



DOL Guidance on Lifetime Income Illustrations: Coloring Within the Lines | Fiduciary Focus Series

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The Setting Every Community Up for Retirement Enhancement (SECURE) Act of 2019 included several lifetime income-focused provisions for defined contribution plans. These provisions are undoubtedly intended to increase retirement savings and the use of lifetime income annuity products by individual account defined contribution plans and their participants and beneficiaries, and thereby address some of the challenges left in the wake of disappearing defined benefit plans, such as retirees and their spouses outliving their retirement savings.

On August 18, 2020, the Department of Labor (DOL) announced an interim final rule (“Interim Rule”) setting forth guidance under one of these provisions.^[1] The SECURE Act Section 203 amends Section 105 of the Employee Retirement Income Security Act (ERISA) and requires plan administrators of individual account plans, such as 401(k) plans and most 403(b) plans, to provide participants and beneficiaries annual illustrations regarding the lifetime income streams that their plan account balance represents as a part of their participant benefit statements. This lifetime income stream illustration required by Section 203 must provide the monthly amounts that both a single life annuity and a qualified joint and survivor annuity would pay based upon the participant or beneficiary’s account and subject to certain assumptions. Because providing this type of inexact illustration is inherently risky, Section 203, in turn, provides a “safe harbor” from liability to plan sponsors or fiduciaries who comply with the requirements of the lifetime income disclosure and use the model language that the DOL is required to develop. Section 203 required the DOL to issue guidance on the assumptions that should be used in the lifetime income illustrations and to provide a model disclosure within a year. The Interim Rule represents the DOL’s satisfaction of this requirement.

Background

The DOL has been considering what lifetime income disclosures might look like for more than a decade. In 2010, the DOL issued a request for information (the “RFI”) [\[2\]](#) which, in part, questioned whether participant benefit statements should include lifetime income illustrations and, if so, what those illustrations might look like and what assumptions should be used. That same year, DOL held a public hearing on lifetime income options, to consider certain issues raised by those responding to the RFI, including the methods and assumptions for lifetime income stream illustrations.

Three years later, the DOL published an advance notice of proposed rulemaking (ANPRM) providing that the DOL was considering requiring four lifetime income stream illustrations as a part of participant benefit statements: a single life annuity and a qualified joint and 50% survivor annuity, each with two separate calculations (one based upon current account balance and the other based upon a projected account balance through normal retirement age using assumed future contributions and investment returns). The proposal included certain assumptions for projecting accounts forward through normal retirement and converting an account into a lifetime income stream. While the DOL received significant comments on the ANPRM in response to its request for comments, it took no further action until it unveiled the Interim Rule in response to SECURE Act Section 203’s requirements.

Interim Rule

The Interim Rule requires a plan administrator of an individual account plan to provide at least annually as a part of the pension benefit statements a lifetime income disclosure that is easy to understand and that includes the following information:

- the beginning and ending date of the statement period,
- the account balance (including the outstanding balance of any plan loan unless the loan is in default and excluding the value of any deferred income annuity held by the account) as of the last day of the statement period (“Account Balance”) and
- the monthly amount that the Account Balance would pay in the form of both a life annuity (equal payments over the

participant's lifetime) and a qualified joint and 100% survivor annuity (equal payments over the joint lives of the participant and a spouse).

To convert a participant's Account Balance into illustrative monthly amounts, such amounts must be calculated as if the lifetime income stream payments began on the last day of the statement period and as if the participant is 67 on such date unless the participant is older than age 67, in which case his or her actual age will be used. The calculation assumes that the spouse is the same age as the participant. The Interim Rule also prescribes the interest rate and mortality assumptions to be used in the calculation. The conversion does not factor in any additional "load" an insurer would charge in providing such an annuity.

