transfer decisions that can have such a significant impact on their future financial security.

COMMENTS ON DRAFT NOTICES

The Issue Committee on Disclosures for Pension Risk Transfers did an excellent job of drafting model notices. Reducing complex information to an understandable and helpful form for the average participant is extremely difficult. The information in the notices will be especially useful to participants and their families because the information will be in one place and not scattered among 40 or 50 pages of confusing text. The comparison chart at the end of the lump- sum notice will be particularly helpful to participants. Providing 90 days for participants and their families to make a decision will give them time to thoroughly explore their options. We encourage the Department of Labor to require employers to include these notices when finalized in the front of any risk transfer materials sent to participants and beneficiaries.

<u>Comments on the lump-sum draft notice</u>

1. Based on the concerns of callers to the Pension Rights Center and the regional pension counseling projects, there should be additional emphasis at the beginning of the notice on the lifetime income guarantee provided by a pension plan for participants and their surviving spouses. Also the notice could clearly state that the participant's pension benefit amount cannot be changed by the employer in the future if the lump sum offer is rejected. Probably an additional sentence or two under Section A(1) would be sufficient. The benefit guarantee often is not obvious to unsophisticated participants.
2. Lump-sum rollovers are a complicated subject. ERISA plans must agree to accept rollovers. There are differences between Roth and traditional IRAs. The discussion of rollovers in the notice could benefit from a sentence or two on items to consider when deciding on a rollover. Rollovers sound easy, but there can be significant restrictions depending on a participant's age and the type of rollover.

[6] 29 CFR 2520.104b-1.

3. A short question-and-answer on spousal benefits and rights would be helpful to couples making a risk-transfer decision. This could include the rights of spouses to survivor benefits including, in the case of a deferred vested participant, the chance for couples to provide for a surviving spouse. It should also include the spousal consent requirement for accepting a lump sum offer.
4. The disclosure of benefit options under the plan is a crucial part of the notice. It would be helpful if Question B(1) could include a description of the level of detail required in disclosing plan benefit options. For example, the question could mention effects on spousal benefits and ages of eligibility for early retirement benefits. Information on benefit options should be sufficiently specific so participants can clearly see their options.
5. If the lump-sum value will be reduced for participants who have not reached normal retirement age, this should be explained. This is particularly important for deferred vested participants. The reduction factor should be specified (e.g., a 6 percent reduction for each year under age 65.)
6. The draft notice rightly requires specific mortality tables and interest rates. It could be helpful to know the source of the tables and interest rates, such as the plan or IRS.
7. An additional sentence about terminating pension plans could be added to Question B(4) to assure participants that a standard termination of a plan will not eliminate or reduce their benefits.
8. It would help participants to have a brief reminder at the end of the notice to verify all personal information provided by the employer, including information on a spouse.

Comments on the annuity-transfer notice

1. The notice should include specific contact information for the insurance company, including name, title, e-mail address, and phone number of person to contact; the appropriate division or department of the insurance company; the address of the insurer; and the address of the contact office of the insurer. Insurance companies are huge and very hard to navigate.
2. It is not clear from the notice that when an insurance company is not licensed in the state where the individual lives, the guarantee limits of the state where the insurance company is incorporated apply.

The Pension Rights Center appreciates this opportunity to express our views on the information that plan participants need to make informed decisions about pension-risk transfer offers.