The Interim Rule offers an example of what this illustration might look like:

Account Balance as of [DATE]	Monthly Payment at 67 (Single Life Annuity)	Monthly Payment at 67 (Qualified Joint and 100% Survivor Annuity)
\$125,000	\$645/month for life of participant	\$533/month for life of participant \$533/month for life of participant's surviving spouse

The Interim Rule also provides that a detailed explanation of the illustration is required to accompany the illustration, specifies the content that the explanation must cover and provides model language that can be used to satisfy the content requirement. This is appropriate because the lifetime income stream illustration without an explanation of the assumptions involved could be misleading.

The explanation must include a description of a single life and a qualified joint and 100% survivor annuity, explain that other survivor percentages are available and address the impact of choosing a lower survivor percentage. The assumptions used in preparing the illustrations must be explained, and the model language includes an explanation of how facts different from the assumptions used might impact the illustration. For example, the Interim Rule requires an

explanation of when the income stream was assumed to begin, i.e., the last day of the statement period, and the age assumption is required. In addition to explaining the age assumption, the model language paired with this content requirement explains how beginning payments at a younger age or an older age would impact the monthly amount.

The explanation must emphasize that (i) the illustrations are only illustrations and are not a guarantee, (ii) the actual monthly income that a participant can purchase with his or her account balance will depend upon a number of factors that may vary substantially from the illustration amount and (iii) such monthly amounts, in an inflationary environment, will provide declining purchasing power.

If a plan offers in-plan annuities, the plan administrator may elect to use the plan's annuity contract terms in preparing the illustrations instead of the assumptions discussed above, except that DOL's assumptions related to a participant's commencement date and age, his or her marital status and his or her spouse's age must continue to be used. If the plan administrator makes this election, the accompanying explanation must refer to the plan's contract provision, and the model language is different. For example, the explanation regarding the interest and mortality provisions used in converting an account balance to a monthly amount would refer to the contract terms in lieu of those assumptions prescribed by DOL.

If a participant holds a deferred income annuity (DIA) as a part of his or her account, different rules apply to that portion of the account, and model language is not provided.^[3] This is because a disclosure related to a DIA will provide the actual (as opposed to illustrated or estimated) payments that will be paid to the participant upon a future date.

Limitation on Liability

If the lifetime income disclosure complies with the requirements of the Interim Rule and uses the model language (or language substantially similar in all material respects), the tradeoff is that plan fiduciaries and sponsors will generally be shielded from liability solely as a result of providing the disclosure. Given the safe harbor protection, it seems advisable to cleave as closely as possible to

the model language. Disclosures related to a DIA, however, are not covered by the safe harbor.

Comments Requested and Effective Date

The DOL requested comments on almost all aspects of the Interim Rule by November 17, 2020. After consideration of comments, the DOL intends to replace the Interim Rule with a final rule sufficiently in advance of the effective date for the Interim Rule, which is September 18, 2021.

Considerations

It is interesting to think about the requirements of SECURE Act Section 203 and the Interim Rule in the context of DOL's proposed approach in ANPRM, where the lifetime income illustrations based upon both a current account balance and a *projected account balance through normal retirement age* would have been provided. To quote Joni Mitchell "well, something's lost, but something's gained."

On the one hand, projecting an account balance through normal retirement age based on assumptions regarding future contributions and investment returns seems incredibly speculative, particularly for younger people. On the other hand, providing a lifetime income illustration to a younger person based on their current account balance and assuming that they are age 67 at the time they receive the disclosure is a very challenging prospect and may not provide much useful information. Providing lifetime income illustrations based upon both a current and a projected account balance may collectively provide more useful information, particularly for younger participants. As a result, some commenters are likely to press the DOL for changes that include a lifetime income stream based upon a projected account balance. It will be interesting to see what adjustments to the Interim Rule that the DOL may make in its final rule.

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[\[1\]](#) The Interim Rule was published in the Federal Register on September 18, 2020.

[\[2\]](#) The RFI was issued in conjunction with the Internal Revenue Service and the Department of Treasury.

[\[3\]](#) Remember that the value of a DIA is excluded from the Account Balance used in the lifetime income illustrations discussed above.

